

INDEPENDENT AUDITORS' 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 City Council  
City of Carson  
Carson, 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 governmental activities, the business-type activity, each major fund, and the aggregate remaining fund information of the City of Carson, California (the City), as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise the City's basic financial statements and have issued our report thereon dated February 28, 2016.

**Internal Control over Financial Reporting**

In planning and performing our audit of the financial statements, we considered the City'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 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 described below, we identified certain deficiencies in internal control that we consider to be material weaknesses and 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.

## **Internal Control over Financial Reporting (Continued)**

### **Material Weaknesses**

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 City's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the following deficiencies in internal control to be material weaknesses.

#### ***Successor Agency Assets***

##### **Auditors' Comment**

We noted that the City was still reporting capital assets and new construction in progress activity in the Successor Agency to the Dissolved Redevelopment Agency Private-Purpose Trust Fund that are considered to be for governmental purposes. In addition, we noted several loans receivable from developers that should be offset by an allowance for uncollectible amounts since the repayment terms involve forgiveness clauses or no set schedule for repayment other than a lump sum due at the end of a long-term period. This private-purpose trust fund is being used to account for the winding down of the affairs of the City's former redevelopment agency which involves converting noncurrent assets, which the California State Department of Finance has determined not to have a specific governmental use, to cash and paying off outstanding debt of the former redevelopment agency. Assets identified and approved as governmental-use assets should have been transferred to the City. New construction activity should not be accounted for in this fund. Allowances for uncollectible loans receivable should be recorded to fairly state the long-term loans receivable. As a result, material adjustments were made to transfer the government-use assets and construction in progress to the City and record allowances against the loans receivable. We recommend that management establish procedures to review transactions involving the Successor Agency to ensure that they are properly recorded.

##### **Management's Response**

We agree with the finding. New construction will no longer be recorded in the Private-Purpose Trust Fund. When any future long-term loans are made, the terms of repayment will be reviewed to determine whether an allowance for uncollectable loans should be recorded. In addition to providing immediate instruction to the Accounting staff, the Director of Finance and Accounting Manager will review Successor Agency transactions at midyear and year-end to ensure proper recording.

#### ***Carson Reclamation Authority Reporting and Accounting***

##### **Auditors' Comment**

We noted that the Carson Reclamation Authority (the Authority), which was formed in the prior fiscal year, was not reported as a component unit in the City's prior year financial statements. In accordance with generally accepted accounting principles, the Authority met the definition of a blended component unit since the City is able to impose its will on this entity and this entity's services almost exclusively benefit the City. As a result, the Authority was included in the current year financial statement. The next time the City creates a new entity, we recommend that management review the authoritative guidance related to potential component units in order to determine the appropriate financial statement reporting requirements for that new entity.

## **Internal Control over Financial Reporting (Continued)**

### **Material Weaknesses (Continued)**

#### ***Carson Reclamation Authority Reporting and Accounting (Continued)***

##### **Auditors' Comment (Continued)**

In addition, we noted that land and inventory was contributed to the Authority in the prior year, however, no amounts were recorded on the general ledger. Generally accepted accounting principles require that contributed assets be recorded at their estimated acquisition values as of the date of contribution. As a result, material adjustments were made to record an estimated value for these assets. We recommend that the City establish procedures to identify contributed assets and properly value and record them. In addition, we recommend that the City establish controls, procedures, and periodic reporting to monitor the changes in the contributed inventory, including periodic physical inventory observations performed no less frequently than annually.

##### **Management's Response**

We agree with the finding. In addition to providing immediate instruction to the Accounting staff, the Director of Finance and Accounting Manager will meet with Community Development staff managing component unit activity, to review transactions at midyear and year-end to ensure proper recording.

#### ***Housing Authority Loans Receivable***

##### **Auditors' Comment**

We noted several Housing Authority loans receivable from developers and related accrued unpaid interest receivable that should have been previously offset by an allowance for uncollectible amounts, since the repayment terms involve no set schedule for repayment other than a lump sum due at the end of a long-term period. As a result, these loans receivable were materially overstated as previously reported in the government-wide financial statements. We recommend that management review the terms of new loans receivable and determine whether an allowance for uncollectible amounts should be recorded given the nature of the facts and circumstances surrounding the loans receivable to ensure that the loans receivable are fairly stated in financial reports.

##### **Management's Response**

We agree with the finding. When any future long-term loans are made, the terms of repayment will be reviewed to determine whether an allowance for uncollectable loans should be recorded. In addition to providing immediate instruction to the Accounting staff, the Director of Finance and Accounting Manager will review Housing Authority transactions at midyear and year-end to ensure proper recording.

