

**CITY OF BEAUMONT**  
**BEAUMONT TRANSIT SYSTEM**  
**FINANCIAL STATEMENTS**

For the Fiscal Years Ended June 30, 2016 and June 30, 2015

**City of Beaumont  
Beaumont Transit System  
Table of Contents**

**TABLE OF CONTENTS**

	<b>Page</b>
<b>I. Independent Auditor's Report</b>	1 - 2
<b>II. Management's Discussion and Analysis</b>	3 - 7
<b>III. Basic Financial Statements</b>	
Statement of Net Position	8
Statement of Revenues, Expenses and Changes in Net Position	9
Statement of Cash Flows	10
Notes to Financial Statements	11 - 21
<b>IV. Independent Auditor's Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of the Financial Statements in Accordance with <i>Government Auditing Standards</i></b>	22 - 30





## **BASIC FINANCIAL STATEMENTS**

**City of Beaumont Transit System**  
**Notes to Financial Statements**  
June 30, 2016 and 2015

**1) REPORTING ENTITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Reporting Entity**

The Beaumont Transit System's (System) financial statements are intended to present the financial position and results of operations of only those transactions attributable to the System, operated by the City of Beaumont, California (City). Within the operations of the System, the City operates both Fixed Route and Dial-A-Ride transit systems. The financial statements of the System are included in the basic financial statements of the City.

As an operator of a public transportation system, the City is eligible for Transportation Development Act Public Utilities Code Section 99260 funds. These funds were allocated by the Riverside County Transportation Commission (RCTC) to supplement the City's existing transit operations.

The accounting policies of the System are in conformity with accounting principles generally accepted in the United States of America applicable to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing accounting and financial reporting principles.

**Fund Accounting**

The accounts of the City are organized on the basis of funds, which are considered to be separate accounting entities. The operations of the System are accounted for in separate sets of self-balancing accounts that comprise the System's assets, liabilities, net position, revenues, and expenses. Government resources are allocated to and for individual funds based on the purposes for which they are spent and means by which spending activities are controlled. The fund represented in the System's financial statements is a proprietary fund.

**Basis of Accounting and Measurement Focus**

As a governmental agency, the System is subject to accounting and reporting standards established by the Governmental Accounting Standards Board (GASB). The System uses the accrual basis of accounting. The financial activities of the System are accounted for using the economic resources measurement focus. Under this method, all assets and liabilities associated with its operations are included on the statement of net position; revenues are recorded when earned and expenses are recorded when liabilities are incurred.

The System reports its transit operations as a single enterprise fund.

**Cash and Cash Equivalents**

For purposes of the statement of cash flows, the System considers all short-term debt securities purchased with an original maturity of three months or less to be cash equivalents.

**City of Beaumont Transit System**  
**Notes to Financial Statements**  
June 30, 2016 and 2015

**1) REPORTING ENTITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Revenue and Expenses**

Revenues and expenses are distinguished between operating and nonoperating items. Operating revenues generally result from providing services in connection with the System's principal ongoing operations. The principal operating revenues of the System are fees in connection with providing transit services to customers.

Operating expenses include the costs of providing transit services, administrative expenses, and depreciation on capital assets. All revenue and expenses not meeting these definitions are reported as nonoperating revenues and expenses.

**Use of Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

**Grants**

Grant revenues and receivables are recorded when earned on the grants that have been approved and funded by the grantor. Grant sources include, State Transit Assistance (STA), Proposition 1B and Local Transportation Fund (LTF). Transportation Development Act (TDA) includes LTF and STA.

**Capital Assets**

All capital assets, consisting primarily of vehicles and equipment, are stated at cost. Depreciation is computed using the straight-line method over the estimated useful lives of the assets, which range from three to five years. Capital assets include contributed assets. Donated capital assets received prior to the implementation of GASB 72 were recorded at fair value on the date of donation. Donated capital assets received subsequent to the implementation of GASB 72 are recorded at acquisition value as of the date received.

**Reclassifications**

Certain amounts in the June 30, 2015 financial statements have been reclassified to conform with the June 30, 2016 financial statement presentation.

**Net Position**

The difference between assets and liabilities is reported as net position. Net position is classified as either net investment in capital assets, restricted, or unrestricted.

**City of Beaumont Transit System**  
**Notes to Financial Statements**  
June 30, 2016 and 2015

**1) REPORTING ENTITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued**

Net investment in capital assets, consists of capital assets, net of accumulated depreciation and reduced by the outstanding principal of related debt. Restricted net position reflects the carrying value of assets less related liabilities that have external constraints placed on them by creditors, grantors, contributors, laws, or regulations of other governments, or through constitutional provisions, or enabling legislation. Unrestricted net position represents the remaining fund equity balance.

