

CITY OF BELL, CALIFORNIA

SINGLE AUDIT REPORT

JUNE 30, 2014

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SINGLE AUDIT REPORT
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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 Honorable Mayor and Members of the City Council
City of Bell, 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, each major fund, and the aggregate remaining fund information of the City of Bell, California, (the City) as of and for the year ended June 30, 2014, and the related notes to the financial statements, which collectively comprise the City's basic financial statements, and have issued our report thereon dated January 20, 2015.

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, 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. 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 deficiency 2014-001 described in the accompanying schedule of findings and questioned costs to be a material weakness.

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 deficiency 2014-003 described in the accompanying schedule of findings and questioned costs to be significant deficiency.



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

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 the instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying schedule of findings and questioned costs as items 2014-002.

Other Matters

Information Technology

During the audit of fiscal year ended June 30, 2014, it was noted that the City lacked the proper Information Technology Controls that a critical for ensuring the integrity of information systems. The City lacked the following controls:

- Contractual agreements for City's outsourcing of financial system programming and support,
- Formal policies and procedures for managing changes or development to the financial system,
- Physical security of network and server hardware,
- General and Application Access Controls such as separate, unique and complex access passwords, and
- Batching and interface capabilities

City's Response to Findings

The City's response to the findings identified in our audit was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

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 entity'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 entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Lance, Soll & Lughard, LLP

Brea, California
January 20, 2015

INDEPENDENT AUDITORS' REPORT ON COMPLIANCE FOR EACH MAJOR PROGRAM AND
ON INTERNAL CONTROL OVER COMPLIANCE; AND REPORT ON SCHEDULE OF EXPENDITURES
OF FEDERAL AWARDS REQUIRED BY OMB CIRCULAR A-133

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

Report on Compliance for Each Major Federal Program

We have audited the City of Bell's (the City) compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of the City's major federal programs for the year ended June 30, 2014. The City's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the City's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the City's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of the City's compliance.

Opinion on Each Major Federal Program

In our opinion, the City of Bell complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2014.



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

Other Matters

The results of our auditing procedures disclosed an instance of noncompliance, which is required to be reported in accordance with OMB Circular A-133 and which is described in the accompanying schedule of findings and questioned costs as item 2014-004. Our opinion on each major federal program is not modified with respect to these matters.

The City's response to the noncompliance findings identified in our audit is described in the accompanying schedule of findings and questioned costs. The City's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

Report on Internal Control over Compliance

Management of the City is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the City's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the City's internal control over compliance.

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

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified. However, we identified a deficiency in internal control over compliance, as described in the accompanying schedule of findings and questioned costs as item 2014-004, that we consider to be a significant deficiency.

The City's response to the internal control over compliance findings identified in our audit is described in the accompanying schedule of findings and questioned costs. The City's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.



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

Report on the Schedule of Expenditures of Federal Awards Required by OMB Circular A-133

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the City of Bell, California, as of and for the year ended June 30, 2014, and the related notes to the financial statements, which collectively comprise the City's basic financial statements. We issued our report thereon dated January 20, 2015, which contained qualified opinions on the Governmental Activities, the General Fund, the Community Development Block Grant Special Revenue Fund, the Community Housing Authority Special Revenue Fund, the Gas Tax Capital Projects Fund, and the aggregate nonmajor governmental funds; and an unmodified opinion on the respective financial position of the Retirement Special Revenue Fund, the Low and Mod Housing Special Revenue Fund, and the Public Financing Authority Debt Service Fund. Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the basic financial statements. The accompanying schedule of expenditures of federal awards is presented for the purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of expenditures of federal awards is fairly stated in all material respects in relation to the basic financial statements as a whole.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.

Lance, Soll & Lughard, LLP

Brea, California
January 20, 2015

CITY OF BELL

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2014**

Federal Grantor/Pass-Through Grantor/Program Title	Federal CFDA Number	Pass-Through Grantor's Number	Expenditures
<u>U.S. Department of Housing and Urban Development</u>			
Passed through the Community Development Commission of the County of Los Angeles			
Community Development Block Grants/Entitlement Grants*	14.218	D96061-13	\$ 193,730
		D96065-13	68,931
		600511-13	25,000
		D96069-13	110,016
		D99075-13	75,000
		601556-12	126,063
		601586-12	5,010
Total U.S. Department of Housing and Urban Development			603,750
<u>U.S. Department of Justice</u>			
Direct Program:			
Bureau of Justice Assistance:			
Edward Byrne Memorial Justice Assistance Grant	16.738	2012-DJ-BX-104	15,228
Edward Byrne Memorial Justice Assistance Grant	16.738	2013-DJ-BX-075	17,993
Total U.S. Department of Justice			33,221
<u>U.S. Department of Treasury</u>			
Direct Program:			
Federal Asset Forfeitures	21.000	CA0190700	47,173
Total U.S. Department of Transportation			47,173
<u>U.S. Department of Homeland Security</u>			
Direct Program:			
U.S. Department of Education Tech Grant	84.215	U215K100191	32,100
Total U.S. Department of Education			32,100
<u>U.S. Department of Homeland Security</u>			
Passed through the County of Los Angeles:			
Homeland Security Grant Program	97.067	2011-0077	10,174
Total U.S. Department of Homeland Security			10,174
Total Federal Expenditures			\$ 726,418

* Major Program

CITY OF BELL

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2014**

<u>Federal Grantor/Pass-Through Grantor/Program Title</u>	<u>Federal CFDA Number</u>	<u>Pass-Through Grantor's Number</u>	<u>Expenditures</u>
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Note a: Refer to Note 1 to the schedule of expenditures of federal awards for a description of significant accounting policies used in preparing this schedule.

Note b: There was no federal awards expended in the form of noncash assistance and insurance in effect during the year.

Note c: Total amount provided to subrecipients during the year was \$0.

**NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2014**

Note 1: Summary of Significant Accounting Policies Applicable to the Schedule of Expenditures of Federal Awards

a. Scope of Presentation

The accompanying schedule presents only the expenditures incurred by the City of Bell, California, that are reimbursable under federal programs of federal financial assistance. For the purposes of this schedule, federal awards include both federal financial assistance received directly from a federal agency, as well as federal funds received indirectly by the City from a non-federal agency or other organization. Only the portion of program expenditures reimbursable with such federal funds is reported in the accompanying schedule. Program expenditures in excess of the maximum federal reimbursement authorized or the portion of the program expenditures that were funded with state, local or other non-federal funds are excluded from the accompanying schedule.

b. Basis of Accounting

The expenditures included in the accompanying schedule were reported on the modified accrual basis of accounting. Under the modified accrual basis of accounting, expenditures are incurred when the City becomes obligated for payment as a result of the receipt of the related goods and services. Expenditures reported included any property or equipment acquisitions incurred under the federal program.

c. Relationship to City Basic Financial Statements and Federal Financial Reports

Information reported in the accompanying Schedule agrees with the amounts reported in both the basic financial statements and related federal financial reports for the federal award programs. Revenues from federal award programs are reported as intergovernmental revenues in the basic financial statements.

d. Loan Programs with Continuing Compliance Requirements

The City participates in the Community Development Block Grants/Entitlement Grants (CFDA No. 14.218) of the U.S. Department of Housing and Urban Development, which is subject to continuing compliance requirements for outstanding loans. The program's outstanding loans balances with continuing compliance requirements is \$322,393.

CITY OF BELL

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2014**

SECTION I - SUMMARY OF AUDITORS' RESULTS

Financial Statements

Type of auditors' report issued: Qualified Opinion and Unmodified Opinion

Internal control over financial reporting:

- Significant deficiencies identified? ☒ yes ☐ no
- Material weaknesses identified? ☒ yes ☐ none reported

Noncompliance material to financial statements noted? ☐ yes ☒ no

Federal Awards

Internal control over major programs:

- Significant deficiencies identified? ☒ yes ☐ no
- Material weaknesses identified? ☐ yes ☒ none reported

Type of auditors' report issued on compliance for major programs: Unmodified Opinion

Any audit findings disclosed that are required to be reported in accordance with Section 510(a) of Circular A-133? ☒ yes ☐ no

Identification of major programs:

CFDA Number(s)

Name of Federal Program or Cluster

14.218

Community Development Block Grants/
Entitlement Grants

Dollar threshold used to distinguish between type A and type B program \$300,000

Auditee qualified as low-risk auditee? ☐ yes ☒ no

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2014**

SECTION II - FINANCIAL STATEMENT FINDINGS

MATERIAL WEAKNESS

2014-001 Internal Controls over Significant Accounting Procedures

Criteria

An organization should have a system of internal controls, which are suitable designed to allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements of the City's financial statement on a timely basis. Formal written policies and procedures are an integral part of a system of internal controls. Such policies and procedures are established to ensure integrity over financial reporting, including compliance with provisions of laws, regulations, contracts, and grant agreements that could have a direct and material effect on the financial statements, and to safeguard assets. An effective system of internal controls also needs to operate as designed. Key duties and responsibilities need to be divided or segregated amongst different people to reduce the risk of error or fraud. This should include separating the responsibilities for authorizing transactions, processing and recording them, reviewing the transactions, and handling any related assets. No one individual should control all key aspects of a transaction or event.

Condition, Cause and Effect

We have identified the following material weaknesses in internal controls during our audit:

1. Liabilities and cash disbursements:
 - a. There is a lack of segregation of duties within the Finance Department. The cash disbursement system is accessible via a password; however, the password is shared with the various users of the system. New vendors can be established by any user in the system. The approval process is performed verbally among the Finance Director, the Accounting Manager, and the Account Clerk. Lack of documentation over the approval process can cause the City to be at higher risk for inaccurate and unauthorized payments. The City's management expects to correct this during the implementation of their new accounting system.
2. Cash handling, cash receipts, receivables, bank reconciliations and investments:
 - a. The cash receipts system for the City is outdated and constrictive. The system requires that the prior month's transactions be completed, approved and posted before the current month's data can be entered. This delays the recording of the current month's transactions and could result in inaccurate posting of revenues. The City's management expects to correct this during the implementation of their new accounting system.
3. Loans receivable and deposits payable:
 - a. The City is not monitoring the terms of loans receivable in the Low and Moderate Housing Fund, and deposits payable resulting from rental agreements. They are not aware of payment terms, interest earned, or amounts collected and payable to renters. As a result, loan receivable and deposits payable balances may not accurately reflect City assets and obligations, respectively, as of June 30, 2014.

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2014**

SECTION II - FINANCIAL STATEMENT FINDINGS (CONTINUED)

4. Salaries, employee benefits and compensated absences:
 - a. The City is allocating employee salaries, wages and related benefits expenditures to governmental funds based on budgetary amounts and not actual costs incurred. Pursuant to government accounting standards, costs allocated to funds should be based on actual costs.
 - b. The City did not maintain personnel files for some retirees. As a result, census information for those retirees could not be verified as it relates to retiree pension calculations.

Recommendation

We recommend that the City take immediate action to implement the policies and procedures that the Finance Department developed to address the material weaknesses noted above. In addition, we recommend the City to perform periodic monitoring reviews to determine that the controls are functioning as intended. The City should also perform periodic risk assessments of the control environment to determine whether changes in policies and procedures are warranted, when there are changes in the operating environment.

Management Response and Corrective Action

In November 2013, the Finance Department published its "Financial Management Policies and Procedures Manual." The Manual penetrates deeply into the internal controls observations above. As further testament to the City's motivation in regard to continued improvement in all facets of accounting and financial management, the City implemented a new Accounting ERP System July 2014; unfortunately, these controls still existed at the close of fiscal year 2014. However, the finance department is confident that such weaknesses identified above will be resolved by the end of fiscal year 2015.

Expected Completion Date and Contact Information

The City plans on being in complete compliance with all controls weaknesses by at least FY 2015.

Responsible parties for corrective action are:

- a. Josh Beta, Finance Director
- b. Hector Vazquez, Accounting Manager

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2014**

SECTION II - FINANCIAL STATEMENT FINDINGS (CONTINUED)

COMPLIANCE AND OTHER MATTERS

Finding 2014-002: Noncompliance with Laws, Regulations, Contracts, and Grant Agreements

Criteria

Governmental entities are subject to a variety of laws, regulations, contracts and grant agreements that have a direct and material effect on their financial statements. Accordingly, governmental entities should establish a system of internal control over compliance to ensure compliance with laws, regulations, contracts and grant agreements.

