

CITY OF HESPERIA, CALIFORNIA
SINGLE AUDIT OF FEDERALLY ASSISTED
GRANT PROGRAMS

JUNE 30, 2012

CITY OF HESPERIA

TABLE OF CONTENTS

June 30, 2012

	<u>Page Number</u>
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 <i>Government Auditing Standards</i>	1 - 2
Independent Auditors' Report on Compliance with Requirements That Could Have a Direct and Material Effect on Each Major Program and on Internal Control Over Compliance in Accordance with <u>OMB Circular A-133</u> and on the Schedule of Expenditures of Federal Awards	3 - 5
Schedule of Expenditures of Federal Awards and Schedule of Findings and Questioned Costs:	
Schedule of Expenditures of Federal Awards	6
Notes to Schedule of Expenditures of Federal Awards	7
Schedule of Findings and Questioned Costs	8 - 16
Summary Schedule of Prior Audit Findings	17

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 Members of City Council
City of Hesperia, California

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 Hesperia as of and for the year ended June 30, 2012, which collectively comprise City of Hesperia's basic financial statements and have issued our report thereon dated January 29, 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 City of Hesperia is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the City of Hesperia'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 Hesperia's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the City of Hesperia'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 certain deficiencies in internal control over financial reporting 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 the accompanying "Schedule of Findings and Questioned Costs" to be material weaknesses (Finding # 2012-04 through 2012-12).

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City of Hesperia'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*.

The City of Hesperia'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 Hesperia's responses and, accordingly, we express no opinion on them.

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

White Nelson Nick Evans LLP

March 26, 2013
Carlsbad, California

INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH
REQUIREMENTS THAT COULD HAVE A DIRECT AND MATERIAL
EFFECT ON EACH MAJOR PROGRAM AND ON INTERNAL CONTROL
OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133 AND
ON THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

To the Members of the City Council
City of Hesperia, California

Compliance

We have audited City of Hesperia's compliance 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 of Hesperia's major federal programs for the year ended June 30, 2012. The City of Hesperia'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 Hesperia's management. Our responsibility is to express an opinion on the City of Hesperia'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 Hesperia'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 Hesperia's compliance with those requirements.

In our opinion the City of Hesperia complied, in all material respects, