

CITY OF FORT BRAGG
MANAGEMENT REPORT
AND
AUDITOR'S COMMUNICATION LETTER

June 30, 2013

CITY OF FORT BRAGG
June 30, 2013

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February 4, 2014

Members of the City Council
City of Fort Bragg
416 N. Franklin Street
Fort Bragg, CA 95437

In planning and performing our audit of the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Fort Bragg (City), as of and for the fiscal year ended June 30, 2013, 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 our auditing procedures 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 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. However, as discussed below, we identified certain deficiencies in internal control that we consider to be significant deficiencies.

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 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 did not identify any deficiencies in internal control that we consider 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 deficiencies presented in the current year recommendations section as Findings 2013-01 through 2012-03 to be significant deficiencies in internal control.

During our audit we noted certain other matters involving internal controls and their operations, and are submitting for your consideration, related recommendations designed to help the City make improvements and achieve operational efficiencies. These recommendations are described in the current year recommendations section as Findings 2013-04 through 2013-11. Our comments reflect our desire to be of continuing assistance to the City.

The City's written responses to the findings identified in our audit are described in the current year recommendations section. We did not audit the City's responses and, accordingly, we express no opinion on them. In addition, we would be pleased to discuss the recommendations in further detail at your convenience, to perform any additional study of these matters, or to assist you in implementing these recommendations.

We have included in this letter a summary of communications with the members of the City Council as required by professional auditing standards. We would like to thank the City's management and staff for the courtesy and cooperation extended to us during the course of our engagement. The accompanying communications and recommendations are intended solely for the information and use of the City Council of the City and management of the City and is not intended to be and should not be used by anyone other than these specified parties.

Moss, Levy & Hartzheim

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Culver City, California



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February 4, 2014

Members of the City Council
City of Fort Bragg
416 N. Franklin Street
Fort Bragg, CA 95437

We have audited the financial statements of the governmental activities, business-type activities, each major fund, and the aggregate remaining fund information of the City of Fort Bragg (City) for the fiscal year ended June 30, 2013. Professional standards require that we provide you with the information about our responsibilities under auditing standards generally accepted in the United States of America, *Government Auditing Standards*, and OMB Circular A-133, as well as certain information related to the planned scope and timing of our audit. We have communicated such information in our letter to you dated July 22, 2013. Professional standards also require that we communicate to you the following information related to our audit.

Significant Audit Findings

Qualitative Aspects of Accounting Practices

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by the City are described in Note 1 to the basic financial statements. As discussed in Note 1 of the notes to the basic financial statements, four new accounting policies were adopted during the fiscal year. The new policies are Governmental Accounting Standards Board (GASB) Statements No. 60, 61, 62, and 63. Only GASB Statement No. 63 had an effect on the financial statements. See Note 1.G.8 for the effect on the financial statements. We noted no transactions entered into by the City during the fiscal year for which there is a lack of authoritative guidance or consensus. All significant transactions have been recognized in the financial statements in the proper period.

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimates affecting the financial statements were:

Management's estimates included the funding progress of CalPERS, the estimated historical cost and useful lives of capital assets, and the assumptions used for estimating the other postemployment benefits liability. These estimates are based on CalPERS' actuarial estimates, historical data and industry guidelines for capital assets, and consultant's estimates for postemployment benefits payable. We evaluated the key factors and assumptions used to develop the estimates above in determining that they are reasonable in relation to the financial statements taken as a whole.

The financial statement disclosures are neutral, consistent, and clear.

Difficulties Encountered in Performing the Audit

We encountered no difficulties in dealing with management in performing and completing our audit.

Corrected and Uncorrected Misstatements

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management. Management has corrected all such misstatements. In addition, one of the misstatements detected as a result of audit procedures and corrected by management was material, either individually or in the aggregate, to the financial statements taken as a whole. The adjustment was to reclassify certain revenues to unearned revenue.

Disagreements with Management

For purposes of this letter, a disagreement with management is a financial accounting, reporting, or auditing matter, whether or not resolved to our satisfaction, that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

Management Representations

We have requested certain representations from management that are included in the management representation letter dated February 4, 2014.

Management Consultations with Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the City's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Other Audit Findings or Issues

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the City's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

Other Matters

With respect to the supplementary information accompanying the financial statements, we made certain inquiries of management and evaluated the form, content, and methods of preparing the information to determine that the information complies with accounting principles generally accepted in the United States of America, the method of preparing it has not changed from the prior period, and the information is appropriate and complete in relation to our audit of the financial statements. We compared and reconciled the supplementary information to the underlying accounting records used to prepare the financial statements or to the financial statements themselves.

This information is intended solely for the use of the City Council and management of the City and is not intended to be and should not be used by anyone other than these specified parties.

Very truly yours,

Moss, Levy & Hartzheim

MOSS, LEVY & HARTZHEIM, LLP
Culver City, CA

CURRENT YEAR RECOMMENDATIONS

Significant Deficiencies

2013-01 Finding – Deficiencies in internal control over cash registers:

During our audit of the City's cash receipt system, we noted that the finance cash register is not assigned to one employee; and there are numerous employees who can access the register. Also, in the police department, there are two employees who can access the cash register.

Effect:

Lack of controls over handling of cash registers can increase the risk of a misappropriation of funds.

Recommendation:

We recommend that the City implement policies and procedures to ensure that a proper cash receipts system is in place. Each person who has access to the cash register should have his/her own cash register drawer, which is reconciled by a different employee.

Management's Response:

As noted in the June 30, 2010, June 30, 2011 and June 30, 2012 Management Report responses, individual cash drawers are not practical due to the limited number of employees in the Finance Department and in the front office of the Police Department. Cash procedures include verification of all cash transactions by at least two employees then all transactions, summaries, and deposits are verified by the Finance Director and the Assistant City Manager.

2013-02 Finding – Lack of disaster recovery plan:

During our review of internal control, we noted that the City lacks a disaster recovery plan.

Effect:

Important data may be lost during natural disasters or other catastrophic events.

Recommendation:

We recommend that the City implement a disaster recovery plan as soon as possible, to prevent the loss of important information.

Management's Response:

The Information Technology department has prepared a draft disaster recovery plan, which is in the review stage. We anticipate that the plan will be finalized before the end of calendar year 2014.

2013-03 Finding – Deficiencies in internal control over cash receipts:

During our test of cash receipts, we noted the following:

- a) One business license was unpaid, yet the business was still operating.
- b) Four bank deposits were not deposited on a timely basis.
- c) Numerous planning payments for building permit related fees did not have the application and other supporting documentation retained in the property file.

Effect:

Deficiencies in the internal control over cash receipts can increase the risk that errors and irregularities occur and go undetected. It adversely affects the City's ability to initiate, authorize, record, process, or report financial data reliably, which can lead to a misappropriation of funds. Also, businesses that are operating without a business license are not in compliance with the City's Municipal Code.

CURRENT YEAR RECOMMENDATIONS

Significant Deficiencies (Continued)

Recommendation:

We recommend that the City implement stronger controls over business license payments to ensure that all businesses have paid licenses on file. We also recommend that receipts be processed and deposited on a timely basis, and the Planning department should retain all supporting documents for building permit related payments, for future verification.

Management's Response:

- a) Business licenses will be reviewed monthly for unpaid licenses. These will be processed according to the City Municipal Code.
- b) Bank deposits are taken to the bank daily.
- c) Established procedures for retaining the proper planning and payment documentation in the property file have been reviewed with Finance and Community Development employees.

Other Matters

2013-04 Finding – Lack of written fraud reporting policy:

During our review of policies and procedures, we noted that there was no formal written fraud reporting policy.

Effect:

Without a formal fraud reporting policy, employees are less likely to report suspected fraud.

Recommendation:

We recommend the City draft and implement a formal written fraud reporting policy.

Management's Response:

A policy was implemented on October 1, 2013 as City Administrative Regulation F-1.

2013-05 Finding – Disposal of obsolete items at the corporation yard:

During our visit to the corporation yard, we noted that there were numerous miscellaneous and obsolete items being stored, including golf clubs, furniture, automobile wheels, old electronics, and road supplies.

Effect:

Idle and obsolete items are of no benefit to the City and could be sold to generate additional revenue. Also, idle and obsolete items are more likely to be absconded and go undetected.

Recommendation:

We recommend the City sell/dispose of all personal and obsolete items at the corporation yard.

Management's Response:

The City concurs with the comment and will dispose of or sell excess items from the City's corporation yard in a timely manner.

2013-06 Finding – Deficiency in journal entry approval:

During our test of adjusting journal entries, we noted that one adjusting journal entry was prepared and approved by the same employee.

CURRENT YEAR RECOMMENDATIONS

Other Matters (Continued)

Effect:

By having the same employee prepare and approve adjusting journal entries, it exposes the City to an increased risk of fraud and a misappropriation of funds.

Recommendation:

We recommend that the City have different employees prepare and approve adjusting journal entries

Management's Response:

Finance has implemented procedures to ensure that journal entries are not approved by the employee preparing the entry.

2013-07 Finding – No written policy on reversal of late fees:

During our review of accounting policies, we noted that there is no policy for reversal of late fees on utility customer accounts.

Effect:

The lack of a policy for reversal of late fees can lead to the inconsistent application of internal policies.

Recommendation:

We recommend the City to establish a policy for reversal of late fees.

