

2018 Citywide Risk Assessment Information for Audit Committee

Description of Risk

Fiscal stress-risk that decreased City revenues, natural disasters, or emergency repairs to infrastructure may overwhelm the City's general fund.

Enterprise fund-emergency contingencies

Risk is that enterprise funds (e.g. Water, Water Reclamation, Sanitary Landfill) would have insufficient funds to pay for emergency repairs. Enterprise funds are intended to self-supporting and general fund revenues are not allowed by policy to be used for enterprise fund expenses.

Investment of idle funds-custodial credit risk (governmental and business type funds)

Risk is that in the event of the failure of a depository financial institution, the City will not be able to recover deposits or investments that are in possession of an outside party.

How Mitigated or Controlled

City Council mandated policy is that the City maintains a minimum unrestricted cash balance at the end of each month equal to 11% of the general fund budget for that fiscal year. At year end, there must be a general fund unassigned fund balance equal to 25% or greater of general fund expenditures.

Healthy operating reserves are maintained, by policy, in the various enterprise funds. 90 days or more of operating expenses are maintained in enterprise funds (with exception of the landfill fund which maintains 180 days). This reserve is the fiscal year-end fund balance.

City deposits in excess of depository insurance must be 100% collateralized.

Collateral is required to be segregated by each depository and collateral may not be held in any safe deposit vault owned or controlled either directly or indirectly by the pledging financial institution

Has this area been audited?

Internal Audit has verified this through several financial condition analysis reports.

Internal Audit audited the Water Fund in 2012, Water Reclamation in 2009, and the Landfill in 2009. Public Works has hired consultants to perform studies to develop recommendations for utility rate increases to build up reserves for future operating and capital expenses in utility funds.

Internal Audit audited the City's investment policies and the associated control activities in 2013.

Description of Risk

Investment of idle funds-credit risk

(governmental and business type funds)

Risk is that issuer will not fulfill its obligations.

How Mitigated or Controlled

State statute and City policy limit the type of investments allowed to reduce the amount of risk in the City's portfolio.

City's pooled cash investment policy limits the City's pooled cash portfolio to hold no more than 20 percent of the total pool investments in a single financial institution.

Has this area been audited?

Internal Audit audited the City's investment policies and the associated control activities in 2013.

Investment of idle funds-interest rate risk

(governmental and business type funds)

Risk is that changes in interest rates will adversely affect the fair value of an investment.

City's pooled cash investment policy limits pooled cash investments to a maturity of five years or less to ensure adequate liquidity and minimized the impact of interest rate changes.

(See above.)

Investment of fiduciary funds-custodial credit risk

(pension funds)

Risk is that in the event of the failure of a depository financial institution, the City will not be able to recover deposits or investments that are in possession of an outside party.

Pension fund trustees have an investment policy outlining responsibilities, prohibitions, diversification and performance measurement standards.

The cash deposits of the pension funds held by the City are subject to the same requirements as governmental and business-type funds.

Internal Audit performed an audit of the City Pension in 2009.

Investment of fiduciary funds-credit risk

(pension funds)

Risk is that an issuer of an investment will not fulfill its obligations.

In addition to a diversified index fund, the City uses one separately managed account for the management of fixed income securities. Policy requires that all individual securities separately managed must be rated "A" or better at the time of purchase.

(See above.)

Description of Risk

Investment of fiduciary funds-concentration of credit risk

(pension funds)

Risk is the magnitude of loss because of investment in a single issuer.

Pension funds annual required contributions

Risk is that the City's required contribution will consume greater and greater percentage of the City's operating budget with less resources available provide City services and maintain infrastructure.

Solid waste landfill closure costs

City owns and operates a regional landfill site west of the city limits. State and federal require the City to close the landfill once capacity is reached and to monitor/maintain the site for 30 years after that. Risk is that funds will not be available to close and monitor the site.

How Mitigated or Controlled

City policy prevents the separately managed fixed income and equity growth account from holding more than 5 percent of portfolio in a single issue.

Pension system changes approved in 2013 and beginning in 2014:

- Current employees contribute an increased share to the pension funds (went from 3% to 5%).
- New employees will be members of the SD State Retirement System. City's required contribution is a fixed percentage each year.
- Retirees are no longer eligible to remain on the City's health insurance plan.

Local City ordinance (as well as State and Federal law) mandate that the City establish a fund to accumulate financial assets needed for the payment of closure costs and post closure costs. The City accumulates these funds in the Sanitary Landfill enterprise fund as restricted cash funds. In 2017, these funds were approximately \$10 million. The future obligation is recognized as an associated liability for the same amount.

Has this area been audited?

Internal Audit performed an audit of the City Pension in 2009.

(See above.)

Internal Audit did an audit of the Sanitary Landfill in 2010. Eide Bailly, the City's external audit firm, audits the change in liability as part of the audit of the City's financial statements.

