

CITY OF YUBA CITY
MANAGEMENT REPORT
AND
AUDITOR'S COMMUNICATION LETTER

June 30, 2014

CITY OF YUBA CITY
June 30, 2014

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November 26, 2014

Members of the City Council
City of Yuba City
1201 Civic Center Blvd.
Yuba City, CA 95993

In planning and performing our audit of the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Yuba City, California (City), as of and for the fiscal year ended June 30, 2014, in accordance with auditing standards generally accepted in the United States of America, we considered the City's internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control. Accordingly, we do not express an opinion on the effectiveness of the City's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all such deficiencies have been identified. As discussed below, we identified a significant deficiency and other matters related to internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency or 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.

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. During our audit, we noted one significant deficiency, described in the accompany schedule of current year recommendations as Finding #2014-01.

During our audit we also noted certain other matters involving internal controls and their operations, and are submitting, for your consideration, related recommendations designed to help the City make improvements and achieve operational efficiencies. These recommendations are described in the current year recommendations section as Findings 2014-02 through 2014-10. Our comments reflect our desire to be of continuing assistance to the City.

We would be pleased to discuss the recommendations in further detail at your convenience, to perform any additional study of these matters, or to assist you in implementing these recommendations.

We have included in this letter a summary of communication with the City Council as required by professional auditing standards. We would like to thank the City's management and staff for the courtesy and cooperation extended to us during the course of our engagement.

The accompanying communications and recommendations are intended solely for the information and use of management, the City Council, and others within the organization, and is not intended to be and should not be used by anyone other these specified parties.

Moss, Levy & Hartzheim

Moss, Levy & Hartzheim, LLP
Culver City, California



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November 26, 2014

Members of the City Council
City of Yuba City
1201 Civic Center Blvd.
Yuba City, CA 95993

We have audited the financial statements of the governmental activities, business-type activities, each major fund, and the aggregate remaining fund information of the City of Yuba City (City) for the fiscal year ended June 30, 2014. Professional standards require that we provide you with the information about our responsibilities under auditing standards generally accepted in the United States of America, *Government Auditing Standards*, and OMB Circular A-133, as well as certain information related to the planned scope and timing of our audit. We have communicated such information in our letter to you dated June 9, 2014. Professional standards also require that we communicate to you the following information related to our audit.

Significant Audit Findings

Qualitative Aspects of Accounting Practices

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by the City are described in Note 1 to the basic financial statements. As discussed in Note 1 of the notes to the basic financial statements, four new accounting policies were adopted during the fiscal year. The new policies are Governmental Accounting Standards Board (GASB) Statements No. 65, 66, 67, and 70. Only GASB Statement No. 65 had an effect on the financial statements. See Note 4 and Note 6 for the effect on the financial statements. We noted no transactions entered into by the City during the fiscal year for which there is a lack of authoritative guidance or consensus. All significant transactions have been recognized in the financial statements in the proper period.

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

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

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

Difficulties Encountered in Performing the Audit

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

Corrected and Uncorrected Misstatements

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management. Management has corrected all such misstatements. In addition, three of the misstatements detected as a result of audit procedures and corrected by management were material, either individually or in the aggregate, to the financial statements taken as a whole. These adjustments were for the fair market value (GASB 31) adjustment for investments, to adjust bond issue costs to zero (GASB 65), and to adjust loans receivable to their actual balances.

Disagreements with Management

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

Management Representations

We have requested certain representations from management that are included in the management representation letter dated November 26, 2014.

Management Consultations with Other Independent Accountants

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

Other Audit Findings or Issues

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

Other Matters

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

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

Very truly yours,

Moss, Levy & Hartzheim

MOSS, LEVY & HARTZHEIM, LLP
Culver City, CA

CURRENT YEAR RECOMMENDATIONS

Significant Deficiency

2014-01 Finding – Deficiencies in cash receipts:

During our test of cash receipts, we noted the check numbers are not being recorded on the cash register tape at the Police Department and that the cash receipts are locked in the cash register at night. We also noted deficiencies in the following departments:

- a.) One police receipt was over 7 days from the date of receipt until the time of deposit with Finance (#02098170667).
- b.) Four fire department receipts were over 7 days from the date of receipt until the time of deposit with Finance (#02098167952, #02098170624, #02098173566, and #04000104461).

