

City of Beaumont

Beaumont, California

Report on Internal Control Related Matters Identified in an Audit

For the Year Ended June 30, 2017



City of Beaumont

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

In planning and performing our audit of the financial statements of the of the City of Beaumont, California (the "City") as of and for the year ended June 30, 2017, in accordance with auditing standards generally accepted in the United States of America, we considered the City's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control. Accordingly, we do not express an opinion on the effectiveness of the City's internal control.

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. In addition, because of inherent limitations in internal control, including the possibility of management override of controls, misstatements due to error or fraud may occur and not be detected by such controls. However, as described in the accompanying schedule of findings and responses, we identified certain deficiencies in internal control that we consider to be material weaknesses.

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. We consider the deficiencies described in findings 2017-001 through 2017-007 to be material weaknesses.

A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the following deficiencies described in findings 2017-008 through 2017-010 to be significant deficiencies

As part of obtaining reasonable assurance about whether the City's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, 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 is required to be reported under *Government Auditing Standards*.

During our audit, we also became aware of deficiencies in internal control other than significant deficiencies or material weaknesses. These are reported as other matters in this letter and we believe are opportunities for strengthening internal controls and operating efficiency.

The City's written responses included in this report have not been subjected to the audit procedures applied in the audit of the financial statements and, accordingly, we express no opinion on them.

Honorable Mayor and Members of the City Council
of the City of Beaumont
Beaumont, California
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This communication is intended solely for the information and use of management, City Council, others within the organization, and agencies and pass-through entities requiring compliance with generally accepted government auditing standards, and is not intended to be and should not be used by anyone other than these specified parties

The PwC Group, LLP

August 6, 2018

City of Beaumont
Report on Internal Control Related Matters Identified in an Audit
For the Year Ended June 30, 2017

Findings:

Finding 2017-001 Internal Control over Financial Reporting/Accounting Close and Accuracy in Financial Reporting

Criteria:

Management is responsible for designing, implementing, and maintaining appropriate internal control over financial reporting and compliance. Management is also responsible for the accuracy of the financial statements including disclosures. As part of satisfying that responsibility, staff must possess the skills, knowledge, and experience necessary to complete the year-end close and must diligently employ the skills, knowledge, and experience to produce reliable and accurate financial information.

Effective internal control over financial reporting provides reasonable assurance for the completeness and accuracy of accounting records and proper year-end closing. Internal control is defined as a process implemented and monitored by the City Council, management, and other personnel that provides reasonable assurance that the objectives of the City will be achieved. Internal control is not one event, but a series of events that occur throughout an entity's operations. The City's internal control system should be designed to provide reasonable assurance regarding the achievement of objectives in the following categories:

- reliability of financial reporting for internal and external use;
- effectiveness and efficiency of operations; and
- compliance with applicable laws and regulations.

The Internal Control Framework would include establishing or enhancing guidance in the following areas:

- *Control environment* sets the tone of an organization, influencing the control consciousness of its people. It is the foundation for all other components of internal control, providing discipline and structure.
- *Risk assessment* is the entity's identification and analysis of relevant risks to achievement of its objectives, forming a basis for developing appropriate risk responses.
- *Control activities* are the actions management establishes through policies and procedures to achieve objectives and respond to risks in the internal control system.
- *Information and communication* systems support the identification, capture, and exchange of information in a form and time frame that enables people to carry out their responsibilities.
- *Monitoring* consists of activities management establishes and operates to assess the quality of performance over time.

Condition:

Due to limited staffing levels and the financial difficulties faced by the City during our audit period ended June 30 2017, internal controls were either lacking, were not designed properly, and mitigating controls were not sufficient to effectively identify misstatements due from error.

In addition, the City did not have in place during our audit period a systematic method for ensuring that timely and complete year end closing procedures were in operation before presenting the trial balance to auditors, resulting in a number of journal entries being presented to correct or to reclassify balances in financial statements that should normally be captured through the closing process. Those adjustments have been reported and posted by the City.

City of Beaumont
Report on Internal Control Related Matters Identified in an Audit (Continued)
For the Year Ended June 30, 2017

Findings:

Finding 2017-001 Internal Control over Financial Reporting/Accounting Close and Accuracy in Financial Reporting (Continued)

Cause:

Numerous operational challenges were faced by the finance department as a result of the limited staff resources. The City also does not have standard year-end closing procedures which could reduce the risk that there are accounting errors recorded and go undetected in the City's general ledger.

Effect:

Delays in processing transactions timely and closing accounting periods can create accounting errors that could go undetected and may lead the financial statements to be materially misstated and create further delays in the release of audited financial statements, as well as allow for possible irregularities including fraud to exist and continue without notice.