Description of Risk

Business interruption to City departments

Risk is that vital business functions could be interrupted by fire or flooding at City Hall or a pandemic where City employees are ill and cannot come to work. Many other scenarios could result in serious business interruption.

Lawsuits/torts-claims against the City

These could result from "errors and omissions" of public officials, damage to property that was the fault of City employees, etc.

Risk is that the City could be held liable by a court for damages to a plaintiff resulting in a financial loss to the City.

Developers fail to fulfill their responsibility to complete roads in new developments.

Risk is that the City will need to expend public funds to complete roads.

How Mitigated or Controlled

A detailed business continuity/disaster recovery plan was developed and completed by City departments in 2013 and coordinated by the City Emergency Manager. Planning identified core business functions, alternate sites, plans of action etc.

The plan is tested periodically through "table top" exercises.

City is a member of the South Dakota Public Assurance Alliance-essentially an insurance fund for South Dakota local governments. This provides protection for City liabilities resulting from lawsuits and similar liabilities. City Attorney's office provides legal counsel and arranges for outside legal specialists as necessary.

City Attorney's office and City Risk Manager regularly review areas of risk in the City (potential areas where the City might be held liable) and recommend avoiding the risk, transferring the risk, or controlling the risk.

In 2014, City began requiring developers to sign a Construction Agreement which includes a bond which the City holds so that the City has the financial resources available to complete the job (paving of roads) should this become necessary. The developer pays the cost of obtaining this bond.

Has this area been audited?

No. This could be a future audit area.

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Description of Risk

Aging infrastructure

Risk is that streets, water lines, sewer lines, and other infrastructure is deteriorating faster than it can be maintained and repaired. Result would be expensive, emergency repairs and inconvenience to the public.

How Mitigated or Controlled

Following activities address this risk:

- Massive investment in infrastructure through the City's Capital Improvement Program (CIP).
- Systematic and continual visual inspection of water and sewer lines using a dedicated crew with video cameras.
- Systematic relining of water and sewer lines.
- Micro paving of streets to better ensure they reach their expected life.
- Identification of problem areas for buried utility lines (corrosive soil).
- Use of laser technology to precisely and objectively evaluate the condition of City streets.
- Use of consultants to identify best strategies for maintaining infrastructure (maximizing use of available resources).
- Dynamic modeling software is used to better identify remedial action to correct neighborhood drainage issues.

Has this area been audited?

Yes. CIP audit performed in 2010. Water, Water Reclamation, Storm Drainage audits all performed in past ten years.

Construction contract risks

Multiple risks including the following:

- Project expenditures exceeding budget
- Non-compliance with State bid laws
- Contractor having difficulty maintaining work schedule
- Contractor not building according to specs
- Contractor failing financially (City on the "hook")
- Materials/construction failing after a short time (less than a year)

Multiple mitigation strategies address these risks:

- On site supervision by consulting engineers and project manager (City employee)
- Monitoring by Finance including Purchasing Division
- City's General Conditions have various insurance requirements and warranties
- Weekly meetings between Project Manager, Contractor, and architect

Internal Audit has performed multiple audits in this area:

- 2013 Downtown River Greenway
- 2014 Construction Administration
- 2016 Construction Manager at Risk

Compliance risk-grant funding

The City receives many State and Federal grants to fund various services in Police, Health, and Affordable Housing, Public Works, and Transit. Risk is that the City does not comply with grant requirements. This could result in a loss of funding and other penalties.

- Employees specifically trained and tasked with grant compliance in departments receiving grants.
- Finance employees provide assistance.

Eide Bailly, as part of the annual external audit, is required to test a certain percentage of the grants received by the City. This is a requirement of the Single Audit Act of 1984. The auditors determine if the City is in compliance with regulations and laws specific to the federal funding stream.

Description of Risk

Information technology risks/cyber threats

Risks are that server(s) could crash, malicious software could infect our IT infrastructure, hackers could successfully penetrate our system, there could be a loss of power to the City's data center, or there could be a fire in the data center etc.

How Mitigated or Controlled

There are numerous control activities related to this as follows:

- Background checks of the City's IT employees
- Fire suppression equipment appropriate to the data center
- Emergency power generator system (EPS)
- Uninterruptible power supply (UPS)
- Firewalls, anti-spam software, anti-virus software.
- Training and education to City employees for awareness of cyber threats (reminders not to open suspicious attachments to email).
- Use of leading practices for backup storage of data.
- Continual monitoring by IT personnel.
- Segregation of critical duties.
- Regular upgrades of IT infrastructure.

Has this area been audited?

Internal Audit reviewed general and application controls in 2009 and 2016. An IT expert from Eide Bailly reviewed reviewed controls in 2010 as part of the external audit.