Condition, Cause and Effect

As a result of financial conditions at the City and weaknesses in internal control over compliance, we noted the following instances of noncompliance with bond covenants, budget policy, and other applicable laws and regulations, contracts and grant agreements:

1. Pursuant to HSC section 34177, the City of Bell, acting as the Successor Agency to the Former Redevelopment Agency, must submit a *Recognized Obligation Payments Schedule* (ROPS) every six months for the succeeding six months of legal obligations that must be paid using RPTTF monies. The City, acting as the Successor Agency to the Former Redevelopment Agency, must pay those obligations in a manner prescribed in the ROPS, pursuant to HSC section 34177. During our audit, we noted that the City deposited RPTTF monies received from the State of California in January 2013, and deposited such monies into the City's General Checking Account and not the dedicated account of the Successor Agency. The City eventually repaid the Successor Agency in February 2014.

The State Controller's Office (SCO) review of the former Agency for the period July 1, 2000, through June 30, 2011, identified that the former Agency failed to comply with Health and Safety Code requirements in several areas and inappropriately charged the former Agency funds in the amount of \$664,834. This is pending final resolution.

2. The City did not comply with reporting provisions of the indentures for the 2003 Tax Allocation Bonds and the 2007 Taxable Revenue Bonds for the fiscal year ended June 30, 2014. These bond covenants require that the City's audited financial statements be issued within 180 days after the fiscal year end. In addition, in accordance with the former Agency's 2003 Tax Allocation Refunding Bonds Official Statements, the City is required to provide a written Certificate of the former Agency due by 10/1/13 certifying that Tax Revenues Received by the former Agency through the date of the certificate combined with the amount remaining to be paid on all outstanding obligations of the former Agency will not exceed the maximum amount of tax revenues to be divided and allocated to the former Agency pursuant to the former Agency's Redevelopment Plan.
3. The City purchased 5 years of Additional Retirement Service Credits (ARSC) on behalf of the former CAO, the former ACAO, 5 former council members and 4 former department heads between 2005 and 2009 using City funds with an approximate cost of \$1,000,000. CalPERS has made a determination that the purchase of ARSC using City funds for one of the former department heads was not lawful under the Public Employee Retirement Law. In January 2013, the former CAO waived

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2014**

SECTION II - FINANCIAL STATEMENT FINDINGS (CONTINUED)

the purchased of ARSC. However, the determination on the remaining purchases of ARSC is pending.

4. The SCO's audit of the City's administrative and internal accounting system for the period July 1, 2008, through June 30, 2010, identified that the City improperly increased assessments of the Sanitation and Sewerage Assessment System and business licenses taxes. The SCO estimated the amount of overcharge is \$621,737 and \$2,105,441 for assessment of the Sanitation and Sewerage Assessment System and business licenses taxes, respectively. On a follow-up review by the SCO dated May 22, 2013, the SCO estimated the amount of overcharge is \$822,000 and \$2,355,000 for assessment of the Sanitation and Sewerage Assessment System and business licenses taxes, respectively. This is pending final resolution.

Recommendation

We recommend that the City develop, document, and implement policies and procedures to ensure the City's compliance with applicable laws, regulations, contracts and grant agreements. We also recommend that the City's budget process include a mid-year and year-end comparison of budget and actual amounts to allow City Council an opportunity to take any action deemed necessary to ensure compliance with local laws and regulations governing budget appropriations and related expenditures. In addition, we recommend that the City work with the SCO and CalPERS to resolve pending issues.

Management's Response and Corrective Action

Management is working with legal counsel on the non-compliance litigations noted above. The outcome is unknown at this time. The bond covenant compliance finding is known by management and each audit year is getting closer and closer to be reported timely. Management is expecting the CAFR to be filed timely in fiscal year 2015. The information technology matter is known by management and has been addressed. The Finance Department has purchased a new financial software system that will provide the securities, controls, and financial batch processing needed. A new consultant was obtained for the computer monitoring and processes and contractual relationship has been implemented in fiscal year 2015. This matter has been addressed in the new fiscal year.

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2014**

SECTION II - FINANCIAL STATEMENT FINDINGS (CONTINUED)

SIGNIFICANT DEFICIENCY

Finding 2014-003: Fund Balance Restatements

Criteria

Financial statement closing procedures should be designed and followed in a manner that allows the Finance Department to accurately identify financial statement misstatements in a timely manner. The financial statement closing process should include such procedures that allows the Finance Department to accurately reconcile the general ledger balances to sub-ledger information. This includes, not limited to, capital asset sub-ledger information verified through taking a physical inventory of those assets on a periodic basis.

Condition, Cause and Effect

During the fiscal year ended June 30, 2014, the City restated the General Fund and the Indian Gaming Fund to recognize revenues recorded in the proper accounting periods. In addition, a restatement was made to Governmental Activities net position to correct the carrying amounts of Construction in Progress and Storm Drain capital accounts. These restatements were done to correct errors in accounting policies and practices identified by management.

Recommendation

We recommend that the Finance Department, as part of their closing procedures, ensure that all asset and liability balances are fully reconciled from sub-ledger information to the accounting general ledger. This will include ensuring that subsequent cash receipts recorded within the City's revenue recognition policy are reviewed for deferral and accrual to the financial statements. In addition, that a periodic physical inventory is performed to verify the existence of capital assets depicted on the City's capital asset sub-ledgers.

Management's Response and Corrective Action Plan

Management agrees with this audit finding and will continue to improve the City's accounting policies and procedures.

Expected Completion Date

Management has corrected this deficiency for fiscal year ended June 30, 2014.

CITY OF BELL

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2014**

SECTION III - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

US Department of Housing and Urban Development

Program Name: Community Development Block Grant (CDBG)

CFDA # 14.218

Grant No. D96061-13, D96065-13, D96069-13, 601556-12

Finding 2014-004 – Labor Hours

SIGNIFICANT DEFICIENCY

Allowable Cost/Cost Principals

Criteria

Pursuant to OMB Circular A-87 and A-112, allowable costs must be appropriately documented and supported in order for the City to request reimbursement of those costs from federal funding sources.

Condition, cause and effect

The City did not implement reconciliation and monitoring procedures to ensure that hours being charged to programs accurately agree to timecards. As a result, several employees with payroll charged to the Community Development Block Grant programs had hours recorded on their timesheets that do not agree to the labor analysis reports reported to the Los Angeles County Community Development Commission. Even though the funding source approved the costs, the City did not update and reconcile its supporting information.

Questioned Costs

None

Recommendation

We recommend that the City implement procedures to ensure that all costs being charged to federal grants are properly reviewed and reconciled to supporting documentation prior to request for reimbursement.