**Net Position Flow Assumption**

Sometimes the System will fund outlays for a particular purpose from both restricted (e.g. restricted bond or grant proceeds) and unrestricted resources. In order to calculate the amounts to report as restricted – net position and unrestricted – net position in the statement of net position, a flow assumption must be made about the order in which the resources are considered to be applied.

It is the System’s policy to consider restricted net position to have been depleted before unrestricted net position.

**Deferred Outflows/Inflows of Resources**

In addition to assets, the statement of financial position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, *deferred outflows of resources*, represents consumption of net position that applies to future period(s) and so will not be recognized as an outflow of resources (expense) until then. The System reports deferred outflows as a result of the System’s implementation of GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*, which qualify for reporting in this category.

In addition to liabilities, the statement of financial position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, *deferred inflows of resources*, represents an acquisition of net position that applies to a future period(s) and so will not be recognized as an inflow of resources (revenue) until that time. The System reports deferred inflows as a result of the System’s implementation of GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*, which qualify for reporting in this category.

**Pension Plan**

The City participates in the Public Employees’ Retirement System of the State of California covering all of its permanent employees. The excess, if any, of the actuarially computed value of vested benefits over the amounts available in the pension fund would be a liability of the City as a whole, not of the System. Information regarding the plan description, funding status and progress, actuarially determined contribution requirements and contributions made, and trend information may be found in the City’s basic financial statements.

**City of Beaumont Transit System**  
**Notes to Financial Statements**  
June 30, 2016 and 2015

**2) CASH AND INVESTMENTS**

The City has pooled its cash and investments in order to achieve a higher return on investments while facilitating management of cash. The cash balance in excess of current requirements is invested in various interest-bearing accounts and other investments for varying terms. The System's cash is deposited in the City's internal investment pool, which is reported at fair value. Interest income is allocated on the basis of average cash balances. Investment policies and associated risk factors applicable to the System are those of the City and are included in the City's basic financial statements.

See the City of Beaumont's basic financial statements for more information on pooled cash and investments.

Cash and investments as of June 30, 2016 and June 30, 2015 are classified in the accompanying financial statements as follows:

	2016	2015
Statement of Net Position:		
Pooled Cash with the City of Beaumont	\$ 409,583	\$ 589,408
Restricted Cash and Investments	265,140	725,713
Total Cash and Investments	674,723	1,315,121

Cash and investments at June 30, 2016 and June 30, 2015 of \$265,140 and \$725,713 respectively, are restricted for capital improvements.

**City of Beaumont Transit System**  
**Notes to Financial Statements**  
June 30, 2016 and 2015

**3) CAPITAL ASSETS**

Capital assets of the System for fiscal year ended June 30, 2016 are presented as follows:

	Beginning Balance	Increases	Decreases	Ending Balance
Capital Assets, Not Being Depreciated:				
Construction in Progress	\$ -	\$ 2,715	\$ -	\$ 2,715
Total Capital Assets, Not Being Depreciated	-	2,715	-	2,715
Capital Assets, Being Depreciated:				
Vehicles	2,041,986	1,432,305	\$ -	3,474,291
Building	477,782	46,553	-	524,335
Equipment	477,625	-	-	477,625
Total Capital Assets, Being Depreciated	2,997,393	1,478,858	-	4,476,251
Less Accumulated Depreciation:				
Vehicles	(1,690,114)	(274,809)	-	(1,964,923)
Building	(216,750)	(36,291)	-	(253,041)
Equipment	(351,035)	(57,946)	-	(408,981)
Total Accumulated Depreciation	(2,257,899)	(369,046)	-	(2,626,945)
Total Capital Assets Being Depreciated, Net	739,494	1,109,812	-	1,849,306
Capital Assets, Net	\$ 739,494	\$ 1,112,527	\$ -	\$ 1,852,021

**City of Beaumont Transit System**  
**Notes to Financial Statements**  
June 30, 2016 and 2015

**3) CAPITAL ASSETS - Continued**

Capital assets of the System for fiscal year ended June 30, 2015 are presented as follows:

	Beginning Balance	Increases	Decreases	Ending Balance
Capital Assets, Being Depreciated:				
Vehicles	\$ 2,041,986	\$ -	\$ -	\$ 2,041,986
Building	477,782	-	-	477,782
Equipment	467,180	10,445	-	477,625
<b>Total Capital Assets, Being Depreciated</b>	<b>2,986,948</b>	<b>10,445</b>	<b>-</b>	<b>2,997,393</b>
Less Accumulated Depreciation:				
Vehicles	(1,428,903)	(261,211)	-	(1,690,114)
Building	(174,180)	(42,570)	-	(216,750)
Equipment	(279,459)	(71,576)	-	(351,035)
<b>Total Accumulated Depreciation</b>	<b>(1,882,542)</b>	<b>(375,357)</b>	<b>-</b>	<b>(2,257,899)</b>
<b>Total Capital Assets Being Depreciated, Net</b>	<b>1,104,406</b>	<b>(364,912)</b>	<b>-</b>	<b>739,494</b>
<b>Capital Assets, Net</b>	<b>\$ 1,104,406</b>	<b>\$ (364,912)</b>	<b>\$ -</b>	<b>\$ 739,494</b>

Changes in the capital assets by funding source for the fiscal years ended June 30, 2016 and 2015 were as follows:

	STA Funds	LTF Funds	Measure A	Operator Funds	Prop 1B	Total
June 30, 2014	\$ 1,943,346	\$ 528,474	\$ 95,000	\$ 88,026	\$ 332,102	\$ 2,986,948
Additions	10,445					10,445
Deletions						-
June 30, 2015	1,953,791	528,474	95,000	88,026	332,102	2,997,393
Additions	1,481,573					1,481,573
Deletions						-
June 30, 2016	<u>\$ 3,435,364</u>	<u>\$ 528,474</u>	<u>\$ 95,000</u>	<u>\$ 88,026</u>	<u>\$ 332,102</u>	<u>\$ 4,478,966</u>

**City of Beaumont Transit System**  
**Notes to Financial Statements**  
June 30, 2016 and 2015

**4) UNEARNED REVENUES**

Unearned revenue represents excess operating and excess capital assistance.

Changes in unearned revenues for the fiscal years ended June 30, 2016 and 2015 for operating assistance were as follows:

	<u>LTF</u>	<u>LCTOP</u>
Operating Assistance		
Excess of Operating Funds at June 30, 2014	\$ (415,198)	\$ -
Allocations Received	1,847,564	-
Funds Available	1,432,366	-
Less Eligible Costs	(1,589,270)	-
Shortage of Operating Funds at June 30, 2015	(156,904)	-
Allocations Received	2,051,592	-
Grants	-	63,619
Funds Available	1,894,688	63,619
Less Eligible Costs	(1,882,680)	-
Excess of Operating Funds at June 30, 2016	<u>\$ 12,008</u>	<u>\$ 63,619</u>

Changes in unearned revenues for the fiscal years ended June 30, 2016 and 2015 for capital assistance were as follows:

	<u>Proposition 1B</u>	<u>STA</u>	<u>Total</u>
Capital Assistance:			
Excess of Capital Funds at June 30, 2014	\$ 460,700	\$ -	\$ 460,700
Allocations Received	262,967	10,445	273,412
Interest Allocations	2,046	-	2,046
Funds Available	725,713	10,445	736,158
Less Eligible Costs	-	(10,445)	(10,445)
Excess of Capital Funds at June 30, 2015	725,713	-	725,713
Allocations Received	1,019,369	-	1,019,369
Interest Allocations	1,631	-	1,631
Funds Available	1,746,713	-	1,746,713
Less Eligible Costs	(1,481,573)	-	(1,481,573)
Excess of Capital Funds at June 30, 2016	<u>\$ 265,140</u>	<u>\$ -</u>	<u>\$ 265,140</u>

The following is a list of projects related to the deferred capital balance:

<u>Allocation Number</u>	<u>Project Description</u>	<u>Unearned Capital Balance</u>
99313-99314	Rolling Stock Procurement and Security Cameras	\$ 265,140

**City of Beaumont Transit System**  
**Notes to Financial Statements**  
June 30, 2016 and 2015

**5) LONG TERM DEBT**

Long-term liabilities of the System for the fiscal years ended June 30, 2016 and June 30, 2015 consisted of the following:

	Balance July 1, 2015	Additions	Deletions	Balance June 30, 2016	Due Within One Year
Compensated Absences	\$ 200,672	\$ 39,536	\$ -	\$ 240,208	\$ 21,837
Net Pension Liability	491,132	198,708	-	689,840	-
	<u>\$ 691,804</u>	<u>\$ 238,244</u>	<u>\$ -</u>	<u>\$ 930,048</u>	<u>\$ 21,837</u>

  