An external consultant performed a security review in February 2016 of the City's IT systems and protocols.

City uses the assistance of the Department of Homeland Security to identify and correct specific vulnerabilities that could be potentially exploited by terrorists. Example would the SCADA system that municipalities use to control their water purification and distribution system.

Description of Risk

Injuries to employees

City employees in certain departments must enter confined spaces, fight fires, use force to make arrests, use power equipment, and perform other potentially dangerous activities in their employment. Risk is death or injury to employees and financial loss to the City. Risks also come from potential violence to City employees from the public.

How Mitigated or Controlled

- City maintains a Risk Management division to develop and maintain a work place safety program in conjunction with department-specific safety activities.
- City maintains a self-funded Worker's Compensation fund to pay claims.
- Investment in safety equipment for employees.
- City facilities are systematically inspected for safety and security hazards.
- In 2018, City created a new full-time position, Safety Coordinator. This position was filled in October, 2018 and is located in Human Resources. Risk Management will be more involved in insurance claims and other related duties including security of City buildings some of the work place safety responsibility shifted to the Safety Coordinator.
- Department supervisors are tasked with monitoring and enforcing department specific safety protocols.
- Training for City employees in work place safety issues specific to their department.
- Increased security presence in City Hall and Carnegie Town Hall.
- City maintains a \$1,000,000 reinsurance coverage on workers' compensation claims to limit City's financial exposure.

Has this area been audited?

Internal Audit performed an audit of the Workers' Compensation fund in 2010. A consultant performed a study of the City's work place program and activities in 2015. Numerous recommendations were made as a result of that study. Same consultant is now assisting the City in implementation of those recommendations.

Description of Risk

Sioux Falls Fire Rescue response times

Risk is that with an ever increasing city population and expansion of city limits through annexations, Fire Rescue will not be able to maintain response time goals. Performance goal is travel in 5 minutes and 12 seconds or less for 90 percent of calls. If average travel times begin to increase, the potential for injury, loss of life and greater damage to property goes up. Citizens have an expectation (rightly) for prompt response to emergency calls for service.

Transit system requiring increasing percentage of City's funds for operating expenses

Risk is that the growth in transit expenses will be unsustainable. City currently heavily subsidizes operating expenses of the transit system. Fares only cover a small percentage of the actual costs of operating the system (Sioux Area Metro).

How Mitigated or Controlled

- Formal and systematic risk assessment and analysis by SF Fire Rescue.
- Detailed tracking and analysis for response times.
- Creation of an Integrated Response Management Plan.
- Planning and construction of new fire stations through the City Capital Improvement Program (CIP). New stations built in past 12 years include Fire Station 10 (2006), Fire Station 11 (2015), Fire Station 12 (2019-design, 2020-construction)

- Transit Task Force was formed to meet, study, and issue recommendations to the City Council (2014). Recommendations included increasing fares and adjusting routes, particularly paratransit.
- The Director of the newly created Innovation and Technology department is heading up a task force of City managers to take a fresh look at the issues of the Transit system. They will be working with team members from the Bloomberg Harvard City Leadership Initiative to brainstorm and analyze possible solutions and different approaches to Transit system design and management.

Has this area been audited?

No. However, Sioux Falls Fire Rescue is one of a handful of Fire Departments in the world (less than 200) that have gone through the process of accreditation through the Commission for Fire Accreditation International. They received initial accreditation in 2003 and were reaccredited in 2008 and 2013. A peer review team reviews 244 performance indicators and 77 core competencies. A site visit was performed in 2018. Final reaccreditation should occur in March 2019.

Internal Audit performed audits in 2011 and 2015. (Note: rates were adjusted up by the City Council in 2016 based upon recommendations from the Transit Task Force and Internal Audit.

Description of Risk

Misappropriation of assets-fraud

Risk is that an employee and/or vendor steal from the City through various fraud schemes resulting in financial loss to the City and reputational damage to the City and its employees.

How Mitigated or Controlled

Control activities include:

- Segregation of duties.
- Monitoring by management of revenue, expenses, purchasing card purchases.
- Limiting access to City's accounting system
- Fraud awareness training provided periodically to City employees especially mid management and Finance employees.
- Employee dishonesty insurance maintained to help recover losses if they would occur.
- Internal Audit performing audits in higher risk areas such as cash handling and purchasing cards.
- Fraud, waste, and abuse hotline maintained for employees to report anonymously.
- Various antifraud techniques used by Internal Audit such as Benford Law analysis of Accounts Payable.
- Background checks of City job applicants to include drug screenings and credit checks depending upon position applied for.
- Tagging of City's noncapital inventory and fixed assets and annual verification of these assets.

Has this area been audited?

Yes. Internal Audit performs a citywide fraud risk assessment every five years. We consider this risk when doing the audit planning for each individual audit.