



**Independent Auditor's 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***

City Council  
City of Lemon Grove  
Lemon Grove, 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, business-type activities, each major fund and the aggregate remaining fund information of the City of Lemon Grove (City), as of and for the year ended June 30, 2017, 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 10, 2018.

**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.

Our consideration of internal control was for the limited purpose described in the preceding 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 were not identified. However, as described in the accompanying schedule of findings and responses, we identified certain deficiencies in internal control that we consider to be material weaknesses.

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. We consider the deficiencies described in item 2017-1 in the accompanying schedule of findings and responses to be a material weakness.

A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies described in the accompanying schedule of findings and responses as items 2017-2 to 2017-5 to be significant deficiencies.

### **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 of Lemon Grove's Responses to Findings**

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

### **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 City'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 organization's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

*Van Lant & Fankhaed, LLP*

April 10, 2018

**CITY OF LEMON GROVE  
SCHEDULE OF FINDINGS AND RESPONSES  
Year Ended June 30, 2017**

***2017-1 Accounting Records/Financial Reporting***

*Condition:*

In preparation for the 2016-17 annual audit, the City's Finance staff performed analysis and reconciliations of various accounts in the City's general ledger. Although the City provided us with analysis and supporting documentation when we began our year-end audit fieldwork, it became apparent that certain accounts had not yet been thoroughly analyzed and reconciled to supporting documentation. When we brought this to the City's attention, eventually the required analysis, reconciliations, and adjusting journal entries were made by City Finance personnel. However, this was completed several months after year-end, with adjustments still being made to the June 30, 2017 accounting records as late as February 2018. Affected accounts included certain revenues, receivables, capital assets, claims payable, and various payroll-related liabilities. Normally, the year-end accounting records should be fully analyzed, adjusted and reconciled within a few months after year-end.

As disclosed in the City's June 30, 2017 financial statements, some of the required adjustments involved revisions to the June 30, 2016 balances (prior period adjustments). It appeared that certain accounts had not been analyzed/reconciled for quite some time.

*Criteria:*

The City's management is responsible for establishing and maintaining effective internal controls over financial reporting to help ensure that appropriate goals and objectives are met. This responsibility includes the selection and application of accounting principles, ensuring that financial information is reliable and properly recorded, and evaluating and monitoring ongoing activities. The City's management is responsible for preparing accurate year-end accounting records and financial statements, in a timely manner.

Reconciliation and review of all balance sheet accounts and various revenue and expenditure accounts on a recurring basis, and especially at year-end, is a vital part of maintaining the integrity of the accounting and financial reporting system. Periodic reconciliations of all balance sheet and other selected accounts provide accurate data from which to base decisions, prevent costly errors and provide timely financial reports. Year-end analysis and documentation should be maintained on file, in an organized fashion, to provide evidence in support of financial statement amounts and disclosures. The City is subject to various financial reporting deadlines, including State and Federal requirements. This includes the California Government Code and the Single Audit requirements of the Federal Government.

If accounting records are not adequately maintained throughout each fiscal year, the year-end closing process tends to be more difficult and time-consuming, and may contribute to delays in issuing year-end reports.

**CITY OF LEMON GROVE**  
**SCHEDULE OF FINDINGS AND RESPONSES**  
**Year Ended June 30, 2017**

***2017-1 Accounting Records/Financial Reporting - Continued***

*Cause of Condition:*

Based on the City's prior year audit reports and our firm's experience while performing the 2016-17 annual audit, the City's Finance Department has had significant problems in maintaining consistency in management personnel. During the 2016-17 audit process, the City had two temporary, part-time Finance Directors, while the Finance Manager resigned in the middle of our audit fieldwork without any notice.

In addition, it appears the City has not established and documented detailed accounting procedures for the year-end closing process.

*Potential Effect of Condition:*

Because of the issues mentioned above, the 2016-17 audit process was delayed. The City was not able to issue audited financial statements in a timely manner. Overall, the audit process was inefficient from our perspective, and, most likely, the City's perspective. In addition, the financial information and reports being utilized by City management were not necessarily accurate throughout the 2016-17 fiscal year, due to the significant adjustments made during the audit process.

