

City of Morro Bay

Citizens Oversight Committee Agenda, Acting as Citizens Finance Advisory Committee

Mission Statement

The City of Morro Bay is dedicated to the preservation and enhancement of the quality of life. The City shall be committed to this purpose, and will provide a level of municipal service and safety consistent with, and responsive to, the needs of the public.

**REGULAR MEETING
TUESDAY, JULY 19, 2016
VETERANS MEMORIAL HALL – 3:30 PM
209 SURF ST., MORRO BAY, CA**

ESTABLISH QUORUM AND CALL TO ORDER

COMMITTEE MEMBERS ANNOUNCEMENTS & PRESENTATIONS – WELCOME NEW MEMBERS

PUBLIC COMMENT PERIOD - Members of the audience wishing to address the Committee on business matters may do so at this time.

To increase the effectiveness of the Public Comment Period, the following rules shall be followed:

- When recognized by the Chairperson, please come forward to the podium, and state your name and address for the record. Comments are to be limited to three minutes.
- All remarks shall be addressed to the Committee, as a whole, and not to any individual member thereof.
- The Committee respectfully requests that you refrain from making slanderous, profane or personal remarks against any elected official, commissioner, committee member and/or staff.
- Please refrain from public displays or outbursts such as unsolicited applause, comments or cheering.
- Any disruptive activities that substantially interfere with the ability of the Committee to carry out its meeting will not be permitted, and offenders will be requested to leave the meeting.
- Your participation in Committee meetings is welcome, and your courtesy will be appreciated.

In compliance with the Americans with Disabilities Act, if you need special assistance to participate in this meeting, please contact the City Clerk, (805) 772-6205. Notification 24 hours prior to the meeting will enable the City to make reasonable arrangements to ensure accessibility to this meeting.

A. CONSENT CALENDAR

1. APPROVAL OF MINUTES FOR THE JUNE 21, 2016, REGULAR CITIZENS OVERSIGHT/FINANCE ADVISORY COMMITTEE MEETING

B. BUSINESS ITEMS

1. CONTINUED DISCUSSION ON BENCHMARKING MORRO BAY'S BUDGET TO SIMILAR CITIES
2. PRESENTATION ON ACTIONS TAKEN-TO-DATE TO CORRECT FY 2014/15 AUDIT FINDINGS
3. UPDATE ON FIRE STATION CERTIFICATES OF PARTICIPATION
4. PROGRESS UPDATE: PUBLIC-FRIENDLY BUDGET
5. FUTURE AGENDA ITEMS

C. SCHEDULE NEXT MEETING

The regular meeting, scheduled for August 23rd, is cancelled. The Committee will hold a workshop on August 30, 2016, and the next regular meeting will be September 20, 2016.

D. ADJOURNMENT

THIS AGENDA IS SUBJECT TO AMENDMENT UP TO 72 HOURS PRIOR TO THE DATE AND TIME SET FOR THE MEETING. PLEASE REFER TO THE AGENDA POSTED AT CITY HALL FOR ANY REVISIONS, OR CALL CITY HALL AT 772-6201 FOR FURTHER INFORMATION.

MATERIALS RELATED TO AN ITEM ON THIS AGENDA SUBMITTED TO THE COMMITTEE AFTER DISTRIBUTION OF THE AGENDA PACKET ARE AVAILABLE FOR PUBLIC INSPECTION AT CITY HALL LOCATED AT 595 HARBOR STREET DURING NORMAL BUSINESS HOURS.

IN COMPLIANCE WITH THE AMERICANS WITH DISABILITIES ACT, IF YOU NEED SPECIAL ASSISTANCE TO PARTICIPATE IN A CITY MEETING, PLEASE CONTACT THE CITY CLERK'S OFFICE AT LEAST 24 HOURS PRIOR TO THE MEETING TO INSURE THAT REASONABLE ARRANGEMENTS CAN BE MADE TO PROVIDE ACCESSIBILITY TO THE MEETING.

MINUTES - CITIZENS OVERSIGHT/FINANCE ADVISORY COMMITTEE
REGULAR MEETING – JUNE 21, 2016
VETERANS MEMORIAL HALL – 3:30 P.M.

MEMBERS PRESENT:	Barbara Spagnola	Chairperson
	Marlys McPherson	Vice-Chairperson
	David Betonte	Member
	Betty Forsythe	Member
ABSENT:	Roscoe Mathieu	Member
STAFF PRESENT:	Susan Slayton	Administrative Services Director
	Brooke Austin	Deputy City Clerk

ESTABLISH QUORUM AND CALL TO ORDER

A quorum was established with all members, but Member Mathieu, present, and the meeting was called to order at 3:33 p.m.

COMMITTEE MEMBERS ANNOUNCEMENTS AND PRESENTATIONS

Chairperson Spagnola announced the recruitment for additional committee members has been extended and the new deadline is June 24th.

PUBLIC COMMENT PERIOD

The public comment period was opened. Seeing none, the public comment period was closed.