Management's Response:

A policy has been drafted and will be incorporated into the City Administrative Regulations upon approval.

2013-08 Finding – Lack of "Notice to Proceed" for a construction project:

During our audit fieldwork, we noted that there was no "Notice to Proceed" issued for the 2013 Street Resurfacing Project #2013-01 to Intermountain Slurry Seal, Inc.

Effect:

Without a "Notice to Proceed" there is no official notification to the contractor to state the project or official notice that the construction contract was awarded.

Recommendation:

We recommend that the City issue a notice to proceed prior to the start of each construction project.

Management's Response:

The omission of a Notice to Proceed for this particular project was an unusual and accidental oversight. The City's Public Works Department will review, and revise as necessary, its contracting procedures to ensure such an incident does not occur in the future.

CURRENT YEAR RECOMMENDATIONS

Other Matters (Continued)

2013-09 Finding – Deficiencies in internal control over cash disbursements:

During our test of cash disbursements, we noted the following:

- a) Three receiving reports were not obtained/retained (Check #s 68797, 69424, and 69470)
- b) One voided check did not have the signature portion removed (Check # 70075)
- c) One invoice was not stamped “paid” (Check #69424)

Effect:

A deficiency in internal control increases the risk that errors and irregularities may occur and go undetected. It adversely affects the City’s ability to initiate, authorize, record, process, or report financial data reliably, which can lead to a misappropriation of funds. Also, the lack of receiving reports allows for the possibility of paying for materials not received or not received in satisfactory condition. Without the signature portion of a voided check being removed, there is a possibility that the voided check could be re-used. In addition, a lack of a “paid” stamp noted on a paid invoice increases the chances that the invoice could be paid more than once.

Recommendation:

We recommend the following:

- a. The City should obtain/retain receiving reports for all disbursements for goods
- b. The City should ensure that the signature portion be removed from all voided checks.
- c. All paid invoices be stamped “paid”.

Management’s Response:

Established procedures for voiding checks have been reviewed with all Finance Department employees. We have communicated to all managers the importance of reconciling the packing slip to the invoice and forwarding all packing slips to Finance with the invoice.

2013-10 Finding – Stale dated checks on June 2013 bank reconciliation:

During our audit of cash, we noted that as of June 30, 2013, there are outstanding checks over one year old on the bank reconciliation, totaling \$1,325.46.

Effect:

Bank reconciliations that contain stale dated checks may have incorrect balances since the stale dated checks have not been investigated. When the City does not resolve reconciling items timely, there is an increased risk of errors and irregularities going undetected.

Recommendation:

We recommend that the City research these outstanding stale dated checks to determine if they need to be reissued or sent to the State of California as escheat property.

Management’s Response:

All outstanding checks over one year old have been researched and either reissued or will be published in the newspaper at the proper time.

2013-11 Finding – Lack of clarity regarding vacation accruals in Memorandum of Understanding:

During our review of compensated absences, we noted that the Memorandum of Understanding (MOU) is unclear in regards to the accrual of vacation hours based on years of employment.

CURRENT YEAR RECOMMENDATIONS

Other Matters (Continued)

Effect:

Unclear wording in MOUs could lead to incorrect vacation accrual balances and payout of such hours, which results in over/under payments to employees.

Recommendation:

We recommend the City update the MOU to clarify the accrual of vacation hours based on years of employment.

Management's Response:

As the MOUs come up for negotiation, the vacation accrual language will be discussed and clarified.

STATUS OF PRIOR YEAR RECOMMENDATIONS

Significant Deficiencies

2012-01 Finding – Deficiencies over inventory controls and valuation:

During our review of inventory, we noted that there was no complete count of inventory performed at the Corporation Yard. In addition, the value of the inventory at the Corporation Yard was based on current pricing of the inventory items instead of historical cost.

Effect:

Without proper inventory safeguarding and an adequate inventory count, a misappropriation of assets is more likely to occur and go undetected. Also, incorrect valuations of inventory could lead to a misstatement in the financial statements.

Recommendation:

We recommend that the City ensure that all inventory be properly accounted for and valued at historical costs during the year-end inventory count.

Status:

Implemented

2012-02 Finding – Deficiencies in internal control over cash registers:

During our audit of the City's cash receipt system, we noted that the finance cash register is not assigned to one employee; and there are numerous employees who can access the register. Also, in the police department, there are two employees who can access the cash register.

Effect:

Lack of controls over handling of cash registers can increase the risk of a misappropriation of funds.

Recommendation:

We recommend that the City implement policies and procedures to ensure that a proper cash receipts system is in place. Each person who has access to the cash register should have his/her own cash register drawer, which is reconciled by a different employee.

Status:

Not implemented, see Finding #2013-01.

