

CITY OF HEALDSBURG
MANAGEMENT REPORT
AND
AUDITOR'S COMMUNICATION LETTER

June 30, 2013

CITY OF HEALDSBURG
June 30, 2013

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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 Healdsburg (City), as of and for the fiscal year ended June 30, 2013, in accordance with auditing standards generally accepted in the United States of America, we considered the City's internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinion 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. However, as discussed below, we identified certain deficiencies in internal control that we consider to be significant deficiencies.

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

A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies presented in the current year recommendations section as Findings 2013-01 and 2013-02 to be significant deficiencies in internal control.

During our audit, we noted other matters involving internal controls and their operations, and are submitting for your consideration, related recommendations designed to help the City make improvements and achieve operational efficiencies. These recommendations are described in the current year recommendations section as Findings 2013-03 through 2013-05. Our comments reflect our desire to be of continuing assistance to the City.

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

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

Moss, Levy & Hartzheim

MOSS, LEVY & HARTZHEIM, LLP
Culver City, CA
March 3, 2014



MOSS, LEVY & HARTZHEIM LLP

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We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Healdsburg for the fiscal year ended June 30, 2013, and have issued our report thereon dated March 3, 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 and, if applicable, 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 dated May 28, 2013. Professional standards also require that we communicate to you the following information related to our audit.

Significant Audit Findings

Qualitative Aspects of Accounting Practices

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by the City are described in Note 1 to the basic financial statements. As discussed in Note 1 of the notes to the basic financial statements, four new accounting policies were adopted during the fiscal year. The new policies are Governmental Accounting Standards Board (GASB) Statements No. 60, 61, 62, and 63. GASB Statement No. 62 and 63 had an effect on the financial statements. See Note 1L 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, allowance for uncollectable accounts and notes, and consultant's estimates for postemployment benefits payable. We evaluated the key factors and assumptions used to develop the estimates above in determining that they are reasonable in relation to the financial statements taken as a whole.

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

Difficulties Encountered in Performing the Audit

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

Corrected and Uncorrected Misstatements

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management. Management has corrected all such misstatements. In addition, one of the misstatements detected as a result of audit procedures and corrected by management was material, either individually or in the aggregate, to each opinion unit's financial statements taken as a whole. This was the issue of the pension obligation bonds and the corresponding pay off of the CalPERS side fund.

Disagreements with Management

For purposes of this letter, professional standards define a disagreement with management as 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 March 3, 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 of Healdsburg'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 of Healdsburg'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 members of the City Council of the City of Healdsburg and management of the City of Healdsburg 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
March 3, 2014

CURRENT YEAR RECOMMENDATIONS

Significant Deficiencies

2013-01 Finding – Lack of segregation of duties at the Senior Center:

During our review of internal control over cash receipts at the Senior Center, we noted the person who collects money also reconciles the cash receipts at the end of the day. In addition, no other person reviews or approves the reconciliations.

Effect:

A lack of segregation of duties and controls over cash receipts increases the risk that errors and irregularities may occur and go undetected, which could lead to a misappropriation of funds.

Recommendation:

We recommend that the City of Healdsburg (City) ensures that there is a sufficient segregation of duties over cash receipts at the Senior Center.

Management's response:

The Senior Center front counter is staffed by senior volunteers. Finance staff has counseled them on the appropriate steps to follow. The City is unable to staff the Senior Center with regular staff and segregate duties any more than is currently done.

2013-02 Finding – Lack of control over capital assets:

During the review of internal controls over capital assets, the following were noted:

1. Assets purchased with federal funds may not be identified.
2. There is no listing by department of potential impaired assets.
3. Physical inventory should be performed and reconciled with the capital asset listing annually.

Effect:

Without an annual review, the City's capital assets schedule may not be updated for obsolete, impaired, and disposed capital assets, which could result in a misstatement of the value of capital assets. Consistent use of the capitalization policies is needed to have an accurate classification of the City's capital assets.

Recommendation:

We recommend the City implement procedures to review capital assets at least annually and update the capital assets schedule, accordingly.

Management's response:

The City will implement a policy to ensure that capital assets are reviewed on an annual basis and the schedule adjusted accordingly. Staff will identify all capital assets which are no longer in service and record disposition of them in Fiscal Year 2013-2014.

Other Matters

2013-03 Finding – No formal policies or fraud hotline on reporting suspected fraud:

During our review of policies and procedures, it was noted that there is no formal policies or fraud hotline in place for employees to report suspected fraud.

