

**CITY OF BENICIA
MEMORANDUM ON INTERNAL CONTROL
AND
REQUIRED COMMUNICATIONS
FOR THE YEAR ENDED JUNE 30, 2015**

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**CITY OF BENICIA
MEMORANDUM ON INTERNAL CONTROL
AND
REQUIRED COMMUNICATIONS**

For The Year Ended June 30, 2015

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MEMORANDUM ON INTERNAL CONTROL

To the City Council of
the City of Benicia, California

In planning and performing our audit of the basic financial statements of the City of Benicia as of and for the year ended June 30, 2015, in accordance with auditing standards generally accepted in the United States of America, we considered the City's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control. Accordingly, we do not express an opinion on the effectiveness of the City's internal control

Our consideration of internal control was for the limited purpose described in the preceding paragraph 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 and that were not identified. In addition, because of inherent limitations in internal control, including the possibility of management override of controls, misstatements due to error or fraud may occur and not be detected by such controls. However, as discussed below, we identified certain deficiencies in internal control that we consider to be significant deficiencies.

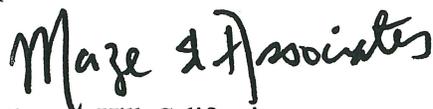
A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the City's financial statements will not be prevented, or detected and corrected on a timely basis. We did not identify any deficiencies in internal control that we consider to be material weaknesses.

A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies in internal control included on the Schedule of Significant Deficiencies to be significant deficiencies.

Included in the Schedule of Other Matters are recommendations not meeting the above definitions that we believe are opportunities for strengthening internal controls and operating efficiency.

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

This communication is intended solely for the information and use of management, City Council, others within the organization, and agencies and pass-through entities requiring compliance with *Government Auditing Standards*, and is not intended to be and should not be used by anyone other than these specified parties.

A handwritten signature in black ink that reads 'Maze & Associates' in a cursive, stylized font.

Pleasant Hill, California
January 28, 2016

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CITY OF BENICIA
MEMORANDUM ON INTERNAL CONTROL
SCHEDULE OF SIGNIFICANT DEFICIENCIES

2015-01: Review of Payroll Register

Criteria: A payroll register should be reviewed and signed for approval by an employee who does not process payroll. Without a review by a second employee, there is a risk that the payroll register may include omissions and errors.

Condition: During our review of internal controls over the City's payroll cycle, we noted the City currently does not perform a review of the payroll run.

Cause: We were informed by the City management that the City is aware of the importance of a review as part of the internal controls. However, the current set up of the payroll system does not produce reports to allow for a meaningful review. The City expects to implement this review process in the new system.

Effect: Without the involvement of a second employee reviewing payroll runs, there is a risk that the payroll register may include omissions and errors.

Recommendation: We recommend that the City establish procedures to have an employee, who does not have access to payroll module and payroll database, to review payroll runs. This employee should also document that the review has taken place (e.g. by signing off on the payroll register) in order to allow for monitoring of such review activities.

Management's Response: The City concurs with the finding and recommendation. The City is currently implementing a new ERP system that includes a payroll module that produces meaningful payroll reports that management can review and approve. New payroll procedures are being established and the Finance Director will be reviewing and approving the payroll registers once the payroll module is live. In the meantime, the Assistant Finance Director is reviewing and approving any changes, including new employees, termination, and step increases, which are entered into the system when a Personnel Action Form (PAF) is sent by the Human Resources Department.

2015-02: Access to the Payroll Database

Criteria: The function of payroll processing and editing of payroll database should be segregated.

Condition: During the audit, we noted that the City's Account System Supervisor, whose responsibilities include entering timesheets, processing payroll and holding unclaimed W-2's, also has access to unclaimed paychecks and payroll database. In addition, the City's Account System Supervisor has edit access to the employee database which includes setting up new employees in the payroll module.

Cause: All payroll duties are performed by the Account System Supervisor due to the City did not train other employees for the payroll processing.

Effect: The combination of the ability to process payroll, access to unclaimed W-2's and paychecks, as well as altering data in the payroll and employee databases creates opportunities for fake employees, and unauthorized changes in payroll data such as pay rates and vacation accruals.

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SCHEDULE OF SIGNIFICANT DEFICIENCIES

Recommendation: As we discussed in Significant Deficiency 2015-01 above, another employee needs to be involved in the review of the payroll process. In addition, the City should segregate the duties of the maintenance of the two databases from payroll processing. Employee who can alter data in the payroll or employee database should not have the ability to process payroll.

Management's Response: The City concurs with the finding and recommendation. As the City is in the process of implementing a new ERP system, procedures and policies are being reviewed and established. The segregation of duties is being reviewed carefully and all Human Resources duties and functions will be performed by a Human Resources staff member, such as setting up new employees and making changes to personnel data. Only payroll functions will remain with the Finance Department. Currently, the Senior Accounting Technician is being cross-trained in payroll to alleviate any omissions and errors that may occur.