2012-03 Finding – Lack of disaster recovery plan:

During our review of internal control, we noted that the City lacks a disaster recovery plan.

Effect:

Important data may be lost during natural disasters or other catastrophic events.

Recommendation:

We recommend that the City implement a disaster recovery plan as soon as possible, to prevent the loss of important information.

Status:

Not implemented, see Finding #2013-02

2012-04 Finding – Control deficiencies in the Finance Department relating to cash receipts:
During our audit, we noted that there is no receipt given by the Finance Department to the Police Department when the Police Department brings over the weekly cash receipts.

Effect:

When a lack of receipts exists, there is an increased risk of misappropriation of funds.

Recommendation:

We recommend that the Finance Department issue receipts when they receive the weekly cash receipts.

Status:

Implemented

2012-05 Finding – Lack of segregation of duties for Accounts Payable:

During our audit, we noted that the accounts payable check preparer is also responsible for handling checks after printing and mailing to vendors.

Effect:

The lack of segregation of duties significantly increases the chance of an error or irregularity going undetected and increases a risk of misappropriation of funds.

Recommendation:

We recommend that these functions be segregated among other employees to safeguard the assets of the City.

Status:

Implemented

2012-06 Finding – Deficiency in internal control over payroll:

During our test of payroll, we noted that two timesheets lacked supervisors' signatures.

Effect:

Without the approval of timesheets by supervisors, there may be an increased risk of misappropriation of funds.

Recommendation:

We recommend that the City make sure supervisors approve all timesheets.

Status:

Implemented

Other Matters

2012-07 Finding – Duplicate payment for the Caspar 2005 COP:

During our audit, we noted that a duplicate payment was made for the Caspar 2005 COP liability in November 2011 for \$73,784.51.

Effect:

The debt service payment was made six months prior to its due date, resulting in a loss of investment income.

Recommendation:

We recommend that the City make all debt service payments as close to their due dates as possible.

Status:

Implemented

2012-08 Finding – Deficiencies in internal control over cash disbursements:

During our test of cash disbursements, we noted the following deficiencies:

- 1) Five receiving reports were not obtained/retained (Check No.: 65608, 65854, 66110, 66232, and 66461)
- 2) Two invoices lacked approvals (Check No. 65854 and 66232, both Office Depot)
- 3) One check selected did not reconcile between the check register and actual check (Check No. 66113)
- 4) One reimbursement request was not stamped “paid” (Check No. 66113)
- 5) Two invoices were coded to the wrong expenditure accounts (Check No. 65809 and 66098).

Effect:

The lack of receiving reports allows for the possibility of paying for materials not received or not received in satisfactory condition. Also, the City established procedures of approving invoice requests and stamping invoices “paid,” in order to minimize the risk of misappropriation of funds. However the procedures were not followed consistently. In addition, if invoices are coded to the incorrect expenditure account, the City’s Financial Statements may be misstated.

Recommendation:

We recommend that there is an increased effort by City staff to follow the established procedures over cash disbursements.

Status:

Partially implemented, see Finding #2013-09.

2012-09 Finding – Bank reconciliation not properly approved:

During our audit of cash, we noted that there were no preparer or reviewer signatures on the June 2012 bank reconciliation.

Effect:

The proper review of bank reconciliations ensures that bank reconciliations are accurate and reconcile to the general ledger. Without proper review, there is no assurance that bank reconciliations are accurate.

Recommendation:

We recommend that bank reconciliations be reviewed by a responsible employee after they are prepared.

Status:

Implemented.

2012-10 Finding – No annual verification of capital assets:

During our audit of capital assets, we noted that there is no annual verification that capital assets still exist or if their values are impaired.

Effect:

If there is no verification that capital assets still exist or assessment of impairment, the City's capital assets may be overstated.

Recommendation:

We recommend that the City establish a policy of reviewing capital assets on an annual basis, for existence and possible impairment.

Status:

Implemented

2012-11 Finding – No written policy on reversal of late fees:

During our review of accounting policies, we noted that there is no policy for reversal of late fees on utility customer accounts.

Effect:

The lack of a policy for reversal of late fees can lead to the inconsistent application of internal policies.

Recommendation:

We recommend the City to establish a policy for reversal of late fees.

Status:

Not implemented, see Finding #2013-07

2012-12 Finding – Outstanding checks on June 30, 2012:

During our audit of cash, we noted that as of June 30, 2012, there are outstanding checks over one year old on the Wells Fargo bank reconciliation.

Effect:

Tracking outstanding checks is an important control that ensures that all outgoing checks are accounted for.

Recommendation:

We recommend that the City research these outstanding checks to determine if they need to be reissued or published in the newspaper.

Status:

Not Implemented, see Finding #2013-10.