Effect:

Lack of check numbers on the cash register tape at the Police Department makes it difficult to trace payments paid by check. Locking the cash receipts in the cash register is a deficiency in internal control due to the access of the cash register. Also, lack of timeliness in depositing cash receipts to the Finance Department results in lost investment income and could result in the receipts being misplaced or a misappropriation of funds occurring.

Recommendation:

We recommend that all check numbers be referenced on the cash register tape and that the cash receipts be locked in the safe/vault at night. We also recommend that all receipts be deposited with the Finance department on a daily basis during business days.

Management's Response:

Recommendation will be implemented.

Other Matters

2014-02 Finding – Lack of approval for fee changes:

During our audit, we noted the changes in fees for the Parks & Recreation Department and Gauche Aquatic Park (GAP) were not approved by City Council. We also noted discrepancies in fees charged at the GAP due to the timing of the publishing of the activity guide.

Effect:

Without Council approval for fee schedules, the City may be charging customers incorrect/unauthorized fees.

Recommendation:

We recommend that the City have all fee schedules approved by the City Council.

Management's Response:

Recommendation will be implemented. Staff will notify City Council by memo of any changes to the recreation class fees established by the Activity Guide, prior to the effective date of the adjusted fee, under the authority of the City Manager in Section 3-8 of the municipal code.

CURRENT YEAR RECOMMENDATIONS (Continued)

Other Matters (Continued)

2014-03 Finding – Lack of transfer of property to Successor Agency:

During our audit, we noted that real property that was originally transferred to the City to repay interfund advances from the general fund has been deemed an invalid transfer. Due to this invalid transfer, the properties need to be deeded to the Successor Agency, but were not as of June 30, 2014.

Effect:

The Successor Agency is the rightful owner of these properties, yet they have not been deeded to the Successor Agency as of yet.

Recommendation:

We recommend that the City deed the titles of this property to the Successor Agency immediately.

Management's Response:

Recommendation was fully implemented November 13, 2014 when Grant Deeds were recorded with Sutter County.

2014-04 Finding – Control deficiencies over Parks & Recreation cash receipts:

During our test of cash receipts, we noted that any overage amounts collected for Parks and Recreation cash receipts are kept in a separate envelope and the money is used to balance any deficit balances in subsequent days. If it is not used, the amount is deposited with cash receipts. Also the key to the cash drawer is kept unlocked in an employee's desk.

Effect:

By using overage amounts to balance any deficit amounts, it adversely affects the City's ability to record and track cash receipts reliably, which can lead to a misappropriation of funds. Also, without the key to the cash drawer being kept in a secured and locked location, a misappropriation or theft of funds could occur.

Recommendation:

We recommend that the City deposit all cash receipts daily regardless of any overage or under amounts and that the key to the cash drawer be kept in a secured and locked location with limited access.

Management's Response:

Recommendation will be implemented.

2014-05 Finding – Control deficiencies over Fire Department cash receipts:

During our test of cash receipts, we noted the Fire Department deposits are not reviewed by a second party prior to remittance to the Finance Department.

Effect:

Without a second review of receipts prior to remittance to the Finance Department, a misappropriation of funds could occur and go undetected.

CURRENT YEAR RECOMMENDATIONS (Continued)

Other Matters (Continued)

Recommendation:

We recommend that an employee from the Fire Department, other than the preparer of the deposit, review each deposit prior to being remitted to the Finance Department.

Management's Response:

Recommendation will not be implemented as there are times when only one employee is present and there is not a second person to do the review. This procedure would create redundancy with little benefit gained.

2014-06 Finding – Lack of a fraud reporting policy:

During our fraud interviews with various City employees, we noted that many employees were not aware of the procedures to report suspected fraud. Moreover, there is no formal written City policy for employees to report suspected fraud.

Effect:

If employees are not aware of their options to report suspected fraud, there is a less likely chance of the employees actually reporting their suspicions, which could cause fraud to occur and go undetected.

Recommendation:

We recommend that the City implement a formal fraud reporting policy and educate City employees of the procedures to report suspected fraud.

Management's Response:

Recommendation will be implemented.

2014-07 Finding – Control deficiencies over senior center cash receipts:

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

1. Activity cards at the senior center are not pre-numbered.
2. Rummage sales are held once per year, but no receipts are issued to customers.

Effect:

Without the pre-numbering of activity cards, there is a possibility of fraud to occur in which duplicate activity cards are produced. Also, without the issuance of receipts there is no way to track rummage sales, which could also lead to a misappropriation of funds.