	Balance July 1, 2014	Additions	Deletions	Balance June 30, 2015	Due Within One Year
Compensated Absences	\$ 212,773	\$ 53,193	\$ (65,294)	\$ 200,672	\$ 18,060
Net Pension Liability	-	667,183	(176,051)	491,132	-
	<u>\$ 212,773</u>	<u>\$ 720,376</u>	<u>\$ (241,345)</u>	<u>\$ 691,804</u>	<u>\$ 18,060</u>

**6) DEFINED BENEFIT PENSION PLAN**

**General Information about the Defined Benefit Pension Plans**

The City of Beaumont's Transit System participates in the City of Beaumont's cost-sharing multiple employer defined benefit pension plans administered by the California Public Employees' Retirement System (CalPERS). Employees of the System are employees of the City of Beaumont and participate in the miscellaneous cost-sharing plans of the City of Beaumont as a whole. The required note disclosures regarding pension plans are included in the City of Beaumont's financial statements. Please see those financial statements for information about the plan as a whole.

The net pension liability (NPL) of \$689,840 reported by the System, represents the System's proportional share of the City's total miscellaneous pool cost-sharing multiple employer defined benefit pension plan of \$4,407,926. The System's NPL represents 15.65% of the total miscellaneous plan NPL as of June 30, 2016.

**7) TRANSPORTATION DEVELOPMENT ACT CONFORMANCE MATTERS**

The System is subject to the provisions of Public Utilities Code (PUC) Section 99268.5 and must maintain a minimum fare ratio of 10%.

**City of Beaumont Transit System**  
**Notes to Financial Statements**  
June 30, 2016 and 2015

**7) TRANSPORTATION DEVELOPMENT ACT CONFORMANCE MATTERS - Continued**

For fiscal years 2016 and 2015, the System's fare ratio of operating revenues to operating expenses, as calculated below:

	Dial-A-Ride 2016	Fixed Route 2016	Combined 2016	Dial-A-Ride 2015	Fixed Route 2015	Combined 2015
Operating Revenues	\$ 24,004	\$ 202,047	\$ 226,051	\$ 30,093	\$ 206,678	\$ 236,771
Less:						
Fare Revenues Related to New Routes or Extension of Services						-
Total Operating Revenues	<u>\$ 24,004</u>	<u>\$ 202,047</u>	<u>\$ 226,051</u>	<u>\$ 30,093</u>	<u>\$ 206,678</u>	<u>\$ 236,771</u>
Operating Expenses	\$ 396,690	\$ 2,081,931	\$ 2,478,621	\$ 429,825	\$ 1,782,047	\$ 2,211,872
Less:						
Depreciation Expense	(92,261)	(276,785)	(369,046)	(93,839)	(281,517)	(375,356)
Operating Expenses Related to New Routes or Extension Services						-
Total Operating Expenses	<u>\$ 304,429</u>	<u>\$ 1,805,146</u>	<u>\$ 2,109,575</u>	<u>\$ 335,986</u>	<u>\$ 1,500,530</u>	<u>\$ 1,836,516</u>
Fare Ratio	7.9%	11.2%	10.7%	9.0%	13.8%	12.9%

**8) PROPOSITION 1B**

On November 7, 2006, the voters of the State of California approved the Highway Safety, Traffic Reduction, Air Quality, and Port Security Bond Act of 2006, known as Proposition 1B. Proposition 1B included a state program of funding in the amount of \$4 billion and \$1 billion to be deposited in the Public Transportation Modernization, Improvement and Service Enhancement Account (PTMISEA) and Transit System Safety, Security and Disaster Response Account (TSSSDRA), respectively. PTMISEA funds can be used for rehabilitation, safety or modernization improvements, capital service enhancements or expansions, new capital projects, bus rapid transit improvements, or for rolling stock procurement, rehabilitation or replacement. TSSSDRA funds can be used for transportation-related security and safety projects.

**City of Beaumont Transit System**  
**Notes to Financial Statements**  
June 30, 2016 and 2015

**8) PROPOSITION 1B - Continued**

Proposition 1B activities during the fiscal year ended June 30, 2016 and 2015 were as follows:

	TSSDRA CALEMA	PTMISEA CALTRANS	Total
Unspent Prop 1B Funds as of June 30, 2014	\$ 1,450	\$ 459,250	\$ 460,700
Prop 1B Funds Received		247,659	247,659
Funding Correction	15,308		15,308
Interest Allocations	47	1,999	2,046
Funds Available	16,805	708,908	725,713
Prop 1B Funds Used			-
Unspent Prop 1B Funds as of June 30, 2015	16,805	708,908	725,713
Prop 1B Funds Received		1,019,369	1,019,369
Interest Allocations		1,631	1,631
Funds Available	16,805	1,729,908	1,746,713
Prop 1B Funds Used	(16,805)	(1,464,768)	(1,481,573)
Unspent Prop 1B Funds as of June 30, 2016	\$ -	\$ 265,140	\$ 265,140

**9) RESTATEMENT OF NET POSITION**

The System implemented Governmental Accounting Standards Board (GASB) Statement No. 68, *Accounting and Financial Reporting for Pensions*, in fiscal year 2014-15. As a result, beginning net position in the Statement of Revenues, Expenses and Changes in Net Position was restated by \$(547,634), to reflect the cumulative effect of applying this statement. In addition, the 2014-15 beginning net position was restated by \$119,708 for unearned revenues from prior years which are now considered earned due to the implementation of GASB Statement No. 68. The net effect of these adjustments results in a restatement of net position of (\$427,926).

**10) RISK MANAGEMENT**

The System's activities are exposed to various risks of loss related to torts, theft of, damage to, and destruction of assets; errors and omissions, injuries to employees, injuries to others, and natural disasters. The System is insured as part of the City of Beaumont's insurance coverage for general liability, property damage, and workers' compensation. See the City of Beaumont's financial statements for more information.

**City of Beaumont Transit System**  
**Notes to Financial Statements**  
June 30, 2016 and 2015

**11) CONTINGENCIES**

The System's activities are substantially funded by revenues from the State of California, passed through the RCTC. Amounts received from grantor agencies are subject to audit and adjustment by grantor agencies, principally RCTC. Any disallowed claims, including amounts already collected, may constitute a liability of the System. Management expects the amount, if any, of expenses which may be disallowed by the grantor would be immaterial.

**Riverside County District Attorney and FBI Investigation**

On April 22, 2015, the Riverside County District Attorney's Office, assisted by the FBI, served search warrants at the Beaumont Civic Center (City Hall). The joint investigation resulted in the arrest and indictment of seven former members of city management, including the former City Manager and former Finance Director for embezzlement of public funds and conspiracy. The former city attorney and several former consultants were also arrested on related charges. It is unknown at this time what the impact of these investigations will be on the System's financial statements, if any. Management expects the impacts of the investigation on the System's financial statements, if any, would be immaterial.

**Independent Auditor's Report on Internal Control over Financial Reporting and  
on Compliance and Other Matters Based on an Audit of Financial Statements  
Performed in Accordance with *Government Auditing Standards***

To the Honorable Mayor and Members of the City Council  
of the City of Beaumont  
Beaumont, California

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Beaumont Transit System (System) of the City of Beaumont, California (City), as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise the District's basic financial statements, and have issued our report thereon dated September 20, 2017.

**Internal Control Over Financial Reporting**

In planning and performing our audit of the financial statements, we considered the System's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the System's internal control. Accordingly, we do not express an opinion on the effectiveness of the System's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the preceding paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. We did identify certain deficiencies in internal control, described in the accompanying schedule of findings and responses as items 2016-1 to 2016, that we consider to be material weaknesses.

## **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the System's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements including the Transportation Development Act as prescribed in § 6666 and § 6667 of Title 21, Chapter 3, Subchapter 2, Article 5.5 of the California Code of Regulations, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

## **Beaumont Transit System's Responses to Findings**

The System's responses to the findings identified in our audit are described in the accompanying schedule of findings and responses. The System's responses were not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on them.

## **Purpose of this Report**

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the organization's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the organization's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

*Van Lant & Fankhaed, LLP*

September 20, 2017

## **Independent Auditor's Report on Internal Control**

**BEAUMONT TRANSIT SYSTEM  
SCHEDULE OF FINDINGS AND RESPONSES  
Year Ended June 30, 2016**

**2016-1: Policies and Procedures**

*The following is a continuation from the prior year:*

Findings:

Our audit procedures involved obtaining and evaluating various policies and procedures. During our audit, it became apparent that the Beaumont Transit System (described as “City” throughout) lacked formal policies and guidelines in certain areas, including the following:

- Accounting Policies and Procedures
- Fraud Prevention and Detection Policy (Code of Conduct)
- Capital Assets

Although the City may have informal policies in these areas, we believe the City could benefit from a more formal and comprehensive policies and procedures manual, approved by the City Council, which would provide detailed guidance to employees and management. This will help to ensure consistency in these areas, even if there is staff turnover. The following provides more detail regarding these policies and procedures:

*Accounting Policies and Procedures*

Communication is an essential component of a comprehensive framework of internal controls. One method of communication that is particularly effective for controls over accounting and financial reporting is the formal documentation of accounting policies and procedures. A well-designed and properly maintained system of documenting accounting policies and procedures enhances both accountability and consistency. The resulting documentation can also serve as a useful training tool for staff.

