

**Single Audit Report
City of Montebello, California
Year ended June 30, 2012
with Report of Independent Auditors**

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**Report of Independent Auditors 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***

**The Honorable Mayor and Members of City Council
City of Montebello**

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Montebello, California, as of and for the year ended June 30, 2012, which collectively comprise the City of Montebello's basic financial statements, and have issued our report thereon dated March 28, 2013. We conducted our audit in accordance with 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.

Internal Control Over Financial Reporting

Management of the City of Montebello is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the City of Montebello's internal control over financial reporting as a basis for designing our auditing procedures 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 of Montebello's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the City of Montebello's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and; therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying schedule of findings and questioned costs, we identified a certain deficiency in internal control over financial reporting that we consider to be a material weakness.

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 deficiency described in the accompanying schedule of findings and questioned costs as finding F12-01 to be a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City of Montebello's financial statements are free of 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*.

We noted certain other matters that we reported to the management of the City of Montebello in a separate letter dated March 28, 2013.

The City of Montebello's responses to the findings identified in our audit are described in the accompanying schedule of findings and questioned costs. We did not audit the City of Montebello's responses and accordingly, we express no opinion on the responses.

This report is intended solely for the information and use of the City Council, management, federal and state awarding agencies, and pass-through entities and is not intended to be, and should not be, used by anyone other than these specific parties.

Vargus + Company LLP

Los Angeles, California
March 28, 2013

Report of Independent Auditors on Compliance with Requirements that Could Have a Direct and Material Effect on Each Major Program and on Internal Control over Compliance, and on the Schedule of Expenditures of Federal Awards in Accordance with OMB Circular A-133

**The Honorable Mayor and Members of City Council
City of Montebello**

Compliance

We have audited the compliance of the City of Montebello, California with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that could have a direct and material effect on each of the City's major federal programs for the year ended June 30, 2012. The City of Montebello's major federal programs are identified in the summary of auditors' results section of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of the City of Montebello's management. Our responsibility is to express an opinion on the City of Montebello's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States; and *OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and *OMB Circular A-133* require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the City of Montebello's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the City of Montebello's compliance with those requirements.

In our opinion, the City of Montebello complied, in all material respects, with the requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2012. However, the results of our auditing procedures disclosed an instance of noncompliance with those requirements, which is required to be reported in accordance with *OMB Circular A-133* and which is described in the accompanying schedule of findings and questioned costs as F12-02.

Internal Control Over Compliance

The management of the City of Montebello is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the City of Montebello's internal control over compliance with the requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with *OMB Circular A-133*, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the City of Montebello's internal control over compliance.

A *deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance; such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented and corrected on a timely basis.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

The City's responses to the findings identified in our audit are described in the accompanying schedule of findings and questioned costs. We did not audit the City's responses and, accordingly, we express no opinion on the responses.

Schedule of Expenditures of Federal Awards

We have audited the financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the City as of and for the year ended June 30, 2012, and have issued our report thereon dated March 28, 2013, which contained unqualified opinions on those financial statements. Our audit was performed for the purpose of forming opinions on the financial statements as a whole. The accompanying schedule of expenditures of federal awards is presented for the purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of expenditures of federal awards is fairly stated in all material respects in relation to the financial statements as a whole.

This report is intended solely for the information and use of the City Council, management, federal and state awarding agencies, and pass-through entities and is not intended to be, and should not be, used by anyone other than these specified parties.



Los Angeles, California
March 28, 2013

City of Montebello
Schedule of Expenditures of Federal Awards
Year ended June 30, 2012

Federal Grantor/Pass-Through Grantor/Program Title	Federal CFDA Number	Program Identification Number	Federal Award Expenditures
U.S. Department of Transportation			
Direct Assistance			
Federal Transit Cluster:			
ARRA - Federal Transit Cluster	20.507	CA96X083	\$ <u>2,208,028</u>
Federal Transit - Formula Grants (Urbanized Area Formula Grants)	20.507	CA90Y790	1,957,136
	20.507	CA90Y692	168,687
	20.507	CA040204	158,000
	20.507	CA90Y900	<u>74,451</u>
			<u>2,358,274</u>
Total U.S. Department of Transportation			<u>4,566,302</u> *
U.S. Department of Housing and Urban Development			
Direct Assistance:			
Community Development Block Grant	14.218	B-11-MC-06-0555	633,279 *
Home Investment Partnership Program	14.239	M-10-MC-06-0543	<u>34,832</u>
Total U.S. Department of Housing and Urban Development			<u>668,111</u>
U.S. Department of Justice			
Direct Assistance			
Asset Forfeiture	16.000	CA0194700	<u>253,328</u>
Total U.S. Department of Justice			<u>253,328</u>
U.S. Department of Agriculture			
Passed-through the State of California, Department of Education			
Summer Food Service Program for Children	10.559	not available	<u>74,784</u>
Total U.S. Department of Agriculture			<u>74,784</u>
U.S. Department of Homeland Security			
Direct Assistance			
Rail and Transit Security Grant Program	97.075	2010RAT0K048	<u>1,638</u>
Total U.S. Department of Homeland Security			<u>1,638</u>
Total Expenditures of Federal Awards			<u>\$ 5,564,163</u>

* Denotes major program

See Notes to the Schedule of Expenditures of Federal Awards.