Corrections of errors in the prior years (ie. prior period adjustments) were made for the following items:

1. Correction to GASB 68 pension deferred outflows and deferred inflows to match the actuarial reports
2. Correction to prior year unearned revenue for transit
3. To record capital assets, and related depreciation expense, not previously recorded

Reclassifications due to conformity of accounts with other agencies' in the prior years (ie. prior period adjustments) were made for the following items:

1. Reclassification to unearned revenue for prior year developer impact fees recognized in revenue
2. To record the activities of the Beaumont Financing Authority in the governmental fund financial statements and government-wide governmental activities as a blended component unit

Current year adjustments were made for the following items:

1. Adjust self-insured portion of claims liability to match the actuarial report
2. To correct the pension deferred outflows and deferred inflows to match actuarial reports
3. Record adjustment to depreciation expense

Recommendation:

We understand that the City has established year-end closing procedures subsequent to the period of our audit. However, we recommend that the City review those year-end closing procedures to ensure that it adequately addresses and includes an evaluation of the areas that have caused the accounting errors above and the need for correcting journal entries after the year end closing. These procedures should include timely review and approval by management of account reconciliations, sub-ledger transactions, cutoff review for account balances at a fund and overall government-wide level, and revenue and expenditures/expense review. Revenue and expenditures/expenses should be compared to the prior year or prior year trends and to the budget.

City of Beaumont
Report on Internal Control Related Matters Identified in an Audit (Continued)
For the Year Ended June 30, 2017

Findings:

Finding 2017-001 Internal Control over Financial Reporting/Accounting Close and Accuracy in Financial Reporting (Continued)

Management's Response and Corrective Action Plan:

City wide financial policies were adopted by City Council on September 20, 2016. The Finance and Audit Committee has been established to assist in the development and documentation of procedures as well as the implementation of internal controls. Formal Finance department policies were approved by the Finance and Audit Committee on January 16, 2018. With a new software implementation in December 2016 some procedures are being developed as the software is utilized to provide the most current use and oversight measures. The finance department has created a monthly, quarterly, semi-annual and annual checklist of various functions that are to occur to provide the most current reporting once the new software is fully operational. Timing has been an issue due to the City circumstances and staffing levels. FY16/17 was substantially complete for the audit, but improvements are still needed.

Finding 2017-002 Policies and Procedures

Criteria:

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. An accounting policies and procedures manual should include a comprehensive list of accounting procedures along with an indication of the employees and/or position responsible for completing the procedures. It should delineate the authority and responsibility of all employees or positions, including review and approval procedures. Internal control procedures should be described as they are actually intended to be performed. The documentation of accounting policies and procedures should explain the design and purpose of control-related procedures to improve employee understanding and aid in compliance.

The Government Finance Officers Association (GFOA) has issued a "Recommended Practice" regarding having a debt management policy. Specifically, GFOA recommends that local governments that issue should debt develop a comprehensive debt policy. Examples of elements that should be addressed in such a policy include:

- The purpose for which the debt may be issued;
- Legal debt limitations established by policy;
- Types of debt permitted to be issued and criteria for issuance;
- Structural features that may be considered, such as maturity of debt, setting the maturities of the debt equal to or less than the useful life of the project; use of zero coupon bonds, discount bonds, premium bonds.
- Credit objectives;
- Authorized methods of sale;
- Method of selecting outside finance professionals;
- Policy on refunding debt

City of Beaumont
Report on Internal Control Related Matters Identified in an Audit (Continued)
For the Year Ended June 30, 2017

Findings:

Finding 2017-002 Policies and Procedures (Continued)

Condition:

Our audit involved obtaining and evaluating various policies and procedures of the City. During the audit period, the City lacked having formal policies, procedures and guidelines in place for certain areas, including the following:

- Accounting Policies and Procedures
- Debt Management Policy

The City has been working towards establishing a comprehensive policy which was adopted after our audit period. During our audit the City had informal policies in these areas. We reiterate that 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, and continuity in periods of staff turnover.

Cause:

The City is currently in the aftermath and recovering from a major fraud which took place. Therefore its priorities have shifted to fiscal recovery and a focus on those areas of key internal controls that needed to be instituted in order to prevent the risk of fraud from occurring again. The policy aspect of the program, though very important, has not been the highest priority of Management or City Council though there is an awareness that it is necessary. As the City is continuing its recovery process, and with additional time, the comprehensive program and policy can be prioritized.

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. 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.

A debt policy should be formally adopted by the legislative body, and the debt program should be continuously monitored to ensure compliance with the debt policy. We recommend the City consider establishing a formal debt policy, taking into consideration the recommendations of GFOA.

Management's Response:

City wide financial policies adopted by City Council in September 2016 included Accounting Policies, Financial Management Policies, Investment Policies, Fixed Asset Policies, and Capital Improvement Policies. The Financial Management Policies specifically address reserves as they relate to levels of unrestricted fund balances, and debt management.

Specific finance department policies and procedures related to CFD bond debt were ratified by the City Council on February 20, 2018. Financial policy and procedure manuals will continue to be refined, and existing policies and procedures will be reviewed by the Finance Committee on an annual basis.

City of Beaumont
Report on Internal Control Related Matters Identified in an Audit (Continued)
For the Year Ended June 30, 2017

Findings:

Finding 2017-002 Policies and Procedures (Continued)

As the City staff work through software implementation, they are creating checklists and process documents with snapshots. The Finance Department worked with the Finance and Audit Committee to develop a Finance Department Policies and Procedures Manual that covers General Accounting policies, Cash Management policies, Capital Asset policies, Cash Receipts procedures and Accounts Payable procedures. The completed Manual was approved by City Council on January 16, 2018.