CURRENT YEAR RECOMMENDATIONS (CONTINUED)

Other Matters (Continued)

2013-03 Finding – No formal policies or fraud hotline on reporting suspected fraud (Continued):

Effect:

When there are no formal guidelines on reporting suspected fraud, employees are less likely, or not at all likely, to report suspected wrongdoings, which could result in fraud going undetected.

Recommendation:

We recommend that the City establish formal fraud reporting guidelines and inform employees about these procedures immediately.

Management's response:

The City will be researching best management practices in this area and will establish formal fraud reporting guidelines and inform employees about these procedures no later than June 30, 2014.

2013-04 Finding – Voided permits are not retained in the Building department:

During our audit, we noted that voided permits are not retained by the Building department.

Effect

When voided permits are not retained, it will create difficulties when the department needs to obtain backup to verify any records which can increase risk of misappropriation of funds.

Recommendation:

We recommend that the City retain voided permits in the Building department.

Management's response:

The City will retain voided permits in the Building department.

2013-05 Finding – Issues with fuel at the Corporation Yard:

During our visit to the Corporation Yard, we noted that one fuel tank was inoperative and there is no review of analytics of the Fleet Data System reports.

Effect

When one of the fuel tanks is inoperative, the Corporation Yard is not operating at its full capacity. Also, when there is no review of the analytical reports of fuel usage, an increased risk of misappropriation of fuel can go undetected.

Recommendation:

We recommend that the inoperative fuel tank is repaired and that the City review the fuel usage reports.

Management's response:

The inoperative fuel tank has been repaired and the City staff is reviewing the fuel usage reports on a regular basis.

STATUS OF PRIOR YEAR RECOMMENDATIONS

Significant Deficiencies

2012-01 Finding – Deficiencies in internal control over cash receipts at the Swim Center and Foss Creek:

During our review of cash receipts internal control at the Swim Center and Foss Creek, we noted the following deficiencies:

- a) Various Shift Summary Sheets were either not reconciled on a daily basis or signed by the Manager for one out of eight cash receipts reviewed.
- b) For drop-in customers, participants could simply sign in and pay the instructor. In addition, no receipts were given to drop-in participants.
- c) There was a lack of segregation of duties over cash receipts at the Swim Center and Foss Creek. The person who collects money also reconciles the cash receipts at the end of the day. In addition, no other person reviews or approves the reconciliation.
- d) The cash box at the swimming pool area was kept in an unlocked drawer and all lifeguards or part-time staff had access to the cash box during operating hours.

Effect:

A lack of segregation of duties and controls over cash receipts increases the risk that errors and irregularities may occur and go undetected, which could lead to a misappropriation of funds.

Recommendation:

We recommend that the City implement policies that will strengthen the City's internal controls at the Swim Center and Foss Creek, such as establishing a tracking system on the number of customers entering, implementing reconciliation of cash being turned in with the amount of cash receipts collected, segregating the duties of cash receipts process, and keeping cash receipts properly secured.

Status:

Implemented.

2012-02 Finding – Deficiencies in internal control over cash receipts at the Senior Center:

During our review of internal control over cash receipts at the Senior Center, we noted the following:

- a) There was a \$1 fee charged per participant for Bridge that was not on the fee schedule.
- b) One out of 6 cash receipts reviewed did not have the registration form for review.
- c) There was a lack of segregation of duties over the cash receipts at the Senior Center. The person who collects money also reconciles the cash receipts at the end of the day. In addition, no other person reviews or approves the reconciliations.

Effect:

A lack of segregation of duties and controls over cash receipts increases the risk that errors and irregularities may occur and go undetected, which could lead to a misappropriation of funds.

Recommendation:

We recommend that the City ensure that all cash receipts are properly charged based upon the approved fee schedule and booked into the correct account. The City also needs to ensure that there is a sufficient segregation of duties over cash receipts at the Senior Center.

Status:

Partially implemented. See Finding 2013-01.

STATUS OF PRIOR YEAR RECOMMENDATIONS (CONTINUED)

Significant Deficiencies (Continued)

2012-03 Finding – Non-compliance with use of impact fee:

During our review of revenues and expenditures, we noted there appears to be non-compliance with the use of impact fees. Transfers of funds are made to the General Fund with no support as to what the use is.

Effect:

The City is not in compliance with the intended purpose of impact fees.

Recommendation:

We recommend the City ensure expenditures of impact fee revenue is compliant.

Status:

Implemented.

2012-04 Finding – Lack of control over capital assets:

During the review of internal controls over capital assets, the following were noted:

1. Assets purchased with federal funds may not be identified;
2. There is no listing by department of potential impaired assets.
3. Physical inventory should be performed and reconciled with the capital asset listing annually.