Recommendation:

We recommend that the City pre-number the activity cards at the senior center and that pre-numbered receipts be utilized at all rummage sales.

Management's Response:

Recommendation will be implemented.

CURRENT YEAR RECOMMENDATIONS (Continued)

Other Matters (Continued)

2014-08 Finding – Loans are not entered into the loan system (GMS) in a timely manner:
During our audit of loans receivable, we noted that loans are not entered into the loan system (GMS) at the time of issuance resulting in two loans not being entered as of 6/30/2014. Also, adjusting year-end journal entries prepared by the client were incorrect.

Effect:

Loans not entered into the GMS system could be unaccounted for during the audit and incorrect year-end journal entries result in incorrect year-end balances in the general ledger.

Recommendation:

We recommend all loans be entered into the system in a timely manner and that all journal entries be reviewed for accuracy.

Management's Response:

Recommendation will be implemented.

2014-09 Finding – Negative cash balance in the general ledger:
During our review of cash, we noted that the pooled cash had a negative book balance of \$2,163,713.81 as of 6/30/2014.

Effect:

A negative cash balance at fiscal year-end implies that the bank account could be overdrawn and there is a possibility of insufficient funds, which could negatively impact the operations of the City.

Recommendation:

We recommend the City monitor the cash balance on a daily basis and avoid issuing checks if there is insufficient cash in the bank.

Management's Response:

The book balance was negative, but the bank account balance was not negative as the City had issued several large checks at the end of the fiscal year. These checks did not clear the City's bank account prior to the City depositing \$4 million from its investment account the very next day. Staff has historically used check issuance timing to maximize investment earnings. In the future, the City will ensure that the book balance is not negative, particularly at month and fiscal year-end.

2014-10 Finding – Lack of compliance with IRS tax regulations:
During our test of controls, we noted that the City does not report gift cards given to employees under their SIP program as taxable income to employees.

Effect:

The City is not in compliance with IRS tax regulations.

Recommendation:

We recommend the City report all gift card amounts as supplemental wages on the employee's W-2.

CURRENT YEAR RECOMMENDATIONS (Continued)

Other Matters (Continued)

Management's Response:

Recommendation will be implemented beginning with calendar year 2015 W-2s, after City employees have been notified and reporting procedures are put in place for staff to report the additional compensation.

STATUS OF PRIOR YEAR RECOMMENDATIONS

2013-01 Finding – Deficiencies in cash receipt deposits:

During our test of cash receipts, we noted that two Parks and Recreation receipts and two senior center daily receipts were not deposited timely (within one week).

Effect:

Lack of timeliness in depositing cash receipts to the Finance Department results in lost investment income and could result in the receipts being misplaced or a misappropriation of funds occurring.

Recommendation:

We recommend that cash receipts be deposited on a daily basis.

Status:

Not Implemented. See Finding 2014-01.

2013-02 Finding – Lack of transfer of property to Successor Agency:

During our audit, we noted that real property that was originally transferred to the City to repay interfund advances from the general fund has been deemed an invalid transfer. Due to this invalid transfer, the properties need to be deeded to the Successor Agency, but were not as of June 30, 2014.

Effect:

The Successor Agency is the rightful owner of these properties, yet they have not been deeded to the Successor Agency as of yet.

Recommendation:

We recommend that the City deed the titles of this property to the Successor Agency immediately.

Status:

Not Implemented. See Finding 2014-03.

2013-03 Finding – Deficiencies in internal control at the Parks and Recreation Department:

During our review of internal control at the Parks and Recreation Department, we noted that there was no random spot-checking and roll-taking of participants (by a City employee) in recreation classes.

Effect:

There is an increased risk that errors and irregularities may occur and go undetected. It adversely affects the City's ability to initiate, authorize, record, process, or report financial data reliably, which can lead to a misappropriation of funds.

Recommendation:

We recommend that a supervisor perform random spot-checking and roll-taking of participants in the recreation classes, to ensure that the roster reconciles to the actual participants in attendance.

Status:

Implemented.

STATUS OF PRIOR YEAR RECOMMENDATIONS (Continued)

2013-04 Finding –Lack of a formal capital asset policy:

During our audit, we noted that the City has no formal capital asset policy.

Effect:

Employees do not have a policy to follow in regards to the capitalization of fixed assets.