The documentation of accounting policies and procedures should be evaluated annually and updated periodically, as necessary. It should be readily accessible to all applicable employees.

An accounting policies and procedures manual should include a comprehensive list of accounting procedures along with an indication of the employees responsible for completing the procedures. It should delineate the authority and responsibility of all employees, including review and approval procedures. Procedures should be described as they are actually intended to be performed, rather than in some idealized form. The documentation of accounting policies and procedures should explain the design and purpose of control-related procedures to increase employee understanding.

*Code of Conduct (including fraud prevention and detection policies)*

The City Council and Management are responsible for designing and implementing systems and procedures for the prevention and detection of fraud, and for ensuring a culture and environment that promotes honesty and ethical behavior. This includes the responsibility to develop and implement a formal fraud risk assessment program.

**BEAUMONT TRANSIT SYSTEM**  
**SCHEDULE OF FINDINGS AND RESPONSES**  
**Year Ended June 30, 2016**

***2016-1: Policies and Procedures - Continued***

Fraud can range from minor employee theft and unproductive behavior to misappropriation of assets and fraudulent financial reporting. Although external auditors are required to consider the risk of fraud in the audit process, it should be noted that external auditors are not considered part of the City's controls over the prevention and detection of fraud. Rather, external auditors are required to evaluate the City's fraud prevention and detection program, in relation to the audit of the financial statements.

The risk of fraud can be reduced through a combination of prevention, deterrence, and detection measures. However, fraud can be difficult to detect because it often involves concealment through falsification of documents or collusion among management, employees, or third parties. Therefore, it is important to place a strong emphasis on fraud prevention, which may reduce opportunities for fraud to take place, and fraud deterrence, which could persuade individuals that they should not commit fraud because of the likelihood of detection and punishment. Moreover, prevention and deterrence measures are much less costly than the time and expense required for fraud detection and investigation.

During our audit we noted the City has taken steps to address the risk of fraud in certain areas, such as segregation of duties and other internal controls. However, the City should consider developing and expanding its formal fraud policies. For example, the City's current policies do not provide a thorough description of fraud. They also do not provide direction as to what employees should do if they suspect fraud is occurring.

The City should consider establishing a more formal training program for all employees regarding fraud. New employees should be trained at the time of hiring about the entity's code of conduct (and fraud policies). This training should explicitly cover expectations of all employees regarding (1) their duty to communicate certain matters; (2) a list of the types of matters, including actual or suspected fraud, to be communicated along with specific examples; and (3) information on how to communicate those matters. In addition to the training at the time of hiring, employees should receive refresher training periodically thereafter.

As mentioned above, management needs to provide information to employees on how to communicate fraud related matters. Research has shown that most fraud is detected by fellow employees, and not by outside auditors or internal controls. It is important for the City to establish and communicate to employees a reporting system that is appropriate for the City. The City should consider establishing a confidential reporting mechanism, not only for employees, but also for vendors and customers of the City.

Overall, the City should establish a formal fraud risk assessment program, to ensure that the risk of fraud is being periodically evaluated, monitored, and that appropriate action is taken to address the identified risks.

In summary, the City has established controls over fraud in certain areas. However, the City should consider expanding its fraud prevention program as discussed above. The above comments do not address all components of a strong antifraud program. Additional information can be provided regarding this issue.

**BEAUMONT TRANSIT SYSTEM**  
**SCHEDULE OF FINDINGS AND RESPONSES**  
**Year Ended June 30, 2016**

***2016-1: Policies and Procedures - Continued***

*Capital Assets Policies*

We recommend the City establish formal policies regarding capital assets, including capitalization thresholds, depreciation methods and useful lives estimation guidelines, procedures for periodic inventories of tangible assets, procurement and disposal policies, and guidance regarding planning and funding of the City's future capital needs.

As described above, the City should establish procedures for periodic inventories of capital assets. It is essential that governments establish and maintain appropriate inventory systems for their tangible capital assets. Such systems are needed to protect tangible capital assets from the danger of loss or misuse.

As described by GFOA, "Many governments have installed "perpetual" inventory systems to maintain effective control over their tangible capital assets. Perpetual inventory systems are constantly updated to reflect additions and deletions of tangible capital assets, thus providing managers with direct access throughout the year to reliable information on current balances in tangible capital asset accounts. One advantage of establishing and maintaining a sound perpetual inventory system for tangible capital assets is that such a system can relieve a government of the burden of performing an annual inventory of its tangible capital assets. Such a system, however, still requires periodic verification to ensure that it is continuing to function properly as designed."