A. CONSENT CALENDAR

A-1 APPROVAL OF MINUTES FOR THE MAY 17, 2016 REGULAR CITIZENS OVERSIGHT/FINANCE ADVISORY COMMITTEE MEETING
<https://youtu.be/xSxsK1Wa0So?t=2m26s>

MOTION: Committee Member McPherson moved to approve the minutes from the May 17, 2016 meeting. The motion was seconded by Member Forsythe and carried unanimously, 4-0.

B. BUSINESS ITEMS

B-1 DISCUSSION OF FY 16/17 BUDGET
<https://youtu.be/xSxsK1Wa0So?t=3m48s>

Committee Members reviewed the Summary of All Budgeted Funds and inquired of Administrative Services Director Slayton to clarify Capital Replacement, Lower Cost Visitor Accommodations Mitigation, Parking In-Lieu, Utility Discount/Rebate, Accumulation Funds, General Fund Emergency Reserve, Revenue Estimates, Revenues Over(Under) Net Transfers and Expenditures. They reviewed All Funds Revenue by Category, which is a summary of the previous information just sorted differently; All Funds Expenditures by Category; General Fund Revenue by Source; General Fund Expenditures by Division and Category. The Board stated this is a good source for the Public-Friendly Budget Document and recommend receiving this summary prior to budget adoption in future years.

B-2 PROGRESS UPDATE: PUBLIC-FRIENDLY BUDGET

<https://youtu.be/xSxsK1Wa0So?t=29m3s>

Committee Member Betonte, who is also a member of the subcommittee for Public-friendly Budget Documents, stated that there are basically three categories of documents – Budget at a Glance, a two-sided utility mailer; Budget in Brief, a few more pages, that could be added to website for those that want additional information; and the actual Budget, some of which incorporate the other two documents. He questioned what the focus of the subcommittee should be, documents or recommendations. Administrative Services Slayton stated that the City would like a Budget at a Glance and/or Budget in Brief document and recommendations of improvements for future budgets. She will provide the subcommittee with excel documents of budget information to use in creating documents.

The Board discussed needing different summaries for different audiences and including funding by goals and accomplishments, as well as, including a glossary or frequently asked question section. They understand staffing limitations, but would like to start making improvements and build on them each year. The Committee discussed pushing the Public-Friendly Budget Document Workshop to August to allow time to prepare sample documents for review and perform more public outreach.

B-3 BENCHMARKING MORRO BAY'S BUDGET WITH SIMILAR CITIES

<https://youtu.be/YPV44xMs27k?t=21m51s>

The Board discussed benchmarking and what the Council wants to get out of it. Committee Liaison John Heading stated that it was the intent of the Council to benchmark with other cities that might be similar, like the cities Management Partners used previously, to determine areas we might be spending more on than comparable cities. Council would like a higher level review of expenditures, identifying statistically significant differences and the reasons for such, and looking for ways to reduce expenditures.

Committee Member Betonte shared the Pioneer Institute Webpage on benchmarking which is an excellent resource for important metrics.

C. DECLARATION OF FUTURE AGENDA ITEMS

<https://youtu.be/YPV44xMs27k?t=43m56s>

The Committee would like to have future agenda items to review benchmarking, preparing for the public-friendly budget workshop, and an update of remediation steps taken to date in response to the 2014/2015 audit findings.

D. ADJOURNMENT

The meeting adjourned at 4:59 pm. The next Regular Meeting will be held Tuesday, July 19, 2016 at 3:30 p.m. at the Veterans Memorial Hall located at 209 Surf Street, Morro Bay, CA. It is anticipated the Public-Friendly Budget Workshop will be held in August.

Recorded by:

Brooke Austin
Deputy City Clerk



AGENDA NO:	B - 1
MEETING DATE:	July 19, 2016

Staff Report

TO: Chairwoman Spagnola and Committee Members **DATE:** July 12, 2016
FROM: Susan Slayton, Administrative Services Director
SUBJECT: Continued Discussion on Benchmarking Morro Bay's Budget to Similar Cities

The Committee will continue discussing this project with the goal of having a work product to present to the City Council at the October 25, 2016, regular meeting.



AGENDA NO:	B - 2
MEETING DATE:	July 19, 2016

Staff Report

TO: Chairwoman Spagnola and Committee Members **DATE:** July 8, 2016
FROM: Susan Slayton, Administrative Services Director
SUBJECT: Presentation on Actions Taken-to-Date to Correct FY 2014/15 Audit Findings

The City's audit firm, the Pun Group, performed its auditing services for the fiscal year ended June 30, 2015, and issued its reports, which contained audit findings (material weaknesses/significant deficiencies), presented as Finding 2015-001 (Issues 1–8), which were categorized as material weaknesses. A material weakness is a lack, or combination of inadequacies, 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.

Many of the findings were already corrected in 2015/16, but the response had to take into consideration only the situation as it stood in 2014/15. Please remember the audit was not finalized until **March 31, 2016**, so we are talking about awareness and actions taken within a three-month period.

