

CITY OF LEMOORE

REPORT TO MANAGEMENT

**FOR THE YEAR ENDED
JUNE 30, 2019**

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INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

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

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Lemoore, California (the City), as of and for the year ended June 30, 2019, and the related notes to the financial statements, which collectively comprise the City's basic financial statements and have issued our report thereon dated April 16, 2020.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the City's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control. Accordingly, we do not express an opinion on the effectiveness of the City's internal control.

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

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that have not been identified. During our audit we did identify deficiencies in internal control, described in the accompanying schedule of findings and responses that we consider to be material weaknesses: 2019-001, 2019-002 and 2019-003. We also identified a deficiency in internal control, described in the accompanying schedule of findings and responses that we consider to be significant deficiency: 2019-004.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

City's Response to Findings

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

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

HUDSON HENDERSON & COMPANY, INC.

A handwritten signature in blue ink that reads "Hudson Henderson & Company, Inc." in a cursive script.

Fresno, California
April 16, 2020

CITY OF LEMOORE
SCHEDULE OF FINDINGS AND RESPONSES
FOR THE YEAR ENDED JUNE 30, 2019

Finding 2019-001 – Material Weakness
Financial Closing & Reporting

Condition:

During the audit of the City’s financial statements, we identified material misstatements in the City’s general ledger account balances which required material audit adjustments. Additionally, the City still requires an excessive number of year-end closing journal entries to complete the financial closing process.

Criteria:

In accordance with accounting principles generally accepted in the United States of America, adequate internal controls should be implemented to ensure that all assets, liabilities, revenues and expenses are properly recorded and reported. Furthermore, proper accounting principles should be applied to all financial closing accounts and processes, thus resulting in the proper presentation of all City activities and/or funds.

Cause:

The City’s Finance Department hired an outside accounting firm to assist them with the financial closing and recording process, as well as overall accounting policies and procedures. In reviewing accounting records and audit records from the previous year, the City does appear to have made significant strides in improving this process for the current year. However, the City is still in the process of updating and implementing their accounting processes and reporting policies, which has led to the delay in full implementation of prior year findings and noted corrective action plans.

Effect:

Material adjustments were identified through audit procedures performed which resulted in adjustments, including prior period and current year adjustments to long-term debt, and the accrual of payroll related liabilities that existed as of year-end.

Recommendation:

We recommend that the City continue to work on clarifying roles and responsibilities during the year-end closing process, as well as communication with the outside consultant, to integrate itself more into the closing process for areas in which the consultant provides assistance. This includes further enhancing the process to ensure that all accounting records are properly reflected in the financial statements prior to the commencement of the audit. We also recommend that the consultant is brought into the process earlier in the year, to assist throughout the year and help management implement preventative measures to mitigate financial recording errors as opposed to detective measures in fixing financial reporting errors during the financial closing process.

Management Response:

We agree with the finding as it relates to the period of the audit and have taken significant measures – beginning in December 2018 and continuously through the issuance of the financial statements – to address deficiencies within the City’s year-end closing process, including some of the items mentioned in the management recommendation. Much of the closing issues related to a substantial transition period within the Finance Department to address with prior year findings, including the reorganization of the Finance Department, hiring an outside consultant to assist with the year-end closing and the development of other operational controls, the in-progress development of monthly closing processes, etc. We are confident that with the monthly closing process being implemented, an increase in the familiarity with the year-end closing process, as well as the development and implementation of new processes to improve internal controls over financial closing, the City will be able to substantially decrease the number of journal entries required to close the books and, accordingly, reduce the potential for material errors in the City’s trial balance. Additionally, it will result in a timelier close to the City’s accounting records, which will allow the ability to perform a more thorough review of closing journal entries and related supporting documentation.

CITY OF LEMOORE
SCHEDULE OF FINDINGS AND RESPONSES (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2019

Finding 2019-002 – Material Weakness
Bank Reconciliations

Condition:

Through review of the City's bank reconciliations, we noted that the reconciliations were not being done consistently or in a timely fashion throughout the fiscal year. All were completed at one time by the City's accounting consulting firm after year-end as part of the financial close process.

Criteria:

In accordance with accounting principles generally accepted in the United States of America, adequate internal controls should be implemented to ensure the timely preparation of the bank reconciliations in order to identify any discrepancies, errors, and/or suspicious activity in the City's cash accounts.

Cause:

Staff shortages, changes in management, and lack of ability to properly reconcile due to errors and large reconciling items appear to have caused the delay in the reconciliations of the City's cash accounts.