Recommendation:

We suggest that the City implement a written policy that is in compliance with the City's current practice of capitalizing fixed assets.

Status:

Implemented.

2013-05 Finding – Control deficiencies over Parks & Recreation cash receipts:

During our test of cash receipts, we noted that any overage amounts collected for Parks and Recreation cash receipts are kept in a separate envelope and the money is used to balance any deficit balances the next day or two. If it is not used, the amount is deposited with cash receipts. Also the key to the cash drawer is kept hidden on an employee's desk.

Effect:

By using overage amounts to balance any deficit amounts, it adversely affects the City's ability to record and track cash receipts reliably, which can lead to a misappropriation of funds. Also, without the key to the cash drawer being kept in a secured and locked location, a misappropriation or theft of funds could occur.

Recommendation:

We recommend that the City deposit all cash receipts daily regardless of any overage or under amounts and that the key to the cash drawer be kept in a secured and locked location with limited access.

Status:

Not Implemented. See Finding 2014-04.

2013-06 Finding – Control deficiencies over Fire Department cash receipts:

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

1. Fire Department deposits are not reviewed by a second party prior to remittance to the Finance Department.
2. The Fire Department deposits their cash receipts in the Finance Department's inbox instead of taking the deposit to the cashier.
3. Two Fire Department receipts were entered as zero into the general ledger and shown as cash overage for one day in the amount of \$7.
4. There is no double-checking by the Fire Department to ensure that all receipts are entered into the general ledger.

STATUS OF PRIOR YEAR RECOMMENDATIONS (Continued)

Effect:

Without a second review of receipts prior to remittance to the Finance Department, a misappropriation of funds could occur and go undetected. By depositing the cash receipts in the Finance inbox there is no way to ensure that all of the cash receipts are being deposited. Also without the double-checking by the Fire Department to ensure that all receipts are entered into the general ledger, it could lead to incorrect postings in the general ledger and misstatements in the financial statements.

Recommendation:

We recommend that an employee from the Fire Department, other than the preparer of the deposit, review each deposit prior to being remitted to the Finance Department and that the Fire Department bring all of their cash receipts directly to the cashier for receipting. We also recommend that an employee review the general ledger to ensure that all receipts are being properly recorded on a monthly basis.

Status:

Partially Implemented. See Finding 2014-05.

2013-07 Finding – Lack of a fraud reporting policy:

During our fraud interviews with various City employees, we noted that many employees were not aware of the procedures to report suspected fraud. Moreover, there is no formal written City policy for employees to report suspected fraud.

Effect:

If employees are not aware of their options to report suspected fraud, there is a less likely chance of the employees actually reporting their suspicions, which could cause fraud to occur and go undetected.

Recommendation:

We recommend that the City implement a formal fraud reporting policy and educate City employees of the procedures to report suspected fraud.

Status:

Not Implemented. See Finding 2014-06.

2013-08 Finding – Control deficiencies over senior center cash receipts:

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

3. Activity cards at the senior center are not pre-numbered.
4. Cash receipts are kept in an unlocked drawer during the day.
5. The multi-media class instructor collects class fees during the class on occasion, and then slips the money under the door of the office.
6. Rummage sales are held once per year, but no receipts are issued to customers.
7. The petty cash money, for change, is kept in an unlocked drawer.

Effect:

Without the pre-numbering of activity cards, there is a possibility of fraud to occur in which duplicate activity cards are produced. Unlocked cash drawers and petty cash and the collection of class fees during the class could result in a misappropriation of funds occurring and going undetected. Also, without the issuance of receipts there is no way to track rummage sales, which could also lead to a misappropriation of funds.

STATUS OF PRIOR YEAR RECOMMENDATIONS (Continued)

Recommendation:

We recommend that the City pre-number the activity cards at the senior center and that cash receipts and petty cash be kept in a locked drawer at all times. We also recommend that class fees be collected at the front desk only. In addition, we recommend that pre-numbered receipts be utilized at all rummage sales.

Status:

Partially Implemented. See Finding 2014-07.

2013-09 Finding – Four loans written off without Council approval or notification:

During our audit of loans receivable, we noted four loans that were written off in fiscal year 12/13 without City Council approval or notification.

Effect:

Without City Council approval or notification, we are unable to determine if the City Council was aware of these write-offs.

Recommendation:

We recommend that all loan write-offs be brought before the City Council for notification, guidance, and approval of writing off, if desired.

Status:

Implemented.