The auditors agreed that a language barrier may have played a part in some misunderstandings about our processes. The individual, who interviewed staff, chose a newer member of our staff to question about processes; this person later told her supervisor she was very nervous when questioned, and in many cases, did not understand the questions asked by the interviewer, due to a language barrier, so she said "I don't know" as her answer to process questions. Additionally, staff pointed out a flaw in the random selection of personnel records, as it targeted part-time staff only.

Finding 2015-001, 1:

This finding was related to the lack of formal policies and procedures (e.g., a physical book entitled Policies and Procedures), and the lack of understanding and following of the Municipal Code.

Management's comment was while a comprehensive document of all policies is not in place, there are multiple policies and procedures in existence and practice. Desk manuals/job duties/procedure checklists do exist. Management has stated the comprehensive book of policies and procedures will be completed in 2016/17.

PROGRESS-TO-DATE: the manual has been established, and as time permits, documents are being collected and added.

Finding 2015-001, 2 & 7:

This finding was related to segregation of duties over disbursements, payroll and cash receipts processes.

Management's comments refuted this finding for disbursements and cash receipts processes, as we work very hard to involve as many people in both processes. However, we did not have a management staff member **SIGNING** off on reports or checklists. With payroll, we also did not have someone **SIGNING** off on reports or checklists, but did have reviews in place. This process was mostly completed by one person, but reviews did occur; the process has significantly changed.

PROGRESS-TO-DATE: during the 2014/15 audit period, we implemented electronic timesheets, removing the second-party manual time sheet entry activity. Electronic timesheets were fully implemented in 2015/16, with all employees entering hours worked through a secure portal, password protected. Payroll retrieves the electronic information, and reviews it for accuracy. If any errors are discovered, payroll has the ability to reject the time sheet for correction, or make corrections to the time sheet, if the error is not discovered in a timely manner (late submission by employee). If payroll makes a change, the employee is notified, **by the payroll system**, with an email, indicating a change was made to the employee's time entry.

Beginning in April, the payroll process register is signed by the Administrative Services Director, **prior to payroll distribution and payment**. The payroll process checklist is reviewed and signed off by the individual assigned as the payroll backup. We have always had the payroll back or the Administrative Services Director separate and prepare the payroll checks and direct deposit advices for pickup by the departments, who sign a form when departmental payroll is picked up.

Previous reviews for both payroll and accounts payable occurred by notifying the Administrative Services Director, both in written format (payroll) and e-mail, of the amount of distribution. This information has been recorded in an Excel spreadsheet for many years by the Administrative Services Director, and this process continues.

Also beginning in April, we have the accounts payable backup signing off on the accounts payable process register, after she reviews it for accuracy. The accounts payable process checklist is also signed off by the backup individual. Cash receipts have always been signed off and carefully separated as best as possible with a small staff.

Finding 2015-001, 3:

This finding was related to reconciling standalone processes, such as the HdL building permits, Active recreation registration, and HdL business tax certificate software products.

PROGRESS-TO-DATE: we have always received reports directly from these standalone systems, but do not have the ability to **transfer** information from the standalone system to the City's main financial software product. This was the crux of the finding.

We are in the process of implementing a new product, CityWorks, which will have transfer protocol for

both building permits and business tax certificate processes.

Regarding Active recreation registration and payment software, there is an issue with this product. Old deposits continue to be reported as unreconciled, and with the significant change in personnel in Recreation, there is a significant challenge with exploring and correcting this problem. Management is well-aware of the issue, and is working on resolution.

Finding 2015-001, 4:

This finding was related to our lack of a purchase order system.

PROGRESS TO DATE: the City has purchased a purchase order module, installed it, and has a procedure manual under review by the City Attorney. This was all accomplished prior to the issuance of the audit findings, but not during the 2014/15 audit period. We will have the purchase order system up and running the 2016/17 fiscal year.

Finding 2015-001, 5:

This finding was related to cash disbursements not being signed off by authorized personnel.

PROGRESS TO DATE: we have a procedure in place, whereby Department Directors have submitted samples of their signatures for comparison to invoice authorization, and have authorized certain management/supervisory personnel to sign invoices, in the Director's absence. If the proper signatures are missing, invoices are returned to the originating department to be properly signed off. This process was implemented in April/May 2016. The accounts payable clerk has copies of the form signed by authorized signers, as well as the designated person, as does the Administrative Services Director. This helps the clerk identify the signature of the person signing to ensure they are authorized.

Finding 2015-001, 6:

This finding was related to Personnel Action Forms not adequately approved and retained by the City, and staff receiving approvals /charges that were informal or verbal.

PROGRESS TO DATE: management was unclear about this finding and challenged the auditor, who revisited our processes by requesting a new selection of employees' personnel files to review. With the new selection, there were no errors discovered. The first selection contained mainly part-time employees, who were in the process of being converted from contracts to Personnel Action Forms (PAF) in recording their hiring information and pay information. Staff is continuing its diligence in obtaining all personnel changes on PAFs or in written format. Staff did not, and does not, take verbal changes for personnel actions.