Effect:

Unreconciled bank accounts can allow for items such as bank errors improperly recorded and unauthorized transactions to go undetected, which limits the City's ability to safeguard those funds.

Recommendation:

The City, either via the Finance Department or the hired accounting consulting firm, should reconcile all cash accounts on a regular basis and additional staff should be trained to help facilitate more timely reconciliations. Management should also ensure that all reconciliations are reviewed for accuracy and completeness on a timely basis.

Management Response:

The City agrees with this finding and has been working internally, and with the consultant to develop controls allowing the City to prepare and adequately review its bank reconciliations within thirty days of the close of each month. Due to the transition that we discussed in Finding 2019-001, as well as preexisting issues in the bank reconciliation process, the City fell behind of its goal. However, we have identified the primary issues previously existing in the bank reconciliation process and believe we are now in a position to meet our goal by the June 2020 bank reconciliation, and do not anticipate future problems.

Finding 2019-003 – Material Weakness
Capital Assets

Condition:

Per audit procedures performed over capital assets, we noted the following conditions:

1. The City had a fire truck purchased via the volunteer fire department, while still under the City's umbrella, for which there was no prior authorization or approval prior to the purchase.
2. We noted errors in the calculation of depreciation and accumulated depreciation that led to a material audit adjustment for under-depreciated assets based on starting acquisition or completion date.
3. We noted capital assets that were recorded as disposed in error, while they were still active in-use assets of the City.

Criteria:

In accordance with accounting principles generally accepted in the United States of America, adequate internal controls should be implemented to ensure that all capital asset purchases are identified, capitalized, depreciated and recorded in the general ledger.

CITY OF LEMOORE
SCHEDULE OF FINDINGS AND RESPONSES (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2019

Criteria (continued):

Furthermore, proper accounting principles should be applied to all asset disposals/deletions when property is sold. This will ensure that all capital asset balances are properly recorded, thus resulting in the proper presentation of all City activities and/or funds.

Cause:

The City lacked proper internal controls over capital asset additions, recording and financial statement presentation.

Effect:

In the current and prior year financial statements, the City's individual fund financial statements were not properly reported, resulting in material adjustments to correct these funds in the current and prior year. In addition, a capital asset was purchased without following the City's purchasing policies.

Recommendation:

We recommend that the City implement different levels or review and/or obtain consultation when recording capital assets to ensure that all current year activity is reported correctly, and all capital assets are properly authorized and reported.

Management Response:

The City agrees with the finding and, in regards to the first condition listed, is developing internal processes, with assistance from the outside consultant, to ensure that capital assets are identified correctly at time of purchase, have been appropriately budgeted, include an appropriate award of construction in accordance with the City's purchasing policy, etc. Additionally, the City is working with the City Attorney to draft updated purchasing policies, which clearly identify the process for purchasing, which will assist in ensuring compliance with all local, State and Federal laws. The City will also be hosting citywide trainings for purchasing after the new policy is adopted by the City Council.

The other two conditions identified, were related to errors in the prior depreciation schedule (resulted in a material audit adjustment) and a typo in the current year depreciation schedule (did not result in an audit adjustment). The first issue was resolved during the closing process, as the City transitioned from the spreadsheet it previously used to track its capital assets to an internally developed spreadsheet overseen by the consultant with the assistance of Finance Department personnel. The second issue was a typo in the spreadsheet that would have been identified during a review process, which will be implemented for the close of the City's accounting records for the year ending June 30, 2020.

Finding 2019-004 – Significant Deficiency
Payroll Reporting

Criteria:

Per federal and state regulations, the City is required to submit quarterly and annual payroll information to the Internal Revenue Service and the State of California. Payroll reporting includes wages paid, taxes withheld and other payroll related information for the City as a whole, as well as all employees of the City.

Condition:

While performing testing on the payroll expenses for the City, we reviewed the quarterly Form 941's as submitted by the City to the Internal Revenue Service. Per our review, we noted obvious errors on the Form 941's as submitted to the Internal Revenue Service.

Cause:

These errors are caused by lack of proper training of employees' completing the forms, and lack of proper review by management prior to the submission of the forms.

CITY OF LEMOORE
SCHEDULE OF FINDINGS AND RESPONSES (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2019

Effect:

The City has submitted payroll reporting forms to the proper regulatory agencies with errors that could lead to issues for the City and their employees.

Recommendation:

We recommend that the City provide training to their payroll staff on the proper ways to complete the forms, as well as implement a stronger internal control structure where the forms are reviewed, reconciled with the underlying payroll records, and ensure they are accurate and complete prior to submitting to the proper agencies.