Corrective Action Plan and Responsible Person(s)

The City's former computerized accounting system, originally purchased in 1986 and unmodified thereafter, did not allow one computing module to communicate with the general ledger of accounts. In this manner, hours of work represented on employee timecards, when paid through the payroll module, were accumulated in a payroll suspension account until distribution was created to line item accounts via journal entry. This system of distribution was premised on employee allocation documented on personnel action forms, but, by its nature, was effectuated by estimate of time worked, not actual hours worked. Deviations in terms of hours worked could not be recognized as a result.

In July 2014, the City implemented a new automated accounting system, replacing the antiquated technology described above. Hours worked as reflected on employee timecards are now reflected accurately on labor distributions and within the general ledger of accounts. In addition, contractual support for CDBG compliance within the City of Bell has been transitioned during FY 2015 to a more highly-qualified contractor, and supervision of this function has been transferred from the City's Community Services Department to the Community Development Department. Said contractor, Community Development Department representatives and Finance Department representatives have collaborated to develop reconciliation and monitoring procedures that will allow for accurate updating and reconciliation of information going forward.

Responsible parties for corrective action are:

- a. Josh Beta, Finance Director
- b. Hector Vazquez, Accounting Manager

**SCHEDULE OF PRIOR YEAR FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2013**

SECTION II – 2013 FINANCIAL STATEMENT FINDINGS

MATERIAL WEAKNESS

2013-001 Internal Controls over Significant Accounting Procedures

Criteria

An organization should have a system of internal controls, which are suitable designed to allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements of the City's financial statement on a timely basis. Formal written policies and procedures are an integral part of a system of internal controls. Such policies and procedures are established to ensure integrity over financial reporting, including compliance with provisions of laws, regulations, contracts, and grant agreements that could have a direct and material effect on the financial statements, and to safeguard assets. An effective system of internal controls also needs to operate as designed. Key duties and responsibilities need to be divided or segregated amongst different people to reduce the risk of error or fraud. This should include separating the responsibilities for authorizing transactions, processing and recording them, reviewing the transactions, and handling any related assets. No one individual should control all key aspects of a transaction or event.

Condition, Cause and Effect

We have identified the following material weaknesses in internal controls during our audit:

1. Capital assets:
 - a. The City has not conducted physical inventory of capital assets. A properly designed system of internal controls should establish guidelines for a periodic physical inventory of capital assets, which reconciles physical counts to accounting records to ensure recorded capital assets exist and to safeguard capital assets.
2. Liabilities and cash disbursements:
 - a. The City does not have formal policies and procedures for determining year-end accruals for accounts payable and other accrued liabilities. Based on our search for unrecorded liabilities through examining subsequent disbursements, we determined that the City under accrued liabilities on some instances and over accrued liabilities in other instances. The net impact was an understatement of liabilities and expenditures/expenses by \$841,433 which included unrecorded payables of \$922,386 in "billed no pay" legal fees, unrecorded payables of \$266,955 in professional fees and an over accrual of payables of \$418,619 in street repairs. Subsequently, the City recorded an adjustment to accrue the liabilities into the proper fiscal year. Proper cutoff at year-end is critical for the accuracy of reporting transactions in the proper period. Without proper cutoff, expenditures/expenses and payables may not be accurately stated.
 - b. There is a lack of segregation of duties within the Finance Department. The cash disbursement system is accessible via a password; however, the password is shared amongst the various users of the system. New vendors can be established by any user in the system. The approval process is performed verbally among the Finance Director, the Accounting Manager, and the Account Clerk. Lack of documentation over the approval process can cause the City to be at higher risk for inaccurate and unauthorized payments. The City's management expects to correct this during the implementation of their new accounting system.

**SCHEDULE OF PRIOR YEAR FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2013**

SECTION II – 2013 FINANCIAL STATEMENT FINDINGS (CONTINUED)

- c. Per our understanding of internal controls, there was no safeguard over the blank check stock. These deficiencies cause the City to be at a high risk for unauthorized payments. The City's management expects to correct this during the implementation of their new accounting system.
 - d. The City does not reconcile the detail list of deposits payable at year-end reported in sub-ledgers to the general ledger account. Accordingly, the balance of deposits payable may not be accurately stated.
 - e. The City also does not have formal process over managing deposits payable. We noted that when a tenant becomes grossly delinquent on rent, the tenant's security deposit will be applied against the back rent. The application of the security deposit against overdue rent is not communicated to the Finance Department. As a result, deposits payable was overstated by \$32,000 at June 30, 2014. Without a formal process over deposits payable, the City is at risk to incorrectly recognize revenues as deposits payable.
 - f. The City does not reconcile workers' compensation payments made by the third-party vendor to the general ledger. As a result, there was an approximately \$102,000 discrepancy in workers' compensation payments per the general ledger and the loss-run claim report maintained by the third-party vendor.
3. Cash handling, cash receipts, receivables, bank reconciliations and investments:
- a. The cash receipts system for the City is outdated and constrictive. The system requires that the prior month's transactions be completed, approved and posted before the current month's data can be entered. This delays the recording of the current month's transactions and could result in inaccurate posting of revenues. The City's management expects to correct this during the implementation of their new accounting system.
 - b. The City does not have formal policies and procedures for determining year-end accruals for receivables. As a result, the City did not reduce receivables recorded in fiscal year 2012 in the amount of \$112,000 for payments received in fiscal year 2013, did not record gas tax receivables of \$25,000 for fiscal year 2013, and recorded \$18,000 of reimbursable expenditures as a reduction of deposits payable. Proper cutoff at year end is critical for the accuracy of reporting transactions in the proper period. Without proper cutoff, revenues and receivables may not be accurately stated.
 - c. The City did not evaluate the collectability of advances to the Successor Agency of approximately \$1,430,000 by the Housing Special Revenue Fund, \$4,252,000 by the General Fund and \$950,000 by the Retirement Special Fund; nor did the City evaluate the collectability of inter-fund receivables from the General Fund of \$574,000 to the Retirement Special Revenue Fund and \$218,000 to the non-major governmental funds. The City subsequently wrote-off advances to the Successor Agency in the amount of \$6,632,000 and reported a loss under a special item. The City also subsequently reclassified approximately \$555,000 of due from the Retirement Special Revenue Fund and approximately \$218,000 of the non-major governmental funds to the General Fund to inter-fund transfers. The City should establish a formal process by which the collectability of advances to and inter-fund receivables are evaluated at least annually.

**SCHEDULE OF PRIOR YEAR FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2013**

SECTION II – 2013 FINANCIAL STATEMENT FINDINGS (CONTINUED)

- d. The City did not comply with the policy for accounting for stale dated checks as the City wrote-off stale checks of approximately \$212,000 from the City's bank account without publishing a notice in a newspaper in accordance with California Government Code Sections 50050-50053.
 - e. The City does not evaluate the cash balances in the pool account to reclassify negative cash balances as inter-fund receivables and payables. Subsequent to our inquiry, the City reclassified approximately \$115,000 of negative cash balances to Due from Successor Agency as of June 30, 2014.
4. Salaries, employee benefits and compensated absences:
- a. The City does not have policies and procedures for the allocation of direct or indirect payroll expenditures and related benefits to City funds and functions. We found various employee payroll expenditures and the related benefits allocated to various functions and funds based on budget estimates. As a result, expenditures and fund balances reported in the General Fund totaling \$7,500,962, Community Housing Authority Special Revenue Fund totaling \$136,965, Gas Tax Capital Projects Fund totaling \$41,317, and aggregate non-major governmental funds totaling \$92,193, as well as functional expenditures reported in the Statement of Activities may not be accurately stated.
5. Transfers in and out:
- a. The City budgeted and made transfers in the amount of \$486,000 from several non-major special revenue funds to the General Fund to reimburse the General Fund for administrative expenditures incurred. These transfers are solely based on budget estimates. These budget estimates were developed based on a cost allocation study. However, there was no analysis performed to compare actual expenditures against budget estimates. As a result, expenditures and fund balances reported in the General Fund and aggregate non-major governmental funds as well as functional expenditures reported in the Statement of Activities may not be accurately stated. For the financial statements presentation, these amounts were not shown as transfers but as reduction to expenditures and expenditures of the General Fund and aggregate non-major governmental funds.
6. Other post-employment benefits (OPEB):
- a. The City did not remove terminated employees from the data sent to the actuary for the OPEB valuation as of July 1, 2012. The inclusion of terminated employees in the data may result in the annual required contribution, the OPEB liability, and the funded status of the OPEB plan as of June 30, 2012, not being accurately stated. Since the City utilized the valuation as of July 1, 2012, as the basis for the current year estimate, the liability as of June 30, 2013, may not be accurately stated. The City should implement a process to review participant data utilized for OPEB estimates.
7. Year-end close process:
- a. The City does not have a documented year-end close process. We found that the process was disorganized and fragmented, which resulted in many audit adjustments to record missed transactions or to correct errors. During our audit we noted that the City did not record entries from the fiscal year 2012 audit of approximately \$182,000 for the General Fund and \$250,000 for the aggregate non-major governmental funds.

CITY OF BELL

SCHEDULE OF PRIOR YEAR FINDINGS AND QUESTIONED COSTS (CONTINUED) FOR THE YEAR ENDED JUNE 30, 2013

SECTION II – 2013 FINANCIAL STATEMENT FINDINGS (CONTINUED)

Recommendation

We recommend that the City review all of its major functions and services and develop, approve, and implement formal written policies and procedures to ensure that the City's system of internal control over financial reporting and the safeguarding of assets is suitably designed. We further recommend that the City take immediate action to develop the policies and procedures related to the material weaknesses noted above. This should include a plan for the year-end closing process, which should detail a step by step guide listing each closing procedure, the individual responsible for the procedure, the time frame in which this procedure will be performed, and the individual who will review and approve the procedure. The City should also perform periodic monitoring reviews to determine that the controls are functioning as intended and that the appropriate controls are in place. In addition, the City should perform periodic risk assessments of the control environment to determine whether changes in policies and procedures are warranted when there are changes in the operating environment.

Management Response and Corrective Action

In November 2013, just weeks before the City receipted \$20.2 million from legal settlements and a land sale -thus completing the economic turnaround of the City of Bell organization --the Finance Department published its "Financial Management Policies and Procedures Manual." The Manual penetrates deeply into the internal controls observations above, and Department management is confident that vast improvement will manifest itself within months. As further testament to the City's motivation in regard to continued improvement in all facets of accounting and financial management, the Department added a second accounting position to its authorized personnel count during FY 2013.

The City's antiquated automated accounting system was purchased in 1986; at about the same time that desktop computing was introduced. Most of the system modules are not integrated, thus developing and reconciling year-end accruals for payable and receivables, to cite two examples, is a manual process. The cash receipting system suffers from similar limitations. At this writing, however, the process of implementing a new automated accounting system is well underway. The Department is on target to go parallel in June and go live with the new system on July 14, 2014.

Expected Completion Date and Contact Information

The City plans on being in complete compliance with all controls weaknesses by at least FY 2015.

Responsible parties for corrective action are:

- c. Josh Beta, Finance Director
- d. Hector Vazquez, Accounting Manager

Status

The City is still in the process of correcting these material weaknesses, on a collective basis. The City has developed internal control policies and procedures, however, as indicated in our recommendation at finding 2014-001, the City should also consider performing periodic risk assessments of the control environment to determine whether changes in policies and procedures are warranted, when there are changes in the operating environment.

**SCHEDULE OF PRIOR YEAR FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2013**

SECTION II – 2013 FINANCIAL STATEMENT FINDINGS (CONTINUED)

MATERIAL WEAKNESS

Finding 2013-002: Information Technology (IT) Control Weaknesses

Criteria

IT controls are a critical mechanism for ensuring the integrity of information systems and the reporting of the City's finances.

Condition, Cause and Effect

Since the FY 2012 Single Audit was issued in July 2013, many deficiencies noted in the 2012 Single Audit continue to exist as follows:

1. City lacks central governance of IT strategy and activities:
 - a. The Committee of Sponsoring Organizations of the Treadway Commission (COSO) standards requires that the top level of governance establish policies and procedures for its entire organization. Additionally, the COSO framework standards encourage that continual monitoring of these controls exist to ensure that the documented controls are actually being adhered to by staff. Such governance is integral to providing direction and establishing an entity's control environment by issuing enterprise-wide policies and procedures and providing oversight over IT activities. No such IT policies or procedures exist within the City.
 - b. The City has hired BreaIT to provide IT Management support. BreaIT also meets with the City regularly and is a member of the City's IT Technology Steering Committee (BITS). However, the City has not established IT policies and procedures.