Finding 2015-001, 8:

This finding was related to expenditures exceeding budgets, without amendments.

PROGRESS TO DATE: staff reviewed the 2015/16 3rd quarter budgets and took additional amendment requests to Council. This practice will continue to ensure compliance with spending and budgets.

Regarding Findings 2015-002, 003 and 004, these are activities that will occur with the fiscal year end process for 2015/16 (September 2016).

City of Morro Bay
Schedule of Findings and Questioned Costs (Continued)
For the Year Ended June 30, 2015

Section II – Financial Statement Findings

Finding 2015-001 Accounting Policies and Procedures

Criteria:

Accounting Policies and Procedures would aid the Finance Department and the City in providing training for accounting personnel, communicating and providing a source of reference to approved policies, and maintaining consistency of recording financial transactions.

Segregation of duties is a key internal control intended to minimize the occurrence of errors or fraud by ensuring that no employee has the ability to both perpetrate and conceal errors or fraud in the normal course of their duties. In event segregation of duties is not feasible, it is important to have mitigating controls to prevent errors and misstatements.

Effective internal control over cash receipts requires proper segregation of duties. The individual collecting the cash and depositing the funds should be someone different than the individual responsible for entering that data into the system. Two individuals should be present when receiving and counting. Each should count the funds individually to ensure accuracy. The counts should be logged on one sheet which is signed by both employees. The individual collecting the funds should not have update access to the system or customer set up.

Effective internal control over purchasing process provides reasonable assurance that the expenses are properly reported. Management or governing body approval of purchase orders is required for purchases that exceed established limits according to City's policy.

Effective internal control over the personnel information and payroll process provides reasonable assurance of the completeness and accuracy of accounting records.

Budgetary or appropriation accounting consists of tracking and maintaining operations concerning appropriations and their uses. It should cover appropriations, apportionment, any increase or decrease in appropriations, commitments/obligations, and expenditures.

Condition:

1. During our review of control environment, we noted that the City did not have a comprehensive policies and procedures for the Finance Department. The Municipal Codes were used as guidance instead.
2. During our observation of internal control, we noted that insufficient segregation of duties existed over disbursements, payroll, and cash receipts processes due to short staff. However, there was no evidence of mitigating controls in place over the final review of these transactions classes.
3. During our observation of internal control over cash receipts, we noted that other sub- ledger programs are not interfaced with the main general ledger system (FSM-Harbor, HDL-business license/public services, Active Network-Parks and Recreation) and the reconciliations procedures are not performed periodically.
4. During our internal control testing of the procurement process, we noted that the City does not require approved purchase orders.
5. During our observation of internal control over cash disbursements, we note that 7 out of 25 transactions we tested did not have approving signatures by department head.

City of Morro Bay
Schedule of Findings and Questioned Costs (Continued)
For the Year Ended June 30, 2015

Section II – Financial Statement Findings (Continued)

Finding 2015-001 Accounting Policies and Procedures (Continued)

Condition (Continued):

6. During our observation of internal control over payroll and human resources, we noted that personnel action forms (PAF) for part-time employees are not adequately approved and retained by the City.
7. During our observation of internal control over payroll, we noted that timesheet hours are entered manually into the payroll system by a city staff prior to conversion to New World in May 2015. However, no one reviewed or approved input or compared input to the approved timesheets. Furthermore, there was lack of segregation of duties in payroll cycle. One staff enters hours, processes payroll, and there was no approval or second review.
8. During our audit, we noted that there were number of excess spending over appropriations.

Cause:

The City has small staff and segregation of duties was not possible and formal policies and procedures were not adopted. The City is in a process of implementing systems and audit was performed during the period of conversion.

Effect:

Without the Accounting Manual, personnel responsible for the daily work and transactions do not have a clear understanding of their role and responsibilities or the accounting standards applicable to their function. In addition, the absence of standardized procedures has created inefficient and inconsistent processing of transactions. Absent clear guidance, delays in financial reporting occur as staffs are unaware of where to find the answers.

Lack of segregation of duties will increase the risk of both erroneous and inappropriate actions. When segregation of duties is not possible, a detailed supervisory review of related activities is needed as a compensating control activity.

There were number of excess spending over appropriations.

Recommendation:

We recommend that the City develop a comprehensive Accounting Manual that would set the guidelines for recording significant transactions in the general ledger. In addition, Management should consider developing an Accounting Manual which includes at a minimum:

- Specific duties and responsibilities (desk procedures)
- Minimum required qualifications or standards
- Council/Management approved policies relating to specific transactions
- Procedures for processing of specific financial activities
- Appropriate monitoring and review controls

City of Morro Bay
Schedule of Findings and Questioned Costs (Continued)
For the Year Ended June 30, 2015

Section II – Financial Statement Findings (Continued)

Finding 2015-001 Accounting Policies and Procedures (Continued)

Recommendation (Continued):

We also recommend that following functions be segregated:

- Initiate, authorize or approve transactions
- Executing the transactions
- Recording the transactions
- Reconcile the transactions

When segregation of duties is not possible, the City should establish compensating controls. The City can implement compensating controls by adding additional reviews and approvals of another person, and/or require reconciliation between systems or reports to ensure that all transactions are properly processed, recorded, and reconciled to the general ledger system. Furthermore, the City should enforce consistent treatment over all processes in accordance to the adopted policies and procedures, require documentation and retain documents necessary, require approval and review signatures, and further investigate when exceptions occur.