GFOA recommends that every "local government periodically inventory its tangible capital assets so that all such assets are accounted for, at least on a test basis, no less often than once every five years. While well-designed and properly maintained perpetual inventory systems can eliminate the need for an annual inventory of a governments tangible capital assets, no inventory system is so reliable as to eliminate completely the need for a periodic physical inventory."

We recommend the City take the necessary steps to ensure that capital assets and related depreciation are properly and consistently reported, including the establishment of formal policies and procedures in this area.

Recommendation:

We recommend the City develop and establish formal policies and procedures as discussed above. The policies and procedures should be developed by appropriate personnel and approved by the City Council. The City should consider GFOA's recommended practices and other resources during the process.

Management's Response:

*Accounting Policies and Procedures*

While the Transit management oversees ongoing service and compliance aspects of the Beaumont Transit System, the City of Beaumont management had ultimate control over the Transit System financial

**BEAUMONT TRANSIT SYSTEM  
SCHEDULE OF FINDINGS AND RESPONSES  
Year Ended June 30, 2016**

***2016-1: Policies and Procedures - Continued***

reporting and other broader based management oversight. City management staff has changed, and with that change, corrective actions have been taken. The City Council has formed an oversight Financial and Audit Committee to review significant financial transactions and vet policies and procedures related to the financial functions of the city. Additionally, City policies and procedures have been adopted that include financial practices. Management has addressed overall segregation of duties and has taken steps to create mitigation controls where necessary.

*Fraud Prevention and Detection Policy (Code of Conduct)*

All City management has participated in ethics training and a code of conduct has been adopted. Staff have been verbally advised that if they “see something, say something.” A formal fraud risk assessment program has not been developed, but will be discussed and drafted in the future.

*Capital Assets*

Capital assets have been properly recorded in the Beaumont Transit System, but overall City related capital asset policies were vague and inconsistent with respect to the classification and the useful lives of fixed assets. A more comprehensive policy has been adopted by City Council and will be applied consistently going forward. Beaumont Transit System maintains an inventory listing of fixed assets placed in service utilizing capital funds as provided through the various funding sources; however, any assets being used by the Beaumont Transit System that were acquired through City funds are not tracked at the same detail level. The City is currently involved in a fixed asset inventory and valuation process to have all City assets identified, tagged, valued and recorded in order to properly comply with GFOA recommendations.

***2016-2: Accounting Records and Financial Reporting***

*The following is a continuation from the prior year:*

Findings:

The City’s Management and City Council are responsible for the preparation and fair presentation of financial statements in accordance with applicable accounting pronouncements. This includes the design and implementation of relevant internal controls to ensure accurate and timely financial reporting. The audit for the 2015-16 fiscal year did not begin until May of 2017, almost an entire year after the fiscal year-end. In addition, when we began the audit, it became apparent that some year-end accounting entries had not yet been completed. Throughout the audit process, the City’s current Finance staff provided us with the necessary analysis and adjustments, as requested. However, much of the analysis, reconciliations and adjustments were completed 12 months after year-end. It should be noted that much of the accounting work for the 2015-16 fiscal year had to be performed by new Finance personnel who joined the City in 2016. In other words, the 2015-16 accounting records were in disarray prior to the current staff, and a significant amount of effort was expended to analyze and adjust these records.

**BEAUMONT TRANSIT SYSTEM  
SCHEDULE OF FINDINGS AND RESPONSES  
Year Ended June 30, 2016**

***2016-2: Accounting Records and Financial Reporting - Continued***

This situation may be the result of various factors, including turnover in City management, inadequate oversight by the City's management, and the lack of formal policies and procedures discussed in Finding 2016-1 above. The year-end closing process, including necessary analysis, reconciliations, and adjustments, should normally be completed within a few months after year-end. If accounting records are consistently and accurately maintained throughout each fiscal year, the year-end closing process can be completed in a much more efficient manner. If balances and transactions have not been analyzed and reconciled in a timely manner, it could be an indication that City management is not receiving accurate financial information throughout each fiscal year. In addition, the City may not be able to comply with various reporting requirements in a timely manner (State and Federal deadlines).

Recommendation:

We recommend the City take steps to evaluate the current accounting policies and procedures, and determine what revisions may be necessary to ensure timely and accurate financial reporting. In addition to the formal accounting policies and procedures manual discussed above, we recommend the City prepare a schedule of accounting procedures to be performed each month, quarter, and at year-end, as applicable. The schedule should include a detailed description of the required analysis and adjustments, along with due dates for the various procedures. The schedule should include provision for sign-off, indicating when the applicable procedures were performed and reviewed as necessary. Applicable City staff should be thoroughly trained and knowledgeable regarding generally accepted accounting principles as they relate to local governments. This will help to ensure accurate, consistent and timely financial reporting.