The secured debt currently maintained by the City is a capital lease agreement for three police department vehicles. Other debt has been recorded in a long-term debt fund and repayment terms have been established where applicable. Debt payments, have been made timely and no defaults have occurred.

Finding 2017-003 Establish a Comprehensive Fraud Program and Policy

Criteria:

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 and detection program.

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, the 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.

City of Beaumont
Report on Internal Control Related Matters Identified in an Audit (Continued)
For the Year Ended June 30, 2017

Findings:

Finding 2017-003 Establish a Comprehensive Fraud Program and Policy (Continued)

Often, 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 and detection, which may reduce opportunities for fraud to take place, and on fraud deterrence, which could persuade individuals that they should not commit fraud because of the likelihood of investigation, corrective action including progressive discipline up to termination and punishment. Moreover, prevention and deterrence measures are much less costly than the time and expense required for fraud detection and investigation.

The City Council, Management and personnel at all levels of the organization — including every level of management and staff— have a responsibility and role in managing fraud risk. Particularly, they are expected to understand how the organization is responding to heightened risks and regulations, to perform duties designed to mitigate the risk of fraud, and to understand their role in safeguarding the assets that are under public and stakeholder scrutiny.

A comprehensive fraud policy should include the following key elements:

- An explicit definition of actions that are deemed to be fraudulent
- Allocation of responsibilities for the overall management of fraud
- A statement that all appropriate measures to deter fraud will be taken
- The formal procedures which employees should follow if a fraud is suspected
- Notification that all instances of suspected fraud will be investigated and reported to the appropriate authorities
- An unequivocal statement that all fraud offenders will be prosecuted and that the police will be assisted in any investigation that is required
- A statement that all efforts will be made to recover wrongfully obtained assets from fraudsters
- Encouragement to employees to report any suspicion of fraud
- The steps to be taken in the event a fraud is discovered and who is responsible for taking action including:
 - procedures staff should follow
 - assigning responsibility for an instant response to the occurrence
recovering funds
 - dealing with the media

City of Beaumont
Report on Internal Control Related Matters Identified in an Audit (Continued)
For the Year Ended June 30, 2017

Findings:

Finding 2017-003 Establish a Comprehensive Fraud Program and Policy (Continued)

Condition:

The City currently lacks a formal comprehensive fraud program required to help prevent, detect and identify fraud and in order to appropriately safeguard assets. According to management, training has been provided with respect to the “tone at the top” to the City employees, however when interviewing employees during our audit they were unaware of a fraud policy. The City has taken steps to address the risk of fraud in certain areas, such as segregation of duties and other internal controls, but continued to lack the policies and a formalized process and program to institutionalize a comprehensive fraud program is needed.

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.

Cause:

The City is currently in the aftermath and recovering from a major fraud which took place. Therefore its priorities have shifted to fiscal recovery and a focus on those areas of key internal controls that needed to be instituted in order to prevent the risk of fraud from occurring again. The policy aspect of the program, though very important, has not been the highest priority of Management or City Council though there is an awareness that it is necessary. As the City is continuing its recovery process, and with additional time, the comprehensive program and policy can be prioritized.

Effect:

The effect of fraud, misappropriation and defalcations and other fiscal irregularities can be far reaching and financially destructive to an organization and its reputation. All organizations are subject to fraud risks and it is impossible to eliminate all fraud in an organization. However, the potential for fraud in an organization and the failure to assess or identify the risk can be an impediment to the organizations achievement of its objections and can be the direct result of the failure to implement a policy and provide avenues for employees to report its concerns.

Recommendation:

The risk of fraud can be reduced through a combination of prevention, deterrence, and detection measures. The City should consider developing a formal fraud policies and institute a formal comprehensive fraud program.

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.

The policy needs to provide information to employees on how to communicate fraud related matters. 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.

The City should also 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.

City of Beaumont
Report on Internal Control Related Matters Identified in an Audit (Continued)
For the Year Ended June 30, 2017

Findings:

Finding 2017-003 Establish a Comprehensive Fraud Program and Policy (Continued)

Management's Response:

Training and management oversight with 'tone of management/tone at the top' has been completed. Additional processes are currently under consideration and will be in place during FY18/19. For FY18-19, budget for an "internal audit" function has been established. City Council must provide guidance and expectations in order for management to implement the program.

Finding 2017-004 Segregation of Duties for Cash Receipts – City Hall

Criteria:

A strong internal control environment designed to prevent and detect errors and fraud necessitates a segregation of duties over the cash receipt function.

Condition:

Currently, Customer Service Coordinators (cashiers) at City Hall can edit and void transactions in Incode (the City's cash receipts system) subsequent to the receipt being issued. The same cashier should not be able to edit or void a transaction after a receipt has been issued unless an appropriate audit trail and approval process is created by individuals outside of the cash collection process.

Cause:

Restrictive controls over the cashier's functions have been partially implemented however system limitation continue to prevent additional application controls to be put in place and strong internal controls, which should include reconciliation and monitoring of the void and adjustment process prior to closing the cash drawers, hasn't been designed or implemented due to limited staffing.

Effect:

Transactions could be voided by cashiers and amounts collected could be misappropriated and go undetected.

Recommendation:

Though the City had implemented a secondary sign off and online viewing of the voids and adjusting entries during the audit period ending June 30, 2017, we recommend the City further expand these procedures to include developing a daily edit report or monitoring function review of the report and reconcile it to the cash drawer before closing out the cash drawers. This should be signed off by a supervisor for the Accounting Technician not involved in the cash collection process. Amounts in excess of a large dollar threshold should be considered for sign off at a higher supervisory level.

Management's Response:

Software issues are being addressed with an upgrade to the cashiering software scheduled in January 2019, limiting the ability of void entries by cashiering staff. The software does create a posting batch each night for each cashier and a control has been put in place for the finance staff to review the posting batch prior to posting into the general ledger. Any unusual void or adjustment activity, or line items greater than \$20 are reviewed against scanned documentation. Entries without proper back up are forwarded to the Director of Administration. Effective July 1, 2018, two staff positions (who do not post cash receipts) have been deemed responsible to approve any void or adjustment entries greater than \$20.

City of Beaumont
Report on Internal Control Related Matters Identified in an Audit (Continued)
For the Year Ended June 30, 2017

Findings:

Finding 2017-005 Segregation of Duties for Building Permits

Criteria:

The same individual should not have access to the payments from customers and the ability to issue building permits unless an appropriate mitigating control has been implemented.

Condition:

The permit technician in the Community Development Department issues building permits and plan checks and collects the payments from customers. There is no reconciliation of the building permits and plan checks issued with the amounts collected and receipted in the City's general ledger.

Cause:

The City did not have proper design of its internal controls which would provide for an adequate segregation of duties.

Effect:

Building permits and plan checks could be issued without a corresponding cash receipt being recorded in the City's general ledger and ultimately deposited into the City's bank account.

Recommendation:

We recommend the City implement a procedure to generate reports from the Salesforce permit system, periodically (i.e. daily, weekly, monthly), and have someone independent of the permit issuance and collection functions review and reconcile the amounts from these reports to the revenue posted in the City's general ledger. In addition, the permit and fees process should be integrated into the accounting software to limit the number of manual entries posted to the general ledger system.

Management's Response:

The software implemented in Spring 2016 automated the building permit process. The issuance software integrates with the financial cash receipts software. The planning department software is available to the finance department, and a report can be run of all building permits issued for a particular period and agreed to the cash receipts posting. This finding was implemented and the process was integrated during FY16/17 but was not operational for a full year until fiscal year 2017/18.

Finding 2017-006 Development Impact Fees (DIF)

Criteria:

Strong internal controls should be established over the billing and collection functions for all significant revenues, to ensure the appropriate fees are being assessed, collected, deposited, and recorded in the City's accounting records.

City of Beaumont
Report on Internal Control Related Matters Identified in an Audit (Continued)
For the Year Ended June 30, 2017

Findings:

Finding 2017-006 Development Impact Fees (DIF) (Continued)

Condition:

The City currently uses a manual system for issuing DIF invoices and reconciling the accounting records which it is in the process of automating. Development impact fees (DIF) have been reconciled by type in order to establish balances at June 30, 2016. Prior to June 30, 2016, the City had recorded all of these revenues in one fund over the years (comingled), without keeping track of the expenditures and remaining unspent balances of each type of DIF. The City's has established in the new general ledger system a separate accounting fund for each DIF fee. The gross, fee credit, and net cash receipt are now tracked manually in Excel spreadsheets but recorded into the software by DIF that are restricted for certain purposes. Though substantial improvements have been made, manual processes including the use of spreadsheets typically are inefficient and can be prone to error or manipulation creating an increased risk of misappropriation or error in the financial statements.

Cause:

Prior lack of policies and procedures and oversight by top management in this area resulted in the lack of internal controls for both automated and manual controls. Implementation of appropriate internal controls has been a priority for the City but take additional time and resources to implement.

Effect:

There is an opportunity for DIF revenues to be misstated due to risk of error or fraud.

Recommendation:

Because the DIF are financially significant to the City, the City should place high priority on and continue with the replacement of the current manual system with a more automated system and set of internal controls over the billing/invoicing and cash receipt functions. The calculation of the DIF and application of fee credits should be subjected to independent analysis and oversight by the Finance Department including controls over the reconciliation of the billings to the receipts, the authorization of any deviations from the standard fees or fee credits, and posting to the general ledger system. Once automated, the system controls should be tested and validated alongside the manual process for a period of time. Once fully automated, the Finance Department should develop specific monitoring (i.e. fee credit reports, void reports, edit report, etc.) and reconciliation of the general ledger to the subsidiary ledger reports should be performed.

Management's Response:

Development impact fees (DIF) have been reconciled by type in order to establish balances at June 30, 2016. The manual reconciliations were performed on an annual basis for fiscal years 2014/15 and 2015/16. The Finance Department was able to perform monthly reconciliations starting with July 2016.

City of Beaumont
Report on Internal Control Related Matters Identified in an Audit (Continued)
For the Year Ended June 30, 2017

Findings:

Finding 2017-007 Segregation of Duties for Business Licenses

Criteria:

The same individual should not have access to the payments from customers and the ability to issue business licenses unless an appropriate mitigating control has been implemented.

Condition:

The permit technician accepts payments for business licenses and has the ability to issue and distribute business licenses. There is no independent reconciliation of the business licenses issued from the HdL system with the amounts collected and posted in the Incode cash receipts system.

Cause:

The City does not perform an independent reconciliation for business licenses between the HdL system and the Incode cash receipts system due to system limitation that were not evident prior to purchasing the system.

Effect:

Business licenses could be issued without a corresponding cash receipt being recorded in the City's general ledger and ultimately deposited into the City's bank account.

Recommendation:

We recommend the City implement a procedure to generate reports from the HdL business license program, periodically (i.e. daily, weekly, monthly), and have someone independent of the business license issuance and collection functions review and reconcile the amounts from these reports to the revenues posted in the City's general ledger. In addition, the permit and fees process should be integrated into the accounting software to limit the number of manual entries posted to the general ledger system.

Management's Response:

Integration has not taken place yet due to software issues. The software solution originally identified for the City related to business licenses has been deemed inadequate. The City is exploring alternative software solutions to improve the business license renewal and issuance process, which will integrate with the financial software. Once the integration issues are resolved and an appropriate solution identified, the review of business names against other available databases will be implemented. The finance department will assume this function in fiscal year 2018-19 and has made resolution of this control weakness a priority.

City of Beaumont
Report on Internal Control Related Matters Identified in an Audit (Continued)
For the Year Ended June 30, 2017

Findings:

Finding 2017-008 Transient Occupancy Tax (TOT) and Utility User's Tax (UUT)

Criteria:

Because the UUT and TOT revenues are significant to the City, strong internal controls should be established and procedures developed to track these revenues closely each month/quarter, including investigating any unusual fluctuations and delinquencies, and possibly perform periodic audits to ensure the hotels and utility companies are properly reporting and submitting the required taxes.

Condition:

Although Finance staff are maintaining a spreadsheet for tracking TOT payments each fiscal year, there does not appear to be anyone checking the TOT returns for accuracy, or keeping track of delinquencies. It also does not appear that the City is requiring the hotels to submit supporting documentation for exemptions. In addition, there have been no recent audits of the hotels. The Finance staff prepared a spreadsheet for tracking UUT payments for 2014-15, but apparently stopped tracking this revenue for amounts received after June 30, 2015. Though it resumed in fiscal year 2016-17.

Cause:

Turnover and lack of City staff; lack of accounting policies and procedures.

Effect:

Hotels and utility companies could be underreporting these taxes with no consequences, resulting in lower revenues to the City.

Recommendation:

We recommend the City establish stronger controls and oversight for these revenues and possibly schedule "audits" of the hotels and/or utility companies.

Management's Response:

The current revenue percentages are in accordance with the City Ordinances. Currently TOT and UUT checklists are maintained that record the source, receipt date, amount, and reporting period to aid in the monitoring process. Any missing remittances triggers a late notice. Effective July 1, 2018, the City will charge late fees, but the City does not perform audit of the receipts. The City has four hotels in the City limits that pays TOT taxes and will start reviewing Airbnb.com options in FY18/19.

An internal audit function is a future consideration based on priorities, financial resources and staff availability. If an internal audit function is not available or sufficient, contracting with an external consultant can be considered if the potential recovery of revenues were greater than the cost of the consultant.

City of Beaumont
Report on Internal Control Related Matters Identified in an Audit (Continued)
For the Year Ended June 30, 2017

Findings:

Finding 2017-009 Lack of Oversight for Fuel Credit Card Activity

Criteria:

Policies should be established to provide detailed guidance on the allowable use of the City's fuel credit cards. In addition, effective monitoring and oversight should be established to ensure the fuel charges on the credit cards are reasonable.

Condition:

Each City vehicle has a fuel credit card inside the vehicle. The City has not established formal policies over the use of the fuel credit cards. In addition, there is no formal analysis of the fuel credit card use, on a periodic basis, to determine if the fuel costs are reasonable based on known operations of the vehicles.

Cause:

Lack of oversight by management and formal policies in this area.

Recommendation:

We recommend the City adopt formal policies providing detailed guidance on the allowable uses of the City's fuel credit cards. In addition, we recommend the City implement procedures to monitor the fuel activity, periodically, to analyze the use of the fuel credit cards. Also, City staff should be made aware of the monitoring and analysis of the fuel usage as an additional deterrent for misuse of the City fuel credit cards.

Management's Response:

Formal policies related to the use of fuel credit cards were drafted for discussion with the Finance and Audit committee on November 6, 2016. The Finance department worked with other departments to implement the policies for use of the fuel cards. Finance department is working with fuel vendors to limit administrative account access and improve monthly reporting.