Management View and Corrective Action Plan:

1. Lack of adopted policies and procedures; employees not aware of Municipal Code and not following it.

In 2015, the City had an organizational assessment by Management Partners, and one of the recommendations was to adopt a set of Financial Policies and Procedures.

Corrective action for adopted financial policies and procedures: management will have draft Financial Policies and Procedures in place in the 2016/17 fiscal year.

Regarding the auditor's finding on the employees' lack of awareness of the Municipal Code, and not following the Code sections, Management offers the following comments:

Title 13 of the Municipal Code has strict guidance on public utilities. The Utility Billing clerk has a copy of the Code, and management has found utility staff members are aware of the location of the Municipal Code, both online on our website and in printed form in the front office, and fully understands that any deviation from the Code requires management approval.

Regarding the lack of policies and procedures, Management offers the following comments:

There are desk manuals/instructions for Utility Billing, Payroll, Accounts Payable, and Miscellaneous Revenue Receipting. These manuals/instructions have been updated as recently as 2016, and are living documents (continually updated). As new staff members are hired, the supervisor requires them to use the manuals/instructions, and note any sections or tasks that are unclear, or any procedures which should be updated for software changes. Manuals/instructions are subsequently reviewed and updated, if needed.

City of Morro Bay
Schedule of Findings and Questioned Costs (Continued)
For the Year Ended June 30, 2015

Section II – Financial Statement Findings (Continued)

Finding 2015-001 Accounting Policies and Procedures (Continued)

Management View and Corrective Action Plan (Continued):

2. Segregation of duties over disbursements, payroll and cash receipts processes.

As stated in the Management Partners assessment, the Administrative Services Division (Finance, Human Resources, Utility Billing and Customer Service, Accounting) is understaffed. We have a staff of five full-time employees in Administrative Services division, which includes the Administrative Services Director plus one clerk in utility billing, one clerk for business tax certificates and revenue processing (Transient Occupancy Tax), one technician for payroll, capital projects reconciliation, grants and journal entries, and one analyst in Human Resources, who assists in many of our functions to aid in segregation of duties. We have two half-time clerks assisting in Utility Billing and Customer Service, while our full-time person begins her return from protected leave. Additionally, we have one part-time clerk for accounts payable and revenue processing (sales tax, property taxes, etc.).

Prior to May 2015, employees submitted paper timesheets, prepared by the employees and signed by their supervisor and department directors. The Technician processed the payroll from beginning to end, with the Human Resources Analyst reviewing the printed checks. In May 2015, staff initiated electronic timesheet entry into the payroll system by each employee. Departmental supervisors approve the timesheets, and transmit them to the Technician. Once all timesheets are approved, the Technician processes them for payment. The payroll process is generally contained to the Technician, once timesheets are received. Payroll checks and direct deposit notices are reviewed and prepared for distribution by our Human Resources Analyst.

Corrective action for the payroll process: management will immediately require the Administrative Services Director to review and authorize the payroll register, prior to the final printing of checks/deposit advices.

For our process with cashiering, daily cash balancing and depositing, management believes duties are sufficiently segregated to avoid fraud, and offers the following comments:

The Utility Billing clerk is the primary person responsible for taking and entering customer payments, either checks from the mail or cash from walk-in customers. When she leaves for lunch or breaks, a temporary employee assists with customer service. However, there are occasions when other staff (Business Tax clerk or Accounts Payable clerk) are required to provide customer service and take payments; we do our best to mitigate the need for Accounts Payable clerk's involvement with the cash acceptance/receipting process, since that individual reconciles and balances daily cash, but with such a small staff, it is not always possible.

When cash is received, there are generally two clerks present at the counter.

The following morning, the Accounts Payable clerk pulls out the previous day's cash drawer, reconciles the previous day's cash and checks to reports of recorded transactions, reconciles, and prepares deposit slips for the bank. Any cash discrepancies are recorded in the General Ledger account Cash Variations. The Technician posts the deposit, and takes the deposit to the bank. The backups for balancing the daily cash and/or taking the deposit to the bank are the Human Resources Analyst and the Administrative Services Director.

City of Morro Bay
Schedule of Findings and Questioned Costs (Continued)
For the Year Ended June 30, 2015

Section II – Financial Statement Findings (Continued)

Finding 2015-001 Accounting Policies and Procedures (Continued)

Management View and Corrective Action Plan (Continued):

Regarding the Cash Variations General Ledger account, below is a historic fiscal yearend balance of our cash variations revenue object:

2011	\$-35.63
2012	\$0.29
2013	\$-49.28 *
2014	\$-101.41 *
2015	\$-63.01
2016 YTD	\$1

The * indicates a time period with an employee, who is no longer here

Reconciliations are performed daily, and cash variations are noted on the day they occur. Staff researches for obvious errors, such \$26, which is the water service application fee. If no answer can be found, the cashier(s) are admonished to take more care, and the over/short is recorded in cash variations. If cash is out of balance frequently, we require a second count of the cash taken as it comes in. We did have a problem with a part-time employee, and addressed it, ultimately separating the employee from City service.