NOTE 1 GENERAL

The accompanying schedule of expenditures of federal awards presents the activity of all federal financial assistance programs of the City of Montebello (City). The City's reporting entity is defined in Note 1 of the notes to the City's basic financial statements. All financial assistance received directly from federal agencies is included in the accompanying schedule.

NOTE 2 BASIS OF ACCOUNTING

The accompanying schedule of expenditures of federal awards is presented using the modified accrual basis of accounting for governmental funds and the accrual basis for proprietary funds, which is described in Note 1 of the notes to the City's basic financial statements.

NOTE 3 RELATIONSHIP TO COMPREHENSIVE ANNUAL FINANCIAL REPORT

Amounts reported in the accompanying schedule of expenditures of federal awards agree to the general ledger and are included in the amounts reported within the City's Comprehensive Annual Financial Report.

NOTE 4 MAJOR PROGRAMS

The following Catalog of Federal Domestic Assistance (CFDA) programs were tested as major programs.

Federal Transit: Urbanized Area Formula Program	CFDA #20.507
Community Development Block Grant Program	CFDA #14.218

NOTE 5 SUBRECIPIENTS

There were subrecipient grants awarded from U.S. Department of Housing and Urban Development, Community Development Block Grant. These subrecipient grants totaled \$65,000.

Section I – Summary of Auditors’ Results

Financial Statements

Type of auditors’ report issued on the financial statements: Unqualified

Internal control over financial reporting:

- Material weakness(es) identified: Yes
- Significant deficiency(ies) identified that are not considered to be material weaknesses? No

Noncompliance material to the financial statements noted: No

Federal Awards

Internal control over its major programs:

- Material weakness(es) identified: No
- Significant deficiency(ies) identified that are not considered to be material weaknesses? None reported

Type of auditors’ report issued on compliance for major programs: Unqualified

Any audit findings disclosed that are required to be reported in accordance with Section .510(a) of OMB Circular A-133? Yes (F12-01 to F12-02)

Identification of Major Programs:

<u>CFDA Number</u>	<u>Name of Federal Program or Cluster</u>
20.507	Federal Transit Cluster
14.218	Community Development Block Grant Program

Dollar threshold used to distinguish between Type A and Type B programs: \$300,000

Auditee qualified as a low-risk auditee: No

Section II – Financial Statement Findings

Finding F12-01 – Year-end Adjustments (Material Weakness)

Criteria or Specific Requirement

Adequate effective internal control systems should be in place to permit the preparation of financial statements that fairly present financial activities and financial position.

Condition

As part of the year-end closing process, there were more than 40 adjusting journal entries required to bring the account balances into agreement with the supporting detail schedules. Some of these adjustments are considered significant and were essential to the preparation of accurate financial statements.

Cause and Effect

Key positions within the City's Finance Department had been vacant for nearly a year or longer as a result of staff turnover and were filled late in fiscal year 2012. While Finance staff made great efforts to ensure that all closing entries were processed timely, challenges with resolving issues from the past, including system security and account set up, consumed a great deal of time and hindered the City's ability to properly maintain the accounting records and monitor them for accuracy. The resulting undetected errors delayed the year-end closing of the books and thus the audit of those books.

Recommendation

To provide assurance of accurate interim financial reports and allow for the timely generation of reliable annual financial statements, we recommend the City perform monthly closing procedures by analyzing the accuracy of the month-end account balances and correcting errors found during this process. Variances should be investigated before adjustments are made, and all adjustments should be reviewed by qualified Finance Department personnel. This procedure will substantially reduce the amount of adjusting journal entries at year-end, improve the reliability of interim financial statements and allow for more timely completion of the annual financial statements and independent audit.

Views of Responsible Officials and Planned Corrective Action

The Finance Department filled three key positions in March 2012, several of which had been vacant for nearly a year or longer, as a result of staff turnover. While Finance staff made great efforts to ensure that all closing entries were processed timely, challenges with resolving issues from the past, including system security and account set up, consumed a great deal of time and energy to ensure that the books were closed to begin the audit. Additionally, during May 2012, Finance staff implemented the City-wide cashiering module in order to ensure proper collection and accounting of cash receipts from all points of cash collections at various City facilities, including the Transit Department and the Municipal Golf Course. The implementation of the cashiering module took a great deal of time and effort to ensure that the books were closed to begin the audit. We concur with the recommendation and will continue to refine the month end and year end closing process.

Section III – Federal Award Findings

Program: Community Development Block Grant
CFDA No: 14.218
Federal Grantor: Department of Housing and Urban Development (HUD)
Pass-through: Not Applicable
Award No.: B-11-MC-06-0555
Compliance Requirement: Reporting
Questioned Costs: N/A

Finding 12-02

Criteria or Requirement

The grant agreement requires the grantee to submit SF-425 Federal Financial Report every 30 calendar days following the end of the calendar quarter.