## Internal Control over Financial Reporting (Continued)

### Material Weaknesses (Continued)

#### *Investment Policy*

##### Auditors' Comment

The City adopted a formal investment policy in December 2015. Based upon our testing of investment policy compliance, we noted a lack of supporting evidence that the City was in compliance with the following provisions:

- a) Article VI(C) and VI(F) state “The City Treasurer will periodically monitor the operating performance of all financial institutions holding City time deposits. Financial institutions must provide proof of collateralization by submitting third party trustee reports detailing securities that represent collateralization for city accounts on a monthly basis.”
- b) Article VI states “The City will not invest in securities maturing more than 5 years from the date of purchase.” The March 2016 investment report that we examined reported three California State bonds violating this provision, although they were purchased prior to the adoption of this investment policy.
- c) Article XI states “A list will be maintained of approved security broker/dealers selected by credit worthiness, adequate capitalization, and an agreement to abide by the conditions set forth in the City of Carson’s Investment Policy.” These conditions include supplying the City Treasurer with a list of 9 documents, contracts, etc. as also detailed within Article XI.
- d) Article XV states “The Treasurer shall render *monthly* investment reports to the Mayor, City Council, City Manager and Finance Director.” The first monthly report rendered appeared to be for March 2016, three months after the investment policy was adopted.

In addition, we noted the following provisions that need to be clarified:

- e) Article VI, Section D, Banker’s Acceptances, discusses a 10% maximum and a 30% maximum limit on the City’s moneys that may be invested in bankers’ acceptances and a 7 day term to maturity. In addition this section mentions that bankers’ acceptances shall be in compliance with Government Code Section 53601(g) which states, “Bankers’ acceptances otherwise known as bills of exchange or time drafts that are drawn on and accepted by a commercial bank. Purchases of bankers’ acceptances shall not exceed 180 days maturity or 40% of the agency’s moneys that may be invested pursuant to this section. However, no more than 30% of the agency’s moneys may be invested in the bankers’ acceptances of any one commercial bank pursuant to this section.”?
- f) Article VI, Section D, Local Agency Investment Fund, mentions both a \$65 million and a \$50 million limit?

We recommend that management review and update the investment policy to clear up any ambiguities and to consider modifications to what information is reported in the monthly investment reports. A good resource to assist with this task is the “Local Agency Investment Guidelines” publication produced by the California Debt and Investment Advisory Commission. Furthermore, we recommend that management establish policies and procedures to ensure that the City is gathering, maintaining, and reviewing the required information to be received from financial institutions holding City funds and approved security broker/dealers.

## **Internal Control over Financial Reporting (Continued)**

### **Material Weaknesses (Continued)**

#### ***Investment Policy (Continued)***

##### **Management's Response**

The City Treasurer has made some updates and improvements since fiscal year 2015-16. In addition, the City has retained a financial advisor to assist the City Treasurer with updates to the investment policy, monthly reports, and monitoring of investments and financial institutions.

#### ***Authorizations for Disbursements of Cash***

##### **Auditors' Comment**

During our testing of cash disbursements, we noted many instances where the person approving the invoice did so even though the amount of the disbursement exceeded their specific approval limits as set forth in the authorized signor listings provided to us. In addition, the Authorized Signor Listing that we received had not been updated recently and was not consistent with the electronic documentation of approvals in the City's accounting system. Furthermore, we noted a few instances where the authorized approval limit for an individual did not appear to be appropriate based on the individual's job titles/roles. Authorizations over procurements and disbursements are essential to ensuring assets are not misappropriated and are spent in accordance with the adopted budget. We recommend that the City implement controls whereby the authorized signor listings are reviewed for propriety and updated on an ongoing basis throughout the year. We further recommend these approval limits be consistent with those referenced in the accounting system.

##### **Management's Response**

We agree with the finding. Updated lists of authorization limits for requisition approval and invoice approval will be prepared prior to the end of fiscal year 2016-17. As part of the City's implementation of a new Enterprise Resource Planning system, workflow and security will be designed to enforce imposed limits.

## **Internal Control over Financial Reporting (Continued)**

### **Significant Deficiencies**

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 in internal control to be significant deficiencies.

#### ***Construction in Progress***

##### **Auditors' Comment**

An important part of financial reporting is ensuring the accuracy of capital asset classifications and appropriately estimating the use of those capital assets in the form of depreciation expense. We identified a certain project where construction was essentially completed and the assets had been placed in service during the year; however, the asset values had not been transferred from construction in progress to the appropriate capital asset classes and depreciation had not yet commenced on these capital assets. As a result, an adjusting entry was made to reclassify the completed project to its appropriate asset class and record current year depreciation expense. We recommend that the City assign a specific staff person with adequate skill, knowledge, and experience to monitor the status of the construction-in-progress projects throughout the year. As these projects are completed and placed in service, the assets should be transferred to the appropriate capital asset classifications, and depreciation of the capital assets should commence in accordance with the City's capitalization policies.