Management Response:

The City agrees with this finding. As was noted in Finding 2019-001, the City went through a significant transition during the 2019 Fiscal Year. As a result, the current staff was able to review practices and procedures for only three months of that year. The City is making progress in identifying issues related to internal practices, including those related to payroll, and is making significant changes with regard to payroll processes. Management has more oversight over work being performed and is seeking other options for payroll processing in order to more effectively accomplish payroll tasks and responsibilities.

CITY OF LEMOORE
SUMMARY SCHEDULE OF PRIOR YEAR FINDINGS AND RESPONSES
FOR THE YEAR ENDED JUNE 30, 2018

Finding 2018-001 – Material Weakness
Year-End Closing Process

Condition:

During the audit of the City's financial statements, we identified material misstatements in the City's general ledger account balance which necessitated the proposal of numerous audit adjustments. Additionally, the City identified an excessive amount of misstatements to the general ledger account balances subsequent to providing us with the final trial balance for the audit.

Criteria:

A strong system of internal controls and management review requires that general ledger account balances be properly reconciled to a subsidiary ledger or other adequate supporting documentation on a periodic basis, as well as during the year-end financial close process in order to accurately and completely close the current year general ledger in a timely manner. Management is responsible for maintaining its accounting records in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP).

Cause:

The City's Finance Department did not perform an adequate year-end closing process.

Effect:

Almost all areas were misstated resulting in numerous adjusting journal entries which included entries proposed by the City and proposed by us subsequent to receiving the City's final trial balance.

Recommendation:

We recommend that the City perform the following steps in order to address the matters described above:

1. Create a closing checklist to assist with the preparation of audit schedules that are complete, accurate, and reconcile to the City's general ledger account balances. Additionally, ensure that a system is in place to allow the City to perform this in a timely manner.
2. Provide additional assistance to the Finance Department through the hiring of additional competent personnel.
3. Provide additional training in accounting specific to government entities to Finance Department staff in order to ensure that they are current with all financial accounting and reporting requirements as directed by the Governmental Accounting Standards Board.

Management Response:

1. The City will create a checklist of procedures for year-end closing processes.
2. The City has reorganized the Finance Department; creating a Finance Manager position to increase effectiveness in general oversight of the Finance Department personnel and process/procedures.
3. The City is seeking to partner with a financial consultant (if financially feasible) to assist in developing internal procedures/practices to enhance financial reporting.
4. The City will seek to engage in accounting specific training for all Finance Department staff to ensure compliance with all reporting requirements and internal control policies.

Current Year Status:

See current year finding 2019-001.

CITY OF LEMOORE
SUMMARY SCHEDULE OF PRIOR YEAR FINDINGS AND RESPONSES (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2018

Finding 2018-002 – Material Weakness
Journal Entries

Condition:

During a review of the City's general ledger, we noted that an excessive amount of journal entries were recorded in the accounting system. Additionally, we noted that journal entries were being posted to the accounting system prior to being adequately reviewed.

Criteria:

A strong system of internal control and management review is necessary in order to ensure that the City transactions are correctly recorded into the City's accounting system and do not require additional subsequent adjustments.

Cause:

Controls, although designed appropriately, were not being adhered to in order to ensure that all transactions or journal entries were reviewed in a timely manner and correctly posted to the City accounting system, requiring an excessive amount of corrective journal entries.

Effect:

Posting more journal entries than would normally be necessary, or have not been properly reviewed by appropriate personnel, increases the risk of material misstatements due to error or fraud.

Recommendation:

We recommend that the City perform the following steps in order to address the matters described above:

1. Adhere to its current internal control policies and ensure all transactions and journal entries are reviewed and approved by appropriate personnel prior to being posted to the City's accounting system.
2. Provide additional assistance to the Finance Department through the hiring of additional competent personnel.
3. Provide training to all department heads responsible for authorizing disbursements on methods to accurately classify all disbursements to the appropriate budget line items.

Management Response:

1. The City has reorganized the Finance Department; creating a Finance Manager position to increase effectiveness in general oversight of the Finance Department personnel and process/procedures.
2. The City is seeking to partner with a financial consultant (if financially feasible) to assist in developing internal procedures/practices to enhance financial reporting.
3. The City will seek to engage in accounting specific training for all Finance Department staff to ensure compliance with all reporting requirements and internal control policies.
4. The Finance Department reorganization and creating of a Finance Manager will help ensure compliance with existing policies/procedures.
5. The Finance Director and Finance Manager will conduct training with each department head regarding methods for classifying disbursements, as well as other City policies and procedures.

Current Year Status:

See current year finding 2019-001.