Finding 2017-010 Overhead Cost Allocation

Criteria:

Cost allocation plan methodologies should be thoroughly documented for transparency purposes, and updates to the plans should be done periodically in accordance with best practices.

Condition:

The City allocates certain General Fund costs (administration, maintenance, etc.) to the Sewer Enterprise, Gas Tax, Transit Enterprise, and the Community Facilities District (CFD) Fund. The amounts are based on calculations included in schedules maintained by the Finance Department.

Cause:

The City does have a formal cost allocation plan to allocate internal costs.

City of Beaumont
Report on Internal Control Related Matters Identified in an Audit (Continued)
For the Year Ended June 30, 2017

Findings:

Finding 2017-010 Overhead Cost Allocation (Continued)

Effect:

The City could potentially be utilizing allocation methods which result in either less administrative costs or excessive administrative costs being allocated than would be allowable if detailed cost allocation studies were performed on a periodic basis, and in accordance with federal grant requirements. Currently the City is not allocating any indirect costs to federal (or state) grants.

Recommendation:

We recommend the City perform a full cost allocation study of administrative costs to ensure the detailed methodology for the allocation of administrative costs is reasonable and appropriate, based on the current circumstances, and that the methodology is clearly defined and documented.

Management's Response:

A consultant was hired to develop an informal cost allocation plan that the City has implemented. A complete cost allocation plan with policies and procedures is being finalized and will be fully implemented in fiscal year 2018/19. Fiscal year 2016/17 did not have federal expenditures in excess of the single audit threshold. However, 2017/18 could exceed that threshold but the analysis has not been completed at this time. Without a complete overhead cost allocation plan, the costs charged to any federal programs will be only the fully supported direct costs. The results of the review will be used to identify any potential impact to the various funds.

Finding 2017-011 Segregation of Duties for Cash Receipts – Police Department

Criteria:

In a strong internal control environment, manual receipts should be used in very limited situations; when used, strong controls over the numerical sequence should be established to ensure completeness of the receipts issued.

Condition:

Dispatchers at the Police Department can accept payment by check or cash after hours. Manual receipts are being issued to customers upon payment. The copy of the manual receipt and the cash and checks are then provided to the Customer Service Coordinator; however, the Customer Service Coordinator is not keeping track of the numerical sequence of the manual receipts that are being issued.

Cause:

The City does not track the numerical sequence of the manual receipts that are being issued for cash being received through the Police Department.

City of Beaumont
Report on Internal Control Related Matters Identified in an Audit (Continued)
For the Year Ended June 30, 2017

Findings:

Finding 2017-011 Segregation of Duties for Cash Receipts – Police Department (Continued)

Effect:

Receipts and payments could be collected and not properly recorded in the City's general ledger and ultimately deposited into the City's bank account.

Recommendation:

We recommend the City implement procedures for the Customer Service Coordinator to verify the numerical sequence of the manual receipts issued by the Dispatchers at the Police Department that are accepting payments by check or cash after-hours. In addition, the City's policy over cash receipts as currently written does not appear to include the remote location cash collection processes. We recommend that the policy be updated to encompass both central cashiering and all remote cashiering locations.

Management's Response:

Policies and procedures were implemented and approved after the audit period ending June 30, 2017. In addition, strict requirements for manual receipts during off hours are enforced with only one active receipt book. Finance staff perform random internal audit of the public safety cash drawer, which includes review of the after-hours receipt book. Formal policies related to after-hours receipts are being drafted for that location and will be in place in August 2018.

Finding 2017-012 Segregation of Duties for Bus Passes

Criteria:

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.

Condition:

City employees that issue bus passes are also responsible for collecting and receipting payments from customers into the City's cash receipts system. Inventory controls over the numeric sequence of bus passes should be established and controlled.

Cause:

The City did not appropriately design its internal controls to segregate the duties between those with access to the recording of payments from customers and the ability to issue bus passes.

Effect:

Bus passes could be issued without a corresponding cash receipt being recorded in the City's general ledger and ultimately deposited into the City's bank account.

City of Beaumont
Report on Internal Control Related Matters Identified in an Audit (Continued)
For the Year Ended June 30, 2017

Findings:

Finding 2017-012 Segregation of Duties for Bus Passes (Continued)

Recommendation:

Though the City had established centralized tracking and reporting during fiscal year 2016/17, the finding and recommendation was not fully implemented at the transit department during our audit period. We recommend the City continue to implement the corrective actions it had identified previously.

Management's Response:

Pre-numbered books are obtained for RTA transit passes and the Transit department is now tracking those books to determine that all revenues have been recorded. City Transit passes are color coded on a monthly basis with a specific stamp identifier which also changes each month. Tracking systems were put in place during fiscal year 2017/18 at the transit department and the tracking system had been in place at City Hall by the end of fiscal year 2016/17. The tracking system was developed by the Transit Department in order to identify bus passes issued to cashiers and bus drivers for sale. The passes issued are counted by the Transit Department staff and the sales are then verified.

City of Beaumont
Report on Internal Control Related Matters Identified in an Audit (Continued)
For the Year Ended June 30, 2017

Status of Prior Year Findings:

2016-1 Policies and Procedures

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.