Effect:

Without an annual review, the City's capital assets schedule may not be updated for obsolete, impaired, and disposed capital assets, which could result in a misstatement of the value of capital assets. Consistent use of the capitalization policies is needed to have an accurate classification of the City's capital assets.

Recommendation:

We recommend the City implement procedures to review capital assets at least annually and update the capital assets schedule, accordingly.

Status:

Not Implemented. See Finding 2013-02.

2012-05 Finding – Lack of supporting documentation:

Program: US Department of Transportation - Highway Safety Improvement Program-ARRA – CFDA 20.205

Effect:

The City is not in compliance with the retention of documents requirement under the Brooks Act and the requirements of *OMB Circular A-133 Compliance Supplement* in regards to procurement and record retention.

Recommendation:

We recommend the City retain all procurement related documents for the required time period in accordance with Federal requirements.

Status:

Implemented.

STATUS OF PRIOR YEAR RECOMMENDATIONS (CONTINUED)

Significant Deficiencies (Continued)

2012-06 Finding – Lack of documentation for sole source justification:

Program: US Department of Transportation - Highway Safety Improvement Program-ARRA – CFDA 20.205

Effect:

The City is not in compliance with the retention of documents requirement under the Brooks Act and the requirements of *OMB Circular A-133 Compliance Supplement* in regards to procurement and record retention.

Recommendation:

We recommend the City retain documentation supporting the conduct of proper procurement procedures for sole sourcing.

Status:

Implemented.

Other Matters

2012-07 Finding – Deficiency in internal control over payroll:

During our review of internal control over payroll, we noted that one out of 25 employees tested did not have a W-4 form on file.

Effect:

Without proper and sufficient payroll documentation, we cannot verify if the employees were paid correctly and it may increase the possibility of fictitious employees.

Recommendation:

We recommend the City implement procedures to ensure that all appropriate payroll documentation is obtained and retained.

Status:

Implemented.

2012-08 Finding – Deficiency in internal control over cash receipts in the Finance Department:

During our review of internal control over cash receipts in the Finance Department, we noted that two out of 10 cash receipts reviewed did not have adequate supporting documentation.

Date	Receipt	Amount
8/1/11	135746	\$149,452.79
10/31/11	135973	\$12,365.35

Effect:

Without sufficient supporting documentation, it is difficult to ascertain that all cash receipts are deposited in a timely manner and could lead to a misappropriation of funds.

Recommendation:

We recommend that the City ensure that detailed and related supporting documentation be obtained and/or retained for all cash receipts.

STATUS OF PRIOR YEAR RECOMMENDATIONS (CONTINUED)

Other Matters (Continued)

2012-08 Finding – Deficiency in internal control over cash receipts in the Finance Department (Continued):

Status:

Implemented.

2012-09 Finding – Deficiencies in internal control over cash receipts at the Community Development Center:

During our review of internal control over cash receipts at the Community Development Center, we noted three out of six cash receipts had incorrect fee charges when calculated based upon the Council approved fee schedule.

Effect:

By not correctly calculating fees, these customers may be under or over charged. In addition, a misappropriation of funds could occur.

Recommendation:

We recommend the City establish procedures over the cash receipts system in the Community Development Center and ensure that all service fees charged are calculated correctly according to the Council approved fee schedule.

Status:

Implemented.

2012-10 Finding – Deficiencies in cash receipts internal control at the Police Department:

During the review of internal control at the Police Department, we noted the following deficiencies:

- a) Cash receipts are not reconciled on a daily basis.
- b) Two out of six cash receipts reviewed did not have sufficient supporting documentation.

Date	Receipt	Amount
9/1/11	70009	\$29
2/24/12	70035	\$24

Effect:

Without restricted access to the cash drawer, a misappropriation of cash is more likely to occur. In addition, lack of supporting documentation and daily reconciliation increase the risk of misappropriation of funds that may occur and go undetected.

Recommendation:

We recommend that the City ensure that all cash drawers are locked and access limited to an employee with cash handling responsibilities only. Cash receipts need to be reconciled daily to avoid the increased risk of a misappropriation of funds. Additionally, detailed and related supporting documentation need to be obtained and/or retained for all cash receipts.

Status:

Implemented.

STATUS OF PRIOR YEAR RECOMMENDATIONS (CONTINUED)

Other Matters (Continued)

2012-11 Finding – Sick and vacation policy is inconsistent with the MOU:

During our review of City policies, we noted that the employee handbook does not agree with the MOU with regard to time for sick and vacation accrual.

Effect:

The City may not be complying with the terms of the MOU. Policies conflict with the agreement.

Recommendation:

We recommend the City ensure that the policies are consistent with the MOU and that the Council approves such changes.

Status:

Implemented.