*Recommendation:*

In order to maintain the integrity of the accounting and financial reporting system, and to ensure timely reporting, we recommend the City develop detailed, written procedures for the year-end closing process. This should include a checklist of all analysis/reconciliations to be performed along with the applicable due dates. All balance sheet accounts and other selected accounts should be analyzed as appropriate. We suggest a schedule of accounting functions to be performed be prepared with the provision for signing off upon completion. This will provide documentation for the year-end closing process even if there is turnover in Finance personnel.

The City should re-evaluate personnel practices and philosophies, especially in the Finance Department. While the City is subject to budget constraints, as are most government agencies, maintaining consistency in Finance management positions will help ensure accurate and timely financial reporting, and also compliance with applicable laws, regulations, and contract provisions. In the long run, having consistent, highly-qualified personnel in the Finance Department will help ensure that the City Council and other City Management are receiving accurate and timely financial information.

**CITY OF LEMON GROVE  
SCHEDULE OF FINDINGS AND RESPONSES  
Year Ended June 30, 2017**

***2017-1 Accounting Records/Financial Reporting - Continued***

*Management's Response:*

We agree that the City's FY 2017 end-of-year closing was too long after year-end. As noted in the Auditor's "Cause of Condition" section, the City encountered some unusual personnel issues in the Finance Department. The City's management is currently implementing a plan to upgrade and stabilize the Finance Department. The City will establish a year-end checklist and reconcile all balance sheet accounts yearly at a minimum.

***2017-2 Segregation of Incompatible Duties***

*Condition:*

Our audit procedures included a review and evaluation of the City's business license function, including the billing and collection of business license fees. Based on our procedures, we noted that the cash receipts clerk at City Hall is responsible for administering the business license program. This includes the billing and collection functions, and maintaining the business license database.

*Criteria:*

In a strong internal control environment, the billing and collection functions should be segregated. The individual responsible for administering the business license function should not also be handling incoming payments.

*Cause of Condition:*

Incompatible duties performed by the same individual creates opportunity for business license revenues to be received but not recorded in the City's general ledger.

*Potential Effect of Condition:*

Lack of internal controls in the City's business license function could result in payments being collected that are not ultimately recorded in the City's general ledger and deposited into the City's bank accounts.

*Recommendation:*

We recommend the City evaluate the business license function to determine if the collection function could be segregated from the administration/billing function. At a minimum, City management should establish procedures for independent personnel to reconcile the business license activity to the revenue in the general ledger and bank deposits.

**CITY OF LEMON GROVE  
SCHEDULE OF FINDINGS AND RESPONSES  
Year Ended June 30, 2017**

***2017-2 Segregation of Incompatible Duties - Continued***

*Management's Response:*

The City agrees that in a strong internal control environment, billing and collection functions should be segregated. The City's Finance Department has limited staff and complete segregation of duties is not always achievable. The City will institute several mitigating controls (for example: tasking the Accounting Analyst the responsibility of matching the business license reports with bank deposits on a monthly basis) to reduce the risks of fraud and errors that can occur with weak internal controls.

***2017-3 Old Outstanding Checks/Bank Account Reconciliations***

*Condition:*

Our review of various bank account reconciliations during the 2016-17 audit indicated that the City was carrying over several old outstanding checks each month. Some of these checks were issued in 2010, which does not appear to be in compliance with the City's established procedures. Also, the City has custody of certain funds and accounts held by a fiscal agent. During our audit, we noted these accounts had not been fully reconciled to the City's general ledger.

*Criteria:*

The City's "Financial Policy and Procedures Manual" includes a section regarding bank account reconciliations. This includes a section providing guidance on stale dated checks identified during the bank reconciliation process. It describes in detail the procedures to be performed for old outstanding checks.

*Cause of Condition:*

It is not clear why the City has not followed its established procedures regarding stale dated checks, other than the lack of consistency in the Finance Department's management function. For the accounts held by a fiscal agent, the personnel turnover in the Finance Department appears to be the cause of certain accounts not being reconciled in a timely manner.

*Potential Effect of Condition:*

The City has recorded decreases to cash along with the related expenditures, for checks issued many years ago, which have not cleared the bank account. This can potentially result in cash (and fund balance) being understated, and the opportunity for the old outstanding checks to be misappropriated. For the fiscal agent accounts, various activity had not been recorded or reconciled for the 2016-17 fiscal year.