2015-03: Governmental/Utilities Cash Receipts Procedures

Criteria: For proper internal control, there should be segregation of duties between cash receipts collection and customer database maintenance. Without the segregation, the City could be exposed to the risk of interception of cash receipts

Condition: Currently, the Customer Service Representatives, who are responsible for governmental and utility billings, have access to cash receipts and general ledger. They also have access to customer database, can adjust the utility accounts for individual customers and are responsible in preparing the daily deposit bags. The Customer Service Representatives are given so much access because they are responsible for billing and revenue collection, as well as recording of receivables.

Cause: All collection duties and recording of collections is done by the customer service representative at the front desk. Since all recording is done upon collection, access is granted to the customer service representative.

Effect: The City is exposed to the risk of interception of cash receipts.

Recommendation: To strengthen internal control, the following functions should be segregated:

- Revenue collection versus adjustments of customer accounts
- Access to cash receipts versus review of cash receipts batches and preparation of deposit bags
- Access to cash receipts versus general ledger, without an approval of a second employee

Management's Response: The City concurs with the finding and recommendation. City management has reviewed, approved and implemented new procedures in cash handling, as a result of a third party audit. Various departments are also following the new procedures established by the Finance Director. In addition, the hiring of a Finance Account Clerk, who is mainly responsible for the front desk function, receiving customer payments without any access to the database reinforces and strengthens internal control. Cash receipt journals are reviewed and approved by either the Accounting System Supervisor or the Assistant Finance Director. With the new ERP system, all procedures and policies are being reviewed for better internal control.

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SCHEDULE OF OTHER MATTERS

NEW GASB PRONOUNCEMENTS OR PRONOUNCEMENTS NOT YET EFFECTIVE

The following comment represents new pronouncements taking effect in the next few years. We have cited them here to keep you abreast of developments:

Effective in fiscal year 2015-16

GASB 72 – *Fair Value Measurement and Application*

This Statement addresses accounting and financial reporting issues related to fair value measurements. The definition of *fair value* is the price that would be received to sell an asset or pay to transfer a liability in an orderly transaction between market participants at the measurement date. This Statement provides guidance for determining a fair value measurement for financial reporting purposes. This Statement also provides guidance for applying fair value to certain investments and disclosures related to all fair value measurements.

GASB 76 - *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*

The objective of this Statement is to identify, in the context of the current governmental financial reporting environment, the hierarchy of generally accepted accounting principles (GAAP). The “GAAP hierarchy” consists of the sources of accounting principles used to prepare financial statements of state and local governmental entities in conformity with GAAP and the framework for selecting those principles. This Statement reduces the GAAP hierarchy to two categories of authoritative GAAP and addresses the use of authoritative and non-authoritative literature in the event that the accounting treatment for a transaction or other event is not specified within a source of authoritative GAAP. This Statement supersedes Statement No. 55, The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments.

Effective in fiscal year 2016-17:

GASB 73 – *Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68*

This Statement establishes requirements for defined benefit pensions that are not within the scope of Statement No. 68, *Accounting and Financial Reporting for Pensions*, as well as for the assets accumulated for purposes of providing those pensions. In addition, it establishes requirements for defined contribution pensions that are not within the scope of Statement 68. It also amends certain provisions of Statement No. 67, *Financial Reporting for Pension Plans*, and Statement 68 for pension plans and pensions that are within their respective scopes.

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SCHEDULE OF OTHER MATTERS

GASB 74 – Financial Reporting for Post-employment Benefit Plans Other Than Pension Plans

The objective of this Statement is to improve the usefulness of information about post-employment benefits other than pensions (other post-employment benefits or OPEB) included in the general purpose external financial reports of state and local governmental OPEB plans for making decisions and assessing accountability. This Statement results from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for all post-employment benefits (pensions and OPEB) with regard to providing decision-useful information, supporting assessments of accountability and inter-period equity, and creating additional transparency.

GASB 77 – Tax Abatement Disclosures

This Statement establishes financial reporting standards for tax abatement agreements entered into by state and local governments. The disclosures required by this Statement encompass tax abatements resulting from both (a) agreements that are entered into by the reporting government and (b) agreements that are entered into by other governments and that reduce the reporting government's tax revenues.

Effective in fiscal year 2017-18:

GASB 75 – Accounting and Financial Reporting for Post-employment Benefits Other Than Pensions

The primary objective of this Statement is to improve accounting and financial reporting by state and local governments for post-employment benefits other than pensions (other post-employment benefits or OPEB). It also improves information provided by state and local governmental employers about financial support for OPEB that is provided by other entities. This Statement results from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for all post-employment benefits (pensions and OPEB) with regard to providing decision-useful information, supporting assessments of accountability and inter-period equity, and creating additional transparency.