Recommendation

The BITS committee, working in conjunction with BreaIT and the City management, should develop and implement IT policies and procedures governing all areas of IT controls, including hardware, software, user access, vendor activities, and general and application-specific IT security.

Management's Response and Corrective Action

The Finance Department published its "Financial Management Policies and Procedures Manual in November 2013, but only after the difficult work of establishing a balanced FY 2013 budget and the completion of economic settlements and a land sale permanently corrected the economic status of the City of Bell organization. The Manual possesses a plethora of IT policies.

Expected Completion Date and Contact Information

The City plans on being in complete compliance with all controls weaknesses by at least FY 2015.

Responsible parties for corrective action are:

- a. Josh Beta, Finance Director
- b. BreaIT

**SCHEDULE OF PRIOR YEAR FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2013**

SECTION II – 2013 FINANCIAL STATEMENT FINDINGS (CONTINUED)

Status

This finding has been corrected.

2. No contractual agreements for the City's outsourcing of financial system programming and support:
 - a. All services performed by outside entities for the City should be performed under contract. The City did not have any contract with DataStream Business Solutions (DataStream), which provides financial programming and support.

Recommendation

The City should 1) determine, via negotiation and forensic documentation analysis as required, ownership of its financial system software and 2) determine desired contractual terms and conditions for IT support vendors. After identifying their IT needs versus the services being provided by their current contractors, the City should evaluate if it should continue with current vendors or issue new Request for Proposals. The City should subsequently document and execute new contracts with its IT service providers.

Management's Response and Corrective Action

The City issued RFPs for a replacement accounting system in FY 2014, completed all relevant contracts, and is currently implementing the system. Go live date is July 14, 2014. The City continues to from time to time utilize its legacy support with DataStream Business Solutions on a time and materials basis for programming in support of the City's outdated system and for transitioning to the new system.

Expected Completion Date and Contact Information

The City plans on being in complete compliance with all controls weaknesses by at least FY 2015.

Responsible parties for corrective action are:

- a. Josh Beta, Finance Director
- b. BreaIT

Status

This finding is no longer considered a material weakness due to the implementation of a new system; however the finding is still warranted for fiscal year ending 2014 due to the use of the legacy system during this period.

3. The City does not have an IT Strategic Plan
 - a. Best practices in IT general controls should ensure that strategic IT plans are developed that are aligned with the goals and objectives of the agency as a whole. The City, however, has not developed an IT Strategic Plan. Without a Strategic Plan in place, IT initiatives may not be in alignment with City needs, and the City may find difficulty in justifying required IT expenditures.

**SCHEDULE OF PRIOR YEAR FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2013**

SECTION II – 2013 FINANCIAL STATEMENT FINDINGS (CONTINUED)

Recommendation

The BITS committee working in conjunction with BreaIT and the City management should develop an IT Strategic Plan. This plan should ensure that IT initiatives are aligned with the goals and objectives of the City.

Management's Response and Corrective Action

On April 17, 2012, BreaIT published the "City of Bell Network Analysis." This has formed the basis for a multitude of projects that have been completed, and others that are ongoing. At this writing, the City has released an RFP for consulting IT services. The successful bidder will be expected to develop a new strategic plan with City management.

Expected Completion Date and Contact Information

The City plans on being in complete compliance with all controls weaknesses by at least FY 2015.

Responsible parties for corrective action are:

- a. Josh Beta, Finance Director
- b. BreaIT

Status

This finding has been corrected.

- 4. A formal policy and procedure for managing changes or development to the financial system has not been established:
 - a. Change control is a formal process used to ensure that changes to a product or system are introduced in a controlled and coordinated manner. Today's computer applications and network infrastructure are extremely complex, and require careful control and testing of changes in order not to disrupt an organization's operations. What seems like an innocuous code change can have disastrous impacts on a downstream process or data integrity. The City, however, has no formal control documentation for how the financial system vendor will manage system changes. Change control, including testing, is currently only based on the institutional knowledge of those involved.

Recommendation

The City should formally document change control processes with its financial systems vendor, including roles, ownership, and responsibility for testing and approvals at both the financial system vendor and within the City.

Management's Response and Corrective Action

Recommendation above is largely impossible with regard to the automated accounting system purchased in 1986. The new accounting system will be in place in July 2014. At that time the Finance Department and the Springbrook (chosen vendor) will establish change controls.

**SCHEDULE OF PRIOR YEAR FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2013**

SECTION II – 2013 FINANCIAL STATEMENT FINDINGS (CONTINUED)

Expected Completion Date and Contact Information

The City plans on being in complete compliance with all controls weaknesses by at least FY 2015.

Responsible parties for corrective action are:

- a. Josh Beta, Finance Director
- b. BrealT

Status

This finding is no longer considered a material weakness due to the implementation of a new system; however the finding is still warranted for fiscal year ending 2014 due to the use of the legacy system during this period.

- 5. The City has an inadequate data backup location for financial system:
 - a. Best practices for disaster recovery require that a data back-up location not be susceptible to the same types of disasters (flood, fire, terrorist acts, etc.) as the main location. In lieu of a formal evaluation of the recovery site risks, the site should be at least 20 miles away from the main location. This control should ensure that the City's systems and data can be restored in the event of a disaster. If the primary and back-up locations are geographically close, it increases the risk that both locations are unavailable in the event of a disaster.
 - b. The financial system is being backed up every night to an internal tape drive and the Finance Department is responsible for changing the tapes. Tapes are stored in a safe in the Finance Department's storage room. By not having a backup location outside of a 20 mile radius from the City, the City is at an increased risk of losing financial data if a disaster event occurs.

Recommendation

The City should implement offsite retention of back-up tapes of the City's financial system.

Management's Response and Corrective Action

The City established contract with Iron Mountain for offsite retention of backup tapes in October 2013.

Expected Completion Date and Contact Information

The City plans on being in complete compliance with all controls weaknesses by at least FY 2015.

Responsible parties for corrective action are:

- a. Josh Beta, Finance Director
- b. BrealT

Status

This finding has been corrected.

**SCHEDULE OF PRIOR YEAR FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2013**

SECTION II – 2013 FINANCIAL STATEMENT FINDINGS (CONTINUED)

6. The City's does not manage or review access role/or its network or financial system:
- a. Organizations need to understand, define, and document their authorization roles and administrator access, in order to properly segregate duties between individuals. Undefined authorization roles and administrator access put organizations at risk of financial fraud, waste, and abuse.
 - b. The City has implemented department shares that are segregated by Access Control Lists (ACLs). The City, however, has no policies or procedures for review of network access or roles, even when employees are terminated.