Status of Management's Corrective Action:

Accounting Policies and Procedures – Not implemented during audit period. See Finding 2017-01 and -02. Policies were adopted in January 2018 after audit period.

Appropriate Level of Unrestricted Fund Balance in General Fund – Implemented. A policy of target reserve balances was established with FY16-17 City budget.

Debt Management Policy – Not implemented during audit period. See Finding 2017-02. A formal Debt Management policy was adopted as part of the Financial Management Policies in January 2018 after audit period.

Fraud Prevention and Detection Policy – Not implemented during audit period. See Finding 2017-03. Though management instituted a fraud training program on prevention and detection before the end of fiscal year 2016-2017, some employees were still unaware of the policy during our interviews.

Capital Assets – Implemented. Fixed Asset Policies and Capital Improvement Policies were adopted by City Council on September 20, 2016. A City-wide street assessment was performed, and an asset tag and inventory was performed by outside contractors. Land and structural inventory was completed prior to the end of the audit period. The data obtained from those engagements was provided to an outside third-party consultant. The consultant was engaged for purposes of valuing and reporting the infrastructure and other capital assets for the audit period ended June 30, 2017 which resulted in an asset report for the fiscal year ended June 30, 2017, and the general ledger conformed with the GASB standards for City governmental capital asset reporting.

2016-2 Accounting Records and Financial Reporting

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 provisions 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.

City of Beaumont
Report on Internal Control Related Matters Identified in an Audit (Continued)
For the Year Ended June 30, 2017

Status of Prior Year Findings:

2016-2 Accounting Records and Financial Reporting (Continued)

Status of Management's Corrective Action:

Partially implemented. See Finding 2017-001.

2016-3 Segregation of Duties for Cash Receipts – City Hall

Recommendation:

We recommend the City implement procedures for the Accounting Technician to obtain reports directly from the Incode cash receipts program and establish a process to track and monitor the number of voided transactions from various cashiers.

Status of Management's Corrective Action:

Partially implemented. See Finding 2017- 004.

2016-4 Segregation of Duties for Cash Receipts – Police Department

Recommendation:

We recommend the City implement procedures for the Customer Service Coordinator to verify the numerical sequence of the manual receipts issued by Dispatchers that collect cash and checks after-hours.

Status of Management's Corrective Action:

Not implemented during audit period. See Finding 2017-011. Only one cash book is currently being used and employees are now following the policies and procedures adopted in January 2018.

2016-5 Segregation of Duties for Cash Receipts – Community Pool

Recommendation:

We recommend the City maintain an appropriate level of inventory for the register tape ink to ensure proper reconciliation can be performed on a daily basis.

Status of Management's Corrective Action:

Implemented. However, policy as currently written does not appear to include the remote location cash collection processes. Recommend that the policy be updated to encompass both central cashiering and remote cashiering locations.

City of Beaumont
Report on Internal Control Related Matters Identified in an Audit (Continued)
For the Year Ended June 30, 2017

Status of Prior Year Findings:

2016-6 Segregation of Duties for Business Licenses

Recommendation:

We recommend the City implement a procedure to generate reports from the HdL business license program, periodically (daily, weekly, monthly), and have someone independent of the business license issuance and collection functions review and reconcile the amounts from these reports to the revenues posted in the City's general ledger.

Status of Management's Corrective Action:

Not implemented during audit period. See Finding 2017-007.

2016-7 Segregation of Duties for Building Permits

Recommendation:

We recommend the City implement a procedure to generate reports from the Salesforce permit system, periodically (daily, weekly, monthly), and have someone independent of the permit issuance and collection functions review and reconcile the amounts from these reports to the revenues posted in the City's general ledger.

Status of Management's Corrective Action:

Not implemented during audit period. See Finding 2017-005. Building permit system is being integrated with the software upgrade currently in progress. The full implementation was completed and placed in operation during fiscal year 2017-18. An internal control will be developed for the finance department to reconcile building permits to the building permit receipts to ensure they are being properly recorded and classified.

2016-8 Segregation of Duties for Bus Passes

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.

Status of Management's Corrective Action:

Partially implemented. See Finding 2017-012. Tracking systems were put in place during fiscal year 2017/18 at the transit department to include pre-numbered books for RTA transit passes and the Transit department is now tracking those books to determine that all revenues have been recorded. City Transit passes are color coded on a monthly basis with a specific stamp identifier which also changes each month. The tracking system had been in place at City Hall as of June 30, 2017. Inventory of bus passes and accountability for bus pass sales is being reviewed currently between the finance office and transit office. A tracking system is being developed to ensure that all revenues are properly captured and recorded, and that there is accountability for all of the passes.

City of Beaumont
Report on Internal Control Related Matters Identified in an Audit (Continued)
For the Year Ended June 30, 2017

2016-9 Transient Occupancy Tax (TOT) and Utility User's Tax (UUT)

Recommendation:

We recommend the City establish stronger controls and oversight for these revenues and possibly schedule "audits" of the hotels and/or utility companies.

Status of Management's Corrective Action:

Partially implemented. See Finding 2017-008.