The City collects approximately \$350,000 in cash annually. These variations do not even amount to 0.05% of that estimate.

For our accounts payable cash disbursement process, management believes duties are sufficiently segregated to avoid fraud, and offers the following comments:

All departments prepare their own invoice batches for payment, with the exception of City Hall; the Accounts Payable Clerk prepares batches for City Hall departments. All departments are responsible for collecting proper signatures for all disbursement requests/invoices. The invoice batches are collected by the Accounts Payable Clerk, reviewed for signatures, added up, and processed to a payment register. This payment register is reviewed and noted for correction by the Technician. The payment register is returned to the Accounts Payable clerk to make the necessary corrections (if any), accept the payment register and process checks. The Accounts Payable clerk prints the checks, and hands all of the printed checks plus the supporting documents to our Utility Billing clerk, who reviews them and match the copy of the check to the invoices processed, places the checks and stubs in envelopes, and places all envelopes in the mail room for stamping and mailing. Stamping is performed by the Human Resources Analyst, City Clerk or the Business Tax clerk. The backups to the reviewing/matching function are the Human Resources Analyst and the Administrative Services Director.

City of Morro Bay
Schedule of Findings and Questioned Costs (Continued)
For the Year Ended June 30, 2015

Section II – Financial Statement Findings (Continued)

Finding 2015-001 Accounting Policies and Procedures (Continued)

Management View and Corrective Action Plan (Continued):

3. Reconciliation procedures for standalone software systems

The current business tax and permitting system (HdL software) is a standalone system that does not have a transfer protocol to record directly to the City's financial system.

Corrective action: the City has purchased CityWorks, a product which will have a transfer protocol. This product will be used for permits and business tax, and is anticipated to be live in the 2016/17 fiscal year.

The Recreation Department uses a standalone system (Active Network) for receipting recreation program revenues. This system does not have a transfer protocol to record directly to the City's financial system.

Corrective action: management is reviewing other software to more effectively and accurately track recreation revenues, and transfer information directly to the City's financial system.

Management offers the following comments regarding the Harbor Department's system and deposit:

The Harbor Department uses a standalone system (FSM) for billing and receipting Harbor leases and slip rentals. This system does not have a transfer protocol to record directly to the City's financial system. However on a monthly basis, staff records the billings from Harbor activity, based on reports printed from the FSM software program. The receipts from the Harbor Department are compared to the cash receipts that are processed during the month.

The Harbor Department is exploring other software, which will have the appropriate transfer protocol.

4. Procurement process – no Purchase Order System.

The City has a purchasing policy in the Municipal Code, Section 3.08, which sets strict guidelines and limits on purchasing of supplies and equipment. Management requires informal bids for contracts for all services of \$1,000 or more, and formal bids/requests for proposals for costs greater than \$35,000. Purchases over \$1,000 require City contracts. Management believes we have been diligent in our efforts, but does feel a formal purchase order system will improve this process, and took formal action to require this, as indicated below:

Ordinance 594 was enacted on 8/25/15 (effective 9/25/15), which directed Management to implement a purchase order system. Anticipating this directive, management purchased, in July 2015, a purchase order module from its financial software provider, New World Systems. Staff participated in training on the module, and is in the process of preparing purchasing guidelines; once approved, staff will begin training departmental staff members on the use of purchase orders.

Corrective action has been taken, and management will launch the purchase order system during the 2016/17 fiscal year.

City of Morro Bay
Schedule of Findings and Questioned Costs (Continued)
For the Year Ended June 30, 2015

Section II – Financial Statement Findings (Continued)

Finding 2015-001 Accounting Policies and Procedures (Continued)

Management View and Corrective Action Plan (Continued):

5. Cash Disbursements not signed by Department Directors

Departmental staff is responsible for ensuring proper signatures have been obtained for disbursements; however, as the final checkpoint, current staff will be counseled to be more diligent in reviewing invoices and requests for disbursement, to ensure the applicable Department Director has signed them all.

6. Personnel Action Forms for part-time employees are not adequately approved and retained by the City; approvals /charges are informal or verbal.

Personnel Action forms (PAFs) were required for part-time employees during the audit period, however not all part-time employees had been converted from contracts to PAFs. PAFs are not required for mass changes, such as COLA's; staff implements those changes via MOU, or for part-time employees, from a list of changed hourly rates by position received from the department supervisor. All PAFs are retained in Human Resources, and placed in employees' permanent personnel files. All PAFs are signed by the employee, when possible; the exception to this is during separation, when an employee may refuse or not be available to sign. All PAFs are signed by the Supervisor and/or Department Director, and Administrative Services Director, however, the Acting City Manager did not wish to sign all PAFs, only those with promotions. With the hiring of new City Manager, this process has changed, and in October 2015, he began signing all PAFs. Copies of all PAFs are provided to payroll. Beginning January 2015, the payroll clerk initials the original PAF, returns it to Human Resources, and is provided with a copy of that initialed PAF.