Condition Found

The City overlooked the filing of the quarterly Federal Financial Report (SF-425).

Cause and Effect

The failure to file the quarterly Federal Financial Report was caused by City staff turnover.

Recommendation

The City should establish procedures to ensure that all reports required by the grant agreement are filed timely.

Views of Responsible Officials

As of the date of this report, this matter has been resolved. Additional staff training and oversight will be implemented to prevent the oversight.

City of Montebello
Status of Prior Year Findings and Questioned Costs
Year ended June 30, 2012

Finding Reference	Finding Description	Recommendation	Current Status	Explanation if not fully implemented
11-01	Cash – bank reconciliation	<p>We recommend certain improvements in the bank reconciliation process:</p> <ol style="list-style-type: none"> 1. The bank reconciliations should be reconciled to the general ledger cash accounts by a member of the City's staff immediately after the end of each month. All reconciling items should be investigated and either substantiated or corrected. 2. A member of the City's management should review all bank reconciliations every month. The bank reconciliations should be initialed by the reviewer. 	Substantially Implemented	Small unreconciled balances are still showing in the bank reconciliations.
11-02	Cash – deposits	An employee other than the person who reconciles cash receipts should be assigned to enter cash receipts into the accounting system.	Implemented	

City of Montebello
Status of Prior Year Findings and Questioned Costs
Year ended June 30, 2012

11-03	Documentation of internal control	The City should update the administrative policies manual, centralize the procedures manuals, and make them available to all employees. Management should effectively communicate to employees how important these policies and procedures are. Management should evaluate the policies and procedures from time to time and evaluate the employees' adherence to the policies and procedures.	Not implemented	While efforts are being made to review and update the manuals, it will continue to remain a work in progress due to fiscal constraint and reduction in staffing levels.
11-04	Financial close and reporting	We recommend that steps be taken to improve the design of the City's financial close and reporting process, document such process and monitor its implementation throughout the year. This may include improving the use of accounting software to assist in this process. Additionally, we recommend training of City staff to improve their knowledge of governmental accounting.	Not implemented.	See finding F-12-01.

11-05	Capital assets and long-term debt account groups	We recommend that all activity affecting long-term debt and capital assets be recorded in their respective account groups. The changes in the long-term debt group should be reconciled to the respective activity in the funds, and the capital asset account group should be reconciled to the activity in the funds and the capital asset listing prepared by Wellspring Company (Wellspring).	Capital asset recommendation not implemented.	The City recently purchased a new financial system, New Worlds, which will be implemented in FY12/13. Included in the new financial software is a fixed asset component that will be utilized to capture the fixed asset purchases and appropriate depreciation calculations.
11-06	Capital Assets	We recommend that the City establish better controls to identify the capital expenditures that need to be capitalized, provide the information to Wellspring, and properly record the capital assets in the City's general ledger. We recommend improving management's monitoring so that the controls are properly implemented. We also recommend periodic reconciliation of the Wellspring information and the City's general ledger to the Transit Department's capital reserve worksheet that summarizes the Transit Fund's capital expenditures.	Not implemented.	The City recently purchased a new financial system, New Worlds, which will be implemented in FY12/13. Included in the new financial software is a fixed asset component that will be utilized to capture the fixed asset purchases and appropriate depreciation calculations.

City of Montebello
Status of Prior Year Findings and Questioned Costs
Year ended June 30, 2012

11-07	Cash allocation	The existing policy is reflective of how various general ledger accounts were set up in the past. Additionally, efforts and due diligence is underway to account for the three project areas separately and to provide for automated methods of accounting for cash balances by project area.	Implemented.
11-08	Agency project allocation	We recommend establishing an accounting system that will enable the Agency to account for each project area within the system that is already in place on a regular basis. This can be done by either establishing new accounts or establishing cost centers within each account in the general ledger.	Implemented. RDA is dissolved.
11-09	Business assistance loans	We recommend that the Agency establish policies and procedures to ensure that they are properly accounting for and collective these receivables.	Implemented. RDA is dissolved.
11-10	Identification of ARRA funds	We recommend that controls be put in place to properly identify the types of federal awards received and expended.	Implemented.
11-11	Cities financial transactions report	We recommend that controls be implemented to ensure that the City is in compliance with reporting requirements of the SCO.	Implemented.

City of Montebello
Status of Prior Year Findings and Questioned Costs
Year ended June 30, 2012

11-12	Administrative costs – low and moderate income housing	We recommend the Agency finalize a cost allocation study that adequately supports the Agency’s allocation of administrative costs.	RDA is dissolved.
11-13	Administrative costs - Agency and Transit Fund	We recommend that the City finalize a cost allocation study that adequately supports the City’s allocation of administrative costs.	RDA is dissolved
11-14	Housing database	We recommend the Agency establish and maintain a housing database.	RDA is dissolved