Recommendation

BreaIT working in conjunction with the City management should develop access roles and policies and procedures to manage these roles, for both the City's network as well as for the City's financial system. The policies and procedures should address hiring and terminations, review of master or super user activity, and annual review of roles.

Management's Response and Corrective Action

The Finance Department published its "Financial Management Policies and Procedures Manual in November 2013, but only after the difficult work of establishing a balanced FY 2013 budget and the completion of economic settlements and a land sale permanently corrected the economic status of the City of Bell organization. The Manual possesses a plethora of IT policies that will be fine-tuned to the new accounting and finance system.

Expected Completion Date and Contact Information

The City plans on being in complete compliance with all controls weaknesses by at least FY 2015.

Responsible parties for corrective action are:

- a. Josh Beta, Finance Director
- b. BreaIT

Status

This finding has been corrected.

7. The City's financial system server is not physically secured:

- a. Physical security practices require that the City provide and enforce physical access protection for the facility or room where the financial system resides. This prevents unauthorized tampering or abuse of the physical server hardware. The server housing the City's financial system is fully accessible, in the back of the City administration office, with no secured access. This places the City's financial system server at increased risk of physical damage.

**SCHEDULE OF PRIOR YEAR FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2013**

SECTION II – 2013 FINANCIAL STATEMENT FINDINGS (CONTINUED)

Recommendation

The City should investigate either building a secure server room with full physical access and environmental controls, or moving the financial system to an external shared services location with such controls.

Management's Response and Corrective Action

The new finance system will be physically secured. The existing finance system has not been moved to the new server room because the hardware is old, antiquated equipment that is oversized and there is no space for it.

Expected Completion Date and Contact Information

The City plans on being in complete compliance with all controls weaknesses by at least FY 2015.

Responsible parties for corrective action are:

- a. Josh Beta, Finance Director
- b. BreaIT

Status

This finding is no longer considered a material weakness due to the implementation of a new system; however the finding is still warranted for fiscal year ending 2014 due to the use of the legacy system during this period.

8. Application password standards need to be strengthened:
- a. General computer controls require that access to the IT network and applications be properly controlled. The City, however, does not have a formal policy regarding complex password standards for financial application access. The City allows passwords of any length or complexity for accessing the financial system. Without formal requirements, password configuration standards may change based on administrator preference, rather than adherence to standard industry practices. The chance of someone hacking into a financial system increases considerably when strong passwords are not utilized to protect the system.

Recommendation

The City working in conjunction with BreaIT should develop and implement a formal administrative procedure defining the minimum password configuration requirements for the financial system. For example:

Password history:	12 to 24 passwords remembered
Maximum password age:	30 to 90 days
Minimum password age:	1 to 3 days
Minimum password length:	8 to 14 characters
Password must meet complexity requirements:	Enabled
Store password using reversible encryption:	Disabled
Password complexity:	Minimum of eight characters
	Contains at least two numeric or special characters

**SCHEDULE OF PRIOR YEAR FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2013**

SECTION II – 2013 FINANCIAL STATEMENT FINDINGS (CONTINUED)

Management's Response and Corrective Action

The Finance Department published its "Financial Management Policies and Procedures Manual" in November 2013, but only after the difficult work of establishing a balanced FY 2013 budget and the completion of economic settlements and a land sale permanently corrected the economic status of the City of Bell organization. The Manual possesses a plethora of IT policies that will be fine-tuned to the new accounting and finance system.

Expected Completion Date and Contact Information

The City plans on being in complete compliance with all controls weaknesses by at least FY 2015.

Responsible parties for corrective action are:

- a. Josh Beta, Finance Director
- b. BreaIT

Status

This finding is no longer considered a material weakness due to the implementation of a new system; however the finding is still warranted for fiscal year ending 2014 due to the use of the legacy system during this period.

9. Lack of disaster recovery plan:

- a. The City recently implemented a new backup system (Barracuda backup appliance), which sends daily offsite backups of the City's data. However, the City does not have a formal disaster recovery plan. Lack of a disaster recovery plan could result in loss of financial data and business interruptions in the event of a disaster.

Recommendation

The City management working in conjunction with BreaIT should develop and implement a disaster recovery plan that will detail how City functions would operate in the event that the City's IT network and applications are unavailable for an extended period of time, or in the event of a disaster. The disaster recovery plan should include detailed disaster recovery procedures that clearly define the roles and responsibilities of personnel in re-establishing the computer network, financial applications and financial data. Once developed, the plan should be periodically tested to ensure viability. Findings from the testing should be incorporated as updates to the plan.

Management's Response and Corrective Action

A disaster recovery plan will be implemented with the City's new IT consultant in FY 2015.

Expected Completion Date and Contact Information

The City plans on being in complete compliance with all controls weaknesses by at least FY 2015.

**SCHEDULE OF PRIOR YEAR FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2013**

SECTION II – 2013 FINANCIAL STATEMENT FINDINGS (CONTINUED)

Responsible parties for corrective action are:

- a. Josh Beta, Finance Director
- b. BrealT

Status

This finding has been corrected.

10. No documentation/or batch processing procedures/or payroll:

- a. There is no documentation for batch processing procedures of financial information between the City's financial system and the bank for payroll. Batch processing is currently based on the institutional knowledge of those involved.

Recommendation

The process of managing batch jobs to transfer financial information between the City's financial system and the bank for payroll should be reviewed and controls should be implemented to ensure that job scheduling is appropriately controlled and authorized.

Management's Response and Corrective Action

The Finance Department published its "Financial Management Policies and Procedures Manual in November 2013, but only after the difficult work of establishing a balanced FY 2013 budget and the completion of economic settlements and a land sale permanently corrected the economic status of the City of Bell organization. The Manual possesses a plethora of IT policies that will be fine-tuned to the new accounting and finance system.

Expected Completion Date and Contact Information

The City plans on being in complete compliance with all controls weaknesses by at least FY 2015.

Responsible parties for corrective action are:

- a. Josh Beta, Finance Director
- b. BrealT

Status

This finding is no longer considered a material weakness due to the implementation of a new system; however the finding is still warranted for fiscal year ending 2014 due to the use of the legacy system during this period.

**SCHEDULE OF PRIOR YEAR FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2013**

SECTION II – 2013 FINANCIAL STATEMENT FINDINGS (CONTINUED)

MATERIAL NONCOMPLIANCE

Finding 2013-003: Noncompliance with Laws, Regulations, Contracts, and Grant Agreements

Criteria

Governmental entities are subject to a variety of laws, regulations, contracts and grant agreements that have a direct and material effect on their financial statements. Accordingly, governmental entities should establish a system of internal control over compliance to ensure compliance with laws, regulations, contracts and grant agreements.

Condition, Cause and Effect

As a result of financial conditions at the City and weaknesses in internal control over compliance, we noted the following instances of noncompliance with bond covenants, budget policy, and other applicable laws and regulations, contracts and grant agreements:

1. The 2007 Taxable Lease Revenue Bonds and the 2009 Promissory Note are in default as of November 2010 and October 2010 and continue to be in default because the City has defaulted on the payment of principal and interest. Subsequent to year-end, the City has reached legal settlements for both of these defaults, which reduced the outstanding liabilities due on the 2007 Taxable Lease Revenue Bonds and the 2009 Promissory Note to \$28.7 million and \$2.5 million, respectively.
2. In accordance with the Series 2004 and 2007 General Obligation Bonds' Official Statements, the bonds are general obligation bonds of the City payable from ad valorem taxes. The City has the power and is obligated to annually cause to be levied ad valorem taxes upon all property within the City for the payment of the bonds principal and interest. Pledged property tax revenue recognized during the fiscal year ended June 30, 2013, was \$2.0 million against the total debt service payments of \$2.8 million. The City was not in compliance with bond requirements because it did not assess property taxes sufficient to pay the principal and interest on the bonds for the current year.
3. The City deposited RPTTF monies received from the State of California in January 2013, and deposited such monies into the City's General Checking Account and not the CRA account. The City eventually repaid the Successor Agency in February 2014; however, due to the fact that these monies were intended to satisfy the obligations outlined in the Successor Agency's ROPS schedules, the obligations during the time that the RPTTF money was received were not met.
4. The City was not in compliance with reporting provisions of the indentures for the 2003 Tax Allocation Bonds and the 2007 Taxable Revenue Bonds for the fiscal year ended June 30, 2014, because the City's audited financial statement were not issued within 180 days of the year-end. Additionally, the City was not in compliance with continuing disclosure requirements under SEC Rule 15c2-12.
5. In accordance with the former Agency's 2003 Tax Allocation Refunding Bonds Official Statements, the City is required to provide a written Certificate of the former Agency due by 10/1/13 certifying that Tax Revenues Received by the former Agency through the date of the certificate combined with the amount remaining to be paid on all outstanding obligations of the former Agency will not exceed the maximum amount of tax revenues to be divided and allocated to the former Agency pursuant to the former Agency's Redevelopment Plan.

**SCHEDULE OF PRIOR YEAR FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2013**

SECTION II – 2013 FINANCIAL STATEMENT FINDINGS (CONTINUED)

6. The City's charter stipulates that actual expenditures may not exceed budgeted appropriations at the department level within the General Fund and at the fund level for other funds without City Council approval. The City's actual General Fund expenditures exceeded the General Fund budget appropriations by a total of \$7.6 million for 12 departments. The City's actual Retirement Special Revenue Fund expenditures exceeded the Retirement Special Revenue Fund budget appropriations by a total of \$1.0 million.
7. The City purchased 5 years of Additional Retirement Service Credits (ARSC) on behalf of the former CAO, the former ACAO, 5 former council members and 4 former department heads between 2005 and 2009 using City funds with an approximate cost of \$1,000,000. CalPERS has made a determination that the purchase of ARSC using City funds for one of the former department heads was not lawful under the Public Employee Retirement Law. In January 2013, the former CAO waived the purchased of ARSC. However, the determination on the remaining purchases of ARSC is pending.
8. The State Controller's Office (SCO) review of the former Agency for the period July 1, 2000, through June 30, 2011, identified that the former Agency failed to comply with Health and Safety Code requirements in several areas and inappropriately charged the former Agency funds in the amount of \$664,834. This is pending final resolution.
9. The SCO's audit of the City's administrative and internal accounting system for the period July 1, 2008, through June 30, 2010, identified that the City improperly increased assessments of the Sanitation and Sewerage Assessment System and business licenses taxes. The SCO estimated the amount of overcharge is \$621,737 and \$2,105,441 for assessment of the Sanitation and Sewerage Assessment System and business licenses taxes, respectively. On a follow-up review by the SCO dated May 22, 2013, the SCO estimated the amount of overcharge is \$822,000 and \$2,355,000 for assessment of the Sanitation and Sewerage Assessment System and business licenses taxes, respectively. This is pending final resolution.

Recommendation

We recommend that the City develop, document, and implement policies and procedures to ensure the City's compliance with applicable laws, regulations, contracts and grant agreements. We also recommend that the City's budget process include a mid-year and year-end comparison of budget and actual amounts to allow City Council an opportunity to take any action deemed necessary to ensure compliance with local laws and regulations governing budget appropriations and related expenditures. In addition, we recommend that the City work with the SCO and CalPERS to resolve pending issues.

Management's Response and Corrective Action

Current management and elected officials are well aware of the criminal acts and improprieties of former management and City Council. The City of Bell's permanent administration, in place since October 2012, is committed to ensuring that there is proper documentation, authority, approvals and adherence to the rules and policies for the future City of Bell.

The two-year period following the Bell scandal of 2010 found the Finance Department unable and unequipped to meet the transactional workload of a viable municipal finance department. Key personnel transitioned from the workforce, staffing was reduced, and much of the Department's attention was directed to meeting the requirements of outside audit and investigation and public records requests. The City is quite aware of the existing weaknesses and the new permanent management team, in place since October 2012, is committed to work out all of these issues. Substantial compliance has been achieved in FY 2013 and FY 2014.

CITY OF BELL

**SCHEDULE OF PRIOR YEAR FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2013**

SECTION II – 2013 FINANCIAL STATEMENT FINDINGS (CONTINUED)

Responsible parties for corrective action are the permanently appointed City of Bell executive management team.

Status

Items 1 and 2 above have been corrected; the remaining non-compliance items are still pending to be corrected as of June 30, 2014.

SECTION III - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

No matters were reported.