REQUIRED COMMUNICATIONS

To the City Council of
the City of Benicia, California

We have audited the basic financial statements of the City of Benicia for the year ended June 30, 2015. Professional standards require that we communicate to you the following information related to our audit under generally accepted auditing standards and, *Government Auditing Standards*.

Significant Audit Findings

Accounting Policies

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 financial statements. No new accounting policies were adopted and the application of existing policies was not changed during the year, except as follows:

The following Governmental Accounting Standards Board (GASB) pronouncements became effective, but did not have a material effect on the financial statements:

GASB Statements No. 69 – *Government Combinations and Disposals of Government Operations*

The following pronouncements became effective, and as disclosed in Note 1 to the financial statements required a prior period restatement for the cumulative effect on the financial statements.

GASB Statement No. 68 – *Accounting and Financial Reporting for Pensions, an Amendment of GASB Statement No. 27*

This Statement establishes standards for measuring and recognizing liabilities, deferred outflows of resources, and deferred inflows of resources, and expense/expenditures. For defined benefit pensions, this Statement identifies the methods and assumptions that should be used to project benefit payments, discount projected benefit payments to their actuarial present value, and attribute that present value to periods of employee service.

Note disclosure and required supplementary information requirements about pensions also are addressed. Distinctions are made regarding the particular requirements for employers based on the number of employers whose employees are provided with pensions through the pension plan and whether pension obligations and pension plan assets are shared.

In addition, this Statement details the recognition and disclosure requirements for employers with liabilities (payables) to a defined benefit pension plan and for employers whose employees are provided with defined contribution pensions. This Statement also addresses circumstances in which a non-employer entity has a legal requirement to make contributions directly to a pension plan.

GASB Statement No. 71 – Pension Transition for Contributions Made Subsequent to the Measurement Date, an Amendment of GASB Statement No. 68

The objective of this Statement is to address an issue regarding application of the transition provisions of Statement No. 68, Accounting and Financial Reporting for Pensions. The issue relates to amounts associated with contributions, if any, made by a state or local government employer or non-employer contributing entity to a defined benefit pension plan after the measurement date of the government's beginning net pension liability.

Unusual Transactions, Controversial or Emerging Areas

We noted no transactions entered into by the City during the 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

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 City's financial statements were:

Estimated Net Pension Assets and Liabilities and Pension-Related Deferred Outflows and Inflows of Resources: Management's estimate of the net pension assets and liabilities and deferred outflows/inflows of resources are disclosed in Note 10 to the financial statements and are based on actuarial studies determined by a consultant, which are based on the experience of the City. We evaluated the key factors and assumptions used to develop the estimate and determined that it is reasonable in relation to the basic financial statements taken as a whole.

Estimated Fair Value of Investments: As of June 30, 2015, the City held approximately \$47.8 million of cash and investments as measured by fair value as disclosed in Note 3 to the financial statements. Fair value is essentially market pricing in effect as of June 30, 2015. These fair values are not required to be adjusted for changes in general market conditions occurring subsequent to June 30, 2015.

Estimate of Depreciation: Management's estimate of the depreciation is based on useful lives determined by management. These lives have been determined by management based on the expected useful life of assets as disclosed in Note 6 to the financial statements. We evaluated the key factors and assumptions used to develop the depreciation estimate and determined that it is reasonable in relation to the basic financial statements taken as a whole.

Estimate of Compensated Absences: Accrued compensated absences which are comprised of accrued vacation, holiday, and certain other compensating time is estimated using accumulated unpaid leave hours and hourly pay rates in effect at the end of the fiscal year as disclosed in Note 1G to the financial statements. We evaluated the key factors and assumptions used to develop the accrued compensated absences and determined that it is reasonable in relation to the basic financial statements taken as a whole.

Disclosures

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

Difficulties Encountered in Performing the Audit

We encountered no significant 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 clearly trivial, and communicate them to the appropriate level of management. Management has corrected all such misstatements. In addition, none of the misstatements detected as a result of audit procedures and corrected by management were material, either individually or in the aggregate, to each opinion unit's financial statements taken as a whole.

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 a management representation letter dated January 28, 2016.

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 Information Accompanying the Financial Statements

We applied certain limited procedures to the required supplementary information that accompanies and supplements the basic financial statements. Our procedures consisted of inquiries of management regarding the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We did not audit the required supplementary information and do not express an opinion or provide any assurance on the required supplementary information.

We were engaged to report on the supplementary information, which accompanying the financial statements but are not required supplementary information. With respect to this supplementary information, 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.

We were not engaged to report on the Introductory and Statistical Sections included as part of the Comprehensive Annual Financial Report but are not required supplementary information. We did not audit or perform other procedures on this other information and we do not express an opinion or provide any assurance on it.

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

Maze & Associates

Pleasant Hill, California
January 28, 2016