Management's Response:

While the Transit management oversees ongoing service and compliance aspects of the Beaumont Transit System, the City of Beaumont management had ultimate control over the Transit System financial reporting and other broader based management oversight. The City Council has adopted formalized policies and procedures, which include financial practices. The entire financial reporting software system has been upgraded allowing the Transit Director and the Transit Management Analyst real-time access to all applicable internal financial reports and data. The day-to-day financial department policies and procedures have been discussed and an initial draft has been prepared. The finance staff includes individuals with training and education in accounting, and the current Director of Finance is a certified public accountant in California with knowledge and background in government accounting practices.

***2016-3 Segregation of Duties for Bus Passes***

*The following is a continuation from the prior year:*

Condition:

The same City staff issuing bus passes are also responsible for collecting and receipting payments from customers into the City's cash receipts system. Also, there does not seem to be any sort of inventory control over the bus passes or a way to reconcile the bus passes sold with corresponding receipts.

**BEAUMONT TRANSIT SYSTEM  
SCHEDULE OF FINDINGS AND RESPONSES  
Year Ended June 30, 2016**

***2016-3 Segregation of Duties for Bus Passes - Continued***

Criteria:

In a strong internal control environment, the same individual should not have access to the payments from customers and the ability to issue bus passes unless an appropriate mitigating control has been implemented.

Potential Effect of Condition:

Bus passes could be issued without the cash receipts being properly deposited into the City's bank account or recorded in the City's general ledger.

Recommendation:

We recommend the City implement a procedure to control the inventory of the bus passes, such as numerical sequence control, in order to reconcile the number of bus passes sold and the amounts recorded as revenue and posted in the City's general ledger.

Management's Response:

While the Transit management oversees ongoing service and compliance aspects of the Beaumont Transit System, the City of Beaumont management had ultimate control over the Transit System financial reporting and other broader based management oversight. Bus passes are sold to the public outside of the Transit department staff. The internal system for issuance of bus passes has been reviewed and a formal procedure is in place to safeguard and track the various bus passes that are purchased and sold. A tracking process was started in July 2017 and is monitored outside of the Finance Office, by the Transit Management Analyst.

***2016-4 Controls Over Accrued Vacation***

*The following is a continuation from the prior year:*

Condition:

The Paychex payroll database tracks the vacation accruals for employees through automatic accruals for each pay period for each employee. The City has established, through Memorandums of Understanding (MOUs) with various employee unions, caps on the number of hours that can be accrued by employees. However, there does not appear to be any monitoring of the vacation hours to ensure the payroll system does not continue to accrue vacation hours once the cap has been reached. Furthermore, our review of the vacation accrual schedule found the number of hours accrued by a couple of employees exceeded the maximum number of hours per the applicable MOU.

Criteria:

Various City MOU's state the maximum vacation accrual shall not exceed the equivalent of the accrual earned for a 2-year period. We found two employees with accrued vacation above this maximum accrual.

**BEAUMONT TRANSIT SYSTEM  
SCHEDULE OF FINDINGS AND RESPONSES  
Year Ended June 30, 2016**

***2016-4 Controls Over Accrued Vacation - Continued***

*Cause of Condition:*

The payroll system does not have a control in place to cap accrual hours once they have exceeded the maximum per the MOUs and no other monitoring by City staff to verify accrued hours are in accordance with the MOUs.

*Potential Effect of Condition:*

The liability for accrued vacation could be misstated, City employees could earn and use more vacation hours than allowable by the MOUs, and payouts to employees upon retirement could be higher than allowable by the MOUs.

*Recommendation:*

We recommend the City review the payroll system to determine if a cap control system could be implemented to prevent vacation hours from continuing to accrue once the maximum hours per the MOUs have been reached. In addition, periodically, the City should monitor the vacation accruals to ensure all vacation hours accruing are within the applicable MOU.

*Management's Response:*

While the Transit management oversees ongoing service and compliance aspects of the Beaumont Transit System, the City of Beaumont management had ultimate control over the Transit System financial reporting and other broader based management oversight. The finance department provides employee time-off bank reports to all responsible directors and supervisors on a monthly basis to verify the accuracy and availability of accrued time for their staff. The MOUs currently contain caps on the sick and vacation that can be accrued. While the finance software is upgraded and integrated, the payroll processing software is also being updated. The goal is to have better integration, reporting, and control over various aspects of the payroll process, which includes implementation of system time bank caps.