2016-10 Development Impact Fees (DIF)

Recommendation:

The City should establish formal policies regarding the billing and collection of DIF, to ensure the billing of the DIF is subject to oversight and review, and that the City Council's approved fees are being accurately and consistently assessed, collected and recorded. The City should consider replacing the current manual system with a more automated system, in which fees cannot be billed and collected without Finance's knowledge. The calculation of the DIF and application of fee credits should be subjected to independent analysis and oversight.

Status of Management's Corrective Action:

Partially implemented. See Finding 2017- 006. During FY16/17 the City began performing the monthly reconciliation s manually. Now the City performs the reconciliation in the first week after month end. The permit and fees process will be integrated into the accounting software during fiscal year 2017-2018. The software integration is not fully functional yet, but is expected to be completed soon. Once full implementation has been completed, manual tracking can be replaced with an internal audit step for the finance department to ensure that all DIF receipts are being properly recorded and tracked.

2016-11 Lack of Competitive Bidding for Vendor Contracts and Purchases

Recommendation:

It should be noted, current City staff, management, and City Council have implemented purchasing policies and procedures and updated the City's Municipal Code to provide for greater transparency and detailed guidance over the purchasing function during the fiscal year ended June 30, 2016. In July 2015, the City adopted Ordinance 1060 which provides detailed guidance regarding the procedures to be followed when procuring professional services. Our recommendation is to continue to monitor the purchasing policies and procedures to ensure they are properly implemented and used throughout the City for all major contracts and purchases.

City of Beaumont
Report on Internal Control Related Matters Identified in an Audit (Continued)
For the Year Ended June 30, 2017

Status of Prior Year Findings:

2016-11 Lack of Competitive Bidding for Vendor Contracts and Purchases (Continued)

Status of Management's Corrective Action:

Implemented. Competitive bidding for vendor contracts and purchases has already been added to the City Ordinances and City employees have followed the process since July 2015. Additional refinement of the Ordinances was submitted to and approved by City Council on November 21, 2017.

2016-12 Lack of Controls over Payroll

Recommendation:

Procedures should be implemented to ensure sufficient oversight and review by someone independent of the payroll function. We recommend the individual responsible for review and oversight of the payroll function obtain payroll reports directly from the payroll system, compare preliminary and final payroll reports, generate an audit trail report each pay period and reconcile all changes made to applicable supporting documentation. In addition, we recommend physical payroll checks be held and distributed by an individual outside of the payroll processing function.

Status of Management's Corrective Action:

Implemented and operating partially throughout the audit period. Payroll has several levels of approval and oversight prior to the submission of data to the third-party preparer. Hours are approved through the software by applicable Directors or Managers, which then releases that data to the payroll preparer. For staff not utilizing the hourly software, reports are provided to the payroll preparer that contain the appropriate approvals and other documentation. Any changes to status or other adjustments are documented with the approval of the Director of Administration. Additional procedures for review and approval after the checks and reports are received from the third-party preparer have been implemented.

2016-13 Lack of Controls over Accrued Vacation

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.

City of Beaumont
Report on Internal Control Related Matters Identified in an Audit (Continued)
For the Year Ended June 30, 2017

Status of Prior Year Findings:

2016-13 Lack of Controls over Accrued Vacation (Continued)

Status of Management's Corrective Action:

Implemented. Reports are provided to Directors monthly to review their staff's accrued vacation balances and amounts earned and taken. Human Resources keeps strict control over banked balances and notifies staff when a problem occurs.

2016-14 Lack of Oversight for Fuel Credit Card Activity

Recommendation:

We recommend the City adopt formal policies providing detailed guidance on the allowable uses of the City's fuel credit cards. In addition, we recommend the City implement procedures to monitor the fuel activity, periodically, to analyze the use of the fuel credit cards. Also, City staff should be made aware of the monitoring and analysis of the fuel usage as an additional deterrent for misuse of the City fuel credit cards.

Status of Management's Corrective Action:

Partially implemented. Not implemented throughout the audit period. See Finding 2017-009. All fuel cards were re-issued in November 2016, and each card is issued to a specific vehicle. When a vehicle is fueled, the odometer reading is input into the pump. The end of month fuel invoice includes a card summary report with the date, number of gallons, odometer reading, and dollar amount of each transaction. The issued cards are audited from time to time. New cards can be issued by the Director of Administration, Director of Finance, or one specifically authorized finance department staff person.

Formal policies related to the use of fuel credit cards were drafted for discussion with the Finance and Audit committee on November 6, 2016. The Finance department worked with other departments to implement the policies for use of the fuel cards. Finance department is working with fuel vendors to limit administrative account access and improve monthly reporting.

2016-15 Overhead Cost Allocation

Recommendation:

We recommend the City perform a full cost allocation study of administrative costs to ensure the detailed methodology for the allocation of administrative costs is reasonable and appropriate, based on the current circumstances, and that the methodology is clearly defined and documented.

Status of Management's Corrective Action:

Not implemented. See Finding 2017-010. An informal overhead cost allocation plan was prepared by an outside consultant. However the City has not yet created and documented a complete cost allocation plan with policies and procedures.