**CITY OF LEMON GROVE  
SCHEDULE OF FINDINGS AND RESPONSES  
Year Ended June 30, 2017**

***2017-3 Old Outstanding Checks/Bank Account Reconciliations - Continued***

*Recommendation:*

We recommend that the City's management review the bank reconciliation function and procedures in relation to the established Financial Policy and Procedures Manual to determine if procedures are being followed. The review process for bank account reconciliations should also be revisited and revised accordingly, to ensure applicable policies are being followed.

*Management's Response:*

The City's bank reconciliation policy is in review and will be updated. Finance management will monitor the bank reconciliation process to ensure it is being followed.

***2017-4 Travel Expenses/City Credit Cards***

*Condition:*

While conducting audit procedures relating to disbursements/expenditures, we were unable to obtain a list of all City-issued credit cards. We also noted that the required travel authorization forms were not included in the supporting documentation for certain travel expenses paid by the City's credit cards. In our testing of credit card statements, we noted that one of them did not have the required signature for payment approval.

*Criteria:*

The City has established policies regarding the use of City credit cards and travel expenses. This includes the utilization of a "Travel Authorization/Expense Report."

*Cause of Condition:*

It appears that the City has not maintained a list of City-issued credit cards. It is not clear why the City has not adhered to the established procedures regarding "Travel Authorization/Expense Reports." Lack of approval signatures may be the result of the issues described in item 2017-1 above.

*Potential Effect of Condition:*

The City's travel expenses and other payments by credit card may not be adequately reviewed and approved. The condition described above could result in a lack of transparency for some of the City's disbursements/expenditures.

**CITY OF LEMON GROVE  
SCHEDULE OF FINDINGS AND RESPONSES  
Year Ended June 30, 2017**

***2017-4 Travel Expenses/City Credit Cards - Continued***

*Recommendation:*

We recommend the City take steps to ensure that all travel costs and credit card payments are properly reviewed, approved and documented, in accordance with established policy.

*Management's Response:*

The City's travel form will be updated to conform to the City's travel policy. The City is creating a list of City-issued credit cards and will maintain the list going forward. All City travel costs and credit card payments will be reviewed, approved and documented, in accordance with established policy.

***2017-5 Allocation of Salaries/Overhead to Restricted Funds***

*Condition:*

Based on our testing of costs charged to the City's Gas Tax Fund (Fund), it appears the City is charging both direct salaries and indirect overhead costs to the Fund. Various percentages are used to allocate the salaries of certain positions, including Finance and Human Resources personnel, to the Fund. However, the City's staff was not able to provide us with documentation in support of these allocation methods. For example, we were not able to find a cost allocation study, or plan, which would provide evidence that these allocations are reasonable.

*Criteria:*

The State Controller's Office has established "Guidelines Relating to Gas Tax Expenditures" to be used by Cities and Counties. Section 440 regarding Overhead indicates, "Overhead will only be allowed via an approved cost allocation plan or an equitable and auditable distribution of overhead to all departments." For the sake of transparency, the City should ensure that all costs charged to restricted funds are adequately documented. This documentation should include evidence that overhead costs are equitable and reasonable, in relation to all costs incurred by the City.

*Cause of Condition:*

The City was not able to provide us with a cost allocation study or plan in support of the costs mentioned above. It is not clear why the City has not maintained documentation to ensure compliance with the State's requirements and to document the reasonableness of all overhead costs.



**CITY OF LEMON GROVE  
SCHEDULE OF FINDINGS AND RESPONSES  
Year Ended June 30, 2017**

***2017-5 Allocation of Salaries/Overhead to Restricted Funds - Continued***

*Potential Effect of Condition:*

Unallowable costs could be charged to restricted funds, including the Gas Tax Fund.

*Recommendation:*

Based on discussions with City staff, it appears the City has taken steps to contract with a consultant to perform a salary distribution study. We recommend the City continue in these efforts to ensure all overhead costs are properly documented.

*Management's Response:*

The City is continuing its efforts to ensure all overhead costs are properly documented.