

**CITY OF SAN LEANDRO
MEMORANDUM ON INTERNAL CONTROL
AND
REQUIRED COMMUNICATIONS**

FOR THE YEAR ENDED JUNE 30, 2018

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CITY OF SAN LEANDRO
MEMORANDUM ON INTERNAL CONTROL
AND
REQUIRED COMMUNICATIONS

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MEMORANDUM ON INTERNAL CONTROL

To the City Council of
the City of San Leandro, California

In planning and performing our audit of the basic financial statements of the City of San Leandro, California, as of and for the year ended June 30, 2018, 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 auditing procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control. Accordingly, we do not express an opinion on the effectiveness of the City's internal control.

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

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

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

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

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

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

Maze & Associates

Pleasant Hill, California
April 26, 2019

Accountancy Corporation

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Pleasant Hill, CA 94523

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**CITY OF SAN LEANDRO
MEMORANDUM ON INTERNAL CONTROL**

SCHEDULE OF SIGNIFICANT DEFICIENCY

2018-01 Access to and Review of the Vendor Database

Criteria: Staff responsible for processing disbursements should be segregated from the function of maintaining vendor database.

Condition: Currently, the Accounts Payable Clerks who process disbursements are also responsible for maintaining vendor database. The Deputy Finance Director reviews a monthly report that indicates changes and edits in the database. However, this report is manually prepared by the Accounts Payable Clerks.

Effect: Although the Deputy Finance Director reviews the manually generated report, there is a risk of unauthorized changes to vendor database not being detected.

Cause: The City's accounting system cannot generate a report that shows database's audit trail history. Additionally, due to limited staff size, the City believes that it cannot segregate the duties of maintaining the vendor database from the Accounts Payable Clerks.

Recommendation: The City should work with its accounting software vendor for the possibility of generating audit trail history reports of the vendor database. If that is not possible, an employee who does not have edit rights to the vendor database should conduct a random audit periodically to ensure that the information on the database is accurate and vendor details supported.

Management Response: As noted, the City's Finance Department is limited due to staff size. While we understand the need for segregation of duties as it relates to changes and edits to the vendor database, implementing such a process would be inefficient for operations. A risk mitigation step currently being followed is the weekly review and approval of vouchers and disbursements by both the Assistant Finance Director and the Assistant City Manager. Going forward, to ensure the vendor database is accurate and supported, the Finance Department will conduct a completeness and existence review of the database on a monthly basis.

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SCHEDULE OF OTHER MATTERS

NEW GASB PRONOUNCEMENTS OR PRONOUNCEMENTS NOT YET EFFECTIVE

The following comment represents new pronouncements taking affect in the next few years. We cite them here to keep you informed of developments:

Effective in fiscal year 2018-19:

GASB 83 – *Certain Asset Retirement Obligations*

This Statement addresses accounting and financial reporting for certain asset retirement obligations (AROs). An ARO is a legally enforceable liability associated with the retirement of a tangible capital asset. A government that has legal obligations to perform future asset retirement activities related to its tangible capital assets should recognize a liability based on the guidance in this Statement.

GASB 88 – *Certain Disclosures Related to Debt, including Direct Borrowings and Direct Placements*

This Statement defines debt for purposes of disclosure in notes to financial statements as a liability that arises from a contractual obligation to pay cash (or other assets that may be used in lieu of cash) in one or more payments to settle an amount that is fixed at the date the contractual obligation is established. This Statement requires that additional essential information related to debt be disclosed in notes to financial statements, including unused lines of credit; assets pledged as collateral for the debt; and terms specified in debt agreements related to significant events of default with finance-related consequences, significant termination events with finance-related consequences, and significant subjective acceleration clauses.

Effective in fiscal year 2019-20:

GASB 84 – *Fiduciary Activities*

This Statement establishes criteria for identifying fiduciary activities of all state and local governments. The focus of the criteria generally is on (1) whether a government is controlling the assets of the fiduciary activity and (2) the beneficiaries with whom a fiduciary relationship exists. Separate criteria are included to identify fiduciary component units and postemployment benefit arrangements that are fiduciary activities.