7. Manual timesheet entry/segregation of duties

As mentioned above, the City has a very small staff dedicated to finance and accounting, and segregation of duties is difficult. As mentioned under #2 above, timesheets are entered into the system by each employee, not the Technician, beginning in May 2015 with a test group, with full implementation in August 2015.

Regarding a review of payroll checks and direct deposit notices, the Human Resources Analyst, who is also the backup for payroll processing, does review the checks and direct deposit advices for anomalies when preparing them for departmental distribution. Corrective action for the payroll process implementation of electronic timesheets resolved some of the segregation of duties issue. Management will immediately require the Administrative Services Director to review and authorize the payroll register, prior to the final printing of checks/deposit advices. Additionally, the Human Resources Analyst, who is the backup to the payroll process, will initial the payroll checklist.

Additionally, the Technician will require written (not verbal) authorization, prior to inputting or correcting a timesheet manually.

8. Excess spending over appropriations

Regarding excess spending over approved budget, management will be more diligent with requesting budget adjustments to ensure this does not happen in future years.

City of Morro Bay
Schedule of Findings and Questioned Costs (Continued)
For the Year Ended June 30, 2015

Section II – Financial Statement Findings (Continued)

Finding 2015-002 Maximum Funding Allowance

Criteria:

Section 6634 (a) of the California Code of Regulation, Title 21, Division 3, Chapter 2, Article 4, “*No operator or Transit Service Claimant shall be eligible to receive moneys during the fiscal year from the local transportation fund and the state transit assistance fund for operating costs in an amount that exceeds its actual operating cost (including payments for disposition of claims arising out of the operator's liability) in the fiscal year less the sum of the actual amount of fare revenues received during the fiscal year.*”

Condition:

Amount claimed and received from the Local Transportation Fund and the State Transit Assistance Fund for operating cost exceeded its actual operating cost (including payments for disposition of claims arising out of the operator's liability) in the fiscal year less the sum of the actual amount of fare revenues received during the fiscal year. The management discovered the error and corrected the reporting of Local Transportation Fund in excess of net operating costs are unearned revenues during the year ended June 30, 2015.

Cause:

Communication process was not sufficient to provide management and staff adequate knowledge on Transportation Development Act regulations and compliance requirements.

Effect:

The City is not in compliance with maximum funding allowance pursuant to *Section 6634 (a) of California Code of Regulation, Title 21, Division 3, Chapter 2, Article 4.*

Recommendation:

We recommend that the City implement procedures to ensure that funds received from the Local Transportation Fund and the State Transit Assistance Fund for operating cost does not exceeded its actual operating cost (including payments for disposition of claims arising out of the operator's liability) in the fiscal year less the sum of the actual amount of fare revenues received during the fiscal year.

Management's Response:

Management agrees with the finding as noted, and beginning with the 2015/16 fiscal year, will ensure compliance with TDA Section 6634(a) by adding a required reconciliation of the Transit fund to the year-end checklist.

City of Morro Bay
Schedule of Findings and Questioned Costs (Continued)
For the Year Ended June 30, 2015

Section II – Financial Statement Findings (Continued)

Finding 2015-003 Bond Coverage Ratio

Criteria:

Section 12 (a) of the Water Treatment and Local Facilities Agreement with the San Luis Obispo County Flood Control and Water Conservation District (the “Agreement”) states, *“The contractor will fix, prescribe and collect rates and charges for the Contractor Water System which will be at least sufficient to yield during each fiscal Year Contractor net Water System Revenues equal to one hundred twenty-five percent (125%) of the contract payments for such Fiscal Year.”*

Condition:

During our audit, we noted that the City did not meet its minimum bond coverage ratio of greater than, or equal to 1.25 as required under Section 20(a) of the Agreement by imposing rates and charges sufficient to collect 125% of the contract payment.

Cause:

The City has not changed its water rates since fiscal year 1995-1996.

Effect:

No sufficient revenue to cover equal to one hundred twenty-five percent (125%) of the contract payments.

Recommendation:

We recommend that the City implement procedures to ensure that the minimum bond coverage ratio is met.

Management’s Response:

The City participates in the State Water Project via an agreement with the County of San Luis Obispo Flood Control and Water Conservation District. A requirement of that agreement is the City will set its rates to collect sufficient funds from its users, so that it annually nets (operating revenues minus operating expenditures) a retention amount of 125% of the contract payments. In fiscal years 2011 through 2015, the City’s debt service coverage (computed in accordance with the Local Water Treatment Agreement) was below 125% of the contract payments. The City did make, and always has made, its required contract payments on time; however, it failed to raise its rates (last raised in 1996) to sufficient levels to meet the 125% requirement.

Corrective Action Plan: on March 27, 2014, the City issued a Request for Proposals for Consulting Services, Water and Sewer Rate Study Services, and on May 23rd, selected Bartle Wells, as the contractor to perform these studies. The City established the following proposed schedule to present, discuss and implement the new rates:

1. Public Works Advisory Board preliminary workshop, January 29, 2015
2. City Council Rate Study Session, February 24, 2015
3. City Council meeting to further discuss and potentially adopt the rate schedule(s), March 24, 2015
4. City Council Prop 218 Public Hearing, May 26, 2015
5. New rates implementation date: July 1, 2015

City of Morro Bay
Schedule of Findings and Questioned Costs (Continued)
For the Year Ended June 30, 2015

Section II – Financial Statement Findings (Continued)

Finding 2015-003 Bond Coverage Ratio (Continued)

Corrective Action Plan (Continued)

On May 26, 2015, the City Council the City of Morro Bay adopted a new rate schedule that was implemented with the July 2015 meter reads (September 1, 2015 billing date). Our consultant, Bartle Wells, has estimated the 2015/16 coverage ratio to be 126%.

Our two biggest issues have been the drought, with the need to use our desalinization facility to create clean water, and water conservation, due to the drought. Our new rate structure factors in both those issues plus created new rates to be implemented in times of severe drought and the excessive use of the desalinization facility.

City of Morro Bay
Schedule of Findings and Questioned Costs (Continued)
For the Year Ended June 30, 2015

Section II – Financial Statement Findings (Continued)

Finding 2015-004 Prior Period Adjustments

Criteria:

Management is responsible for the selection and use of appropriate accounting policies.

GASB Statement No. 68, *Accounting and Financial Reporting for Pension – an amendment of GASB Statement No. 27* requires to report payable to a defined pension plan including short-term payables for legally or contractually required contributions outstanding as of the end of the reporting period, as well as long-term payables, such as those arising from amounts assessed to an individual employer upon joining a multiple-employer pension plan. In financial statements prepared using the economic resources measurement focus and accrual basis of accounting, a payable to a defined benefit pension plan should be recognized separately from liabilities for a net pension liability, if any.

GASB Statement No. 27, *Accounting for Pension by State and Local Government Employers* states, “The employer’s Net Pension Obligation comprises (a) the pension liability (asset) at transition, if any, determined in accordance with paragraph 30-35, and (b) the communicative difference since the effective date of this Statement between annual pension cost and employer’s contribution, excluding (1) short-term differences, and (2) unpaid contributions that have been converted to pension-related debt.”

GASB Statement No. 27, *Accounting for Pension by State and Local Government Employers* also states, “The pension liability at transition of a cost-sharing employer should be equal to the employer’s (a) contractually contributions that are due and payable at the effective date and (b) pension-related debt, if applicable.”

GASB Statement No. 45, *Accounting and Financial Reporting by Employer for Postemployment Benefits Other Than Pension (“OPEB”)* requires employers that participate in single-employer or agent multiple-employer defined benefit OPEB plans (sole and agent employers) are required to measure and disclose an amount for annual OPEB cost on the accrual basis of accounting. Annual OPEB cost is equal o the employer’s annual required contribution to the plan (ARC), with certain adjustments if the employer has a net OPEB obligation for past under- or over-contributions.

GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities* improves financial reporting by clarifying the appropriate use of the financial statement elements deferred outflows of resources and deferred inflows of resources to ensure consistency in financial reporting.

Condition:

During our audit, we noted that the City’s financial statement required number of prior period adjustments.

Cause:

The City was not aware of these requirements for reporting.

City of Morro Bay
Schedule of Findings and Questioned Costs (Continued)
For the Year Ended June 30, 2015

Section II – Financial Statement Findings (Continued)

Finding 2015-004 Prior Period Adjustments (Continued)

Effect:

Pension related debt was understated by \$1,508,441 and other postemployment benefits liability was understated by \$109,837 for the Governmental Activities. Furthermore, unavailable revenues were overstated by \$881,389 for the Community Development Grant Special Revenue Fund.

Recommendation:

We recommend that the City implement procedures to establish a detailed review process to ensure that the financial statements are free of material misstatements and comply with current reporting requirements.

Management's Response:

Management believed it was properly recording its assets and liabilities, and appreciates the auditors finding and correcting previous misstatements.

Corrective Action Plan: management and the auditor will work closely together, prior to the audit's beginning to ensure compliance.



AGENDA NO:	B - 3
MEETING DATE:	July 19, 2016

Staff Report

TO: Chairwoman Spagnola and Committee Members **DATE:** July 8, 2016

FROM: Sub-Committee Members Betonte and Mathieu

SUBJECT: Progress Update: Public-Friendly Budget

This is the Sub-Committee's opportunity to present its efforts made on researching/creating a more Public-Friendly Budget document and presentation. The Committee will routinely discuss this topic for a recommendation to the City Manager by January 2017.

Additionally, the Committee should discuss topics/plans to prepare for the August 30th workshop.