##### **Management's Response**

We agree with the comment. The Accounting division was relying on City Council approval of completed projects before transferring the project expenditures from Construction in Progress to the appropriate asset class. The Engineering staff will be provided with immediate instruction to identify when projects have been placed in service. The Accounting staff will be provided with immediate instruction to properly record the assets and begin depreciation.

## Internal Control over Financial Reporting (Continued)

### Significant Deficiencies (Continued)

#### *Segregation of Duties*

##### Auditors' Comment

One of the basic elements of internal control over financial reporting involves the segregation of duties in such a manner that the work of one employee is checked by others, and the responsibilities for custody of assets is not placed with the same employee that maintains the accounting records. Segregation of duties is not always possible. However, consideration should be given to implementing new checks and balances that would partially offset the internal control weaknesses. During our review and testing of controls over cash receipts, we noted the following situations where there is a lack of segregation of duties:

- a) A cashier has the ability to post cash receipts; has access to cut checks out of several Treasury accounts; is an authorized signor (checks are pre-printed with 2 electronic sigs, require 1 live signature); usually prints checks for each check run, and prepares the positive pay file for the bank. Furthermore, the cashier also prepares bank reconciliations for Parks and Recreation's bank account.
- b) A Treasurer's accountant prepares the bank reconciliation for Treasurers' Trust Account. The accountant also posts cash receipts, tracks all event deposits in a manual book, outside of the systems and general ledger. The accountant is responsible for controls over manual cash receipt carbon-copy booklets, and tracks these manually in a log, including tracking voids.

We recommend that management re-evaluate these staff persons' duties and determine whether any changes can be made and whether any mitigating controls can be implemented to minimize the control risk.

##### Management's Response

We agree with the finding. The Finance Department will work with the City Treasurer's Office to re-evaluate duties, make changes and implement mitigating controls as necessary.

## **Compliance and Other Matters**

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 instances of noncompliance that are required to be reported under *Government Auditing Standards* and which are described below.

### ***Compliance with Senate Bill 341***

#### Auditors' Comment

Senate Bill 341 (SB 341) requires all successor housing entities, beginning with the fiscal year ended June 30, 2014, to comply with annual report requirements within six months after the end of each fiscal year. The annual report must contain all of the required items as described in Health and Safety Code Section 34176.1 beginning with subsection (f) and must be posted to the successor housing agency's website. We noted that the City, in its capacity as the successor housing agency, has not prepared or posted to its website the required annual report for the fiscal year ended June 30, 2016. We recommend the City implement policies and procedures to ensure compliance with the required elements for SB 341.

#### Management's Response

We agree with the comment. Community Development staff are currently working with a consultant to prepare the SB 341 report for fiscal year 2015-16, and expect to have it completed and submitted by the end of March 2017.

### ***Late Budget Adoption***

As required by the provisions of Sections 2951 to 2954 of the City's Municipal Code, "on or before July 20th, the City shall adopt a balanced budget by the affirmative votes of at least three (3) members. Upon final adoption, the budget shall be in effect for the ensuing budget period and funds shall be appropriated for the fiscal year. From the effective date of the appropriation, the several amounts stated therein as proposed expenditures shall be and become appropriated to the several groups, offices and agencies for the respective objects and purposes therein named." This appropriation provides the authority for the City's spending during the fiscal year. In most cases, expenditures may not exceed appropriations at the department level, which is the legal level of control. Although the Carson Reclamation Authority's budget for fiscal year 2015-16 was adopted on July 7, 2015, we noted that the budgets for the City's General Fund and Special Revenue Funds and the Housing Authority, were not adopted until November 17, 2015, which is past the required date of July 20, 2015. We recommend that the City comply with the requirements of the City's Municipal Code by establishing policies and procedures to ensure the timely adoption of the annual budgets.

#### Management's Response

We agree with the comment. The fiscal year 2016-17 budget was adopted on June 21, 2016. The fiscal year 2017-18 budget process has begun with the goal to adopt the budget by June 30, 2017.



## **Compliance and Other Matters (Continued)**

We noted certain matters that we have reported to management and the City Council in a separate letter dated February 28, 2017.

### **City's Responses to the Findings**

The City's responses to the findings are described above. The City'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 City'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 City's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

*White Nelson Dickel Evans LLP*

Irvine, California  
February 28, 2017