GASB 90 – *Majority Equity Interests—an amendment of GASB Statements No. 14 and No. 61*

This Statement defines a majority equity interest and specifies that a majority equity interest in a legally separate organization should be reported as an investment if a government's holding of the equity interest meets the definition of an investment. A majority equity interest that meets the definition of an investment should be measured using the equity method, unless it is held by a special-purpose government engaged only in fiduciary activities, a fiduciary fund, or an endowment (including permanent and term endowments) or permanent fund. Those governments and funds should measure the majority equity interest at fair value. For all other holdings of a majority equity interest in a legally separate organization, a government should report the legally separate organization as a component unit, and the government or fund that holds the equity interest should report an asset related to the majority equity interest using the equity method. This Statement establishes that ownership of a majority equity interest in a legally separate organization results in the government being financially accountable for the legally separate organization and, therefore, the government should report that organization as a component unit.

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SCHEDULE OF OTHER MATTERS

Effective in fiscal year 2020-21:

GASB 87 – Leases

This Statement will increase the usefulness of governments' financial statements by requiring reporting of certain lease liabilities that currently are not reported. It will enhance comparability of financial statements among governments by requiring lessees and lessors to report leases under a single model. This Statement also will enhance the decision-usefulness of the information provided to financial statement users by requiring notes to financial statements related to the timing, significance, and purpose of a government's leasing arrangements.

GASB 89 – Accounting for Interest Cost Incurred before the End of a Construction Period

This Statement establishes accounting requirements for interest cost incurred before the end of a construction period. Such interest cost includes all interest that previously was accounted for in accordance with the requirements of paragraphs 5–22 of Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, which are superseded by this Statement. This Statement requires that interest cost incurred before the end of a construction period be recognized as an expense in the period in which the cost is incurred for financial statements prepared using the economic resources measurement focus. As a result, interest cost incurred before the end of a construction period will not be included in the historical cost of a capital asset reported in a business-type activity or enterprise fund. This Statement also reiterates that in financial statements prepared using the current financial resources measurement focus, interest cost incurred before the end of a construction period should be recognized as an expenditure on a basis consistent with governmental fund accounting principles.

**CITY OF SAN LEANDRO
MEMORANDUM ON INTERNAL CONTROL**

SCHEDULE OF PRIOR YEAR SIGNIFICANT DEFICIENCIES

2017-01 Year-End Close

Criteria: Management is responsible for the accuracy of the financial statements and the maintenance of the general ledger system and other records used to prepare the financial statements. Timeliness of the financial statements is key to a best practices approach in providing policy makers the year-end financial results soon enough to be useful and to meet filing deadlines.

Condition: The City provided approximately twenty-five post-closing adjusting journal entries which resulted in a delay in the timely completion of multiple financial statement items primarily pension, cash and investments, and capital assets.

Cause: The City has experienced key staff turnover since fiscal year 2015-2016 and as a result fell behind in the completion of the year-end close process.

Effect: Without adequate staff resources to ensure that the year-end closing was completed properly and accurately, there is an increased risk that material misstatements of the City's financial statements will not be prevented, or detected and corrected on a timely basis.

Recommendation: The City's fiscal year end closing process and journal entries associated with the close should be completed and posted prior to the commencement of year-end fieldwork. Staff should plan accordingly to ensure that a complete close of the books is performed prior to scheduling auditors to perform fieldwork.

Current Status: Implemented

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MEMORANDUM ON INTERNAL CONTROL**

SCHEDULE OF PRIOR YEAR SIGNIFICANT DEFICIENCIES

2016-01 Year-End Close

Criteria: Management is responsible for the accuracy of the financial statements and the maintenance of the general ledger system and other records used to prepare the financial statements. Timeliness of the financial statements is key to a best practices approach in providing policy makers the year-end financial results soon enough to be useful and to meet filing deadlines.

Condition: The City provided approximately forty post-closing adjusting journal entries which resulted in a delay in the timely completion of multiple financial statement items primarily including cash and investments and capital assets.

Cause: The City has experienced staff turnover during fiscal year 2015-2016 and as a result fell behind in the completion of the year-end close process.

Effect: Without adequate staff resources to ensure that the year-end closing was completed properly and accurately, there is an increased risk that material misstatements of the City's financial statements will not be prevented, or detected and corrected on a timely basis.

Recommendation: The City's fiscal year end closing process and journal entries associated with the close should be completed and posted prior to the commencement of fieldwork. Staff should plan accordingly to ensure that a complete close of the books is performed prior to scheduling auditors to perform fieldwork.

Current Status: Implemented.

REQUIRED COMMUNICATIONS

To the City Council of
the City of San Leandro, California

We have audited the basic financial statements of the City of San Leandro for the year ended June 30, 2018. Professional standards require that we communicate to you the following information related to our audit under generally accepted auditing standards and *Government Auditing Standards* and the Uniform Guidance.

Significant Audit Findings

Accounting Policies

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by City of San Leandro are described in Note 1 to the financial statements. No new accounting policies were adopted, and the application of existing policies were not changed during the year, except as follows:

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

GASB 81 – Irrevocable Split-Interest Agreements

GASB 85 – Omnibus 2017

GASB 86 – Certain Debt Extinguishment Issues

The following Governmental Accounting Standards Board (GASB) pronouncement became effective, and as disclosed in Note 9E to the financial statements, required a prior period adjustment for the cumulative effect on the financial statements.

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

Unusual Transactions, Controversial or Emerging Areas

We noted no transactions entered into by the City during the year for which there is a lack of authoritative guidance or consensus. All significant transactions have been recognized in the financial statements in the proper period.

Accounting Estimates

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

Estimate of Depreciation: Management's estimate of the depreciation is based on useful lives determined by management. These lives have been determined by management based on the expected useful life of assets as disclosed in Note 1H. to the financial statements. We evaluated the key factors and assumptions used to develop the depreciation estimate and determined that it is reasonable in relation to the basic financial statements taken as a whole.

Estimated Fair Value of Investments: As of June 30, 2018, the City's cash and investments were measured by fair value as disclosed in Note 2 to the financial statements. Fair value is essentially market pricing in effect as of June 30, 2018. These fair values are not required to be adjusted for changes in general market conditions occurring subsequent to June 30, 2018.

Estimated Net Pension Liabilities and Pension-Related Deferred Outflows and Inflows of Resources: Management's estimate of the net pension liabilities and deferred outflows/inflows of resources are disclosed in Note 13 to the financial statements and are based on actuarial studies determined by a consultant, which are based on the experience of the City. We evaluated the key factors and assumptions used to develop the estimate and determined that it is reasonable in relation to the basic financial statements taken as a whole.

Estimated Net OPEB Liabilities and OPEB-Related Deferred Outflows and Inflows of Resources: Management's estimate of the net OPEB liabilities and deferred outflows/inflows of resources are disclosed in Note 14 to the financial statements and are based on actuarial studies determined by a consultant, which are based on the experience of the City. We evaluated the key factors and assumptions used to develop the estimate and determined that it is reasonable in relation to the basic financial statements taken as a whole.

Disclosures

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

Difficulties Encountered in Performing the Audit

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

Corrected and Uncorrected Misstatements

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are clearly trivial, and communicate them to the appropriate level of management. Management has corrected all such misstatements. In addition, none of the misstatements detected as a result of audit procedures and corrected by management were material, either individually or in the aggregate, to each opinion unit's financial statements taken as a whole.

Professional standards require us to accumulate all known and likely uncorrected misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management. We have no such misstatements to report to the City Council.

Disagreements with Management

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

Management Representations

We have requested certain representations from management that are included in a management representation letter dated April 26, 2019.

Management Consultations with Other Independent Accountants

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

Other Audit Findings or Issues

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

Other Information Accompanying the Financial Statements

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

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

We were not engaged to report on the Introductory and Statistical Sections which accompany the financial statements, but are not required supplementary information. Such information has not been subjected to the auditing procedures applied in the audit of the basic financial statements, and accordingly, we do not express an opinion or provide any assurance on them.

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

Maze & Associates

Pleasant Hill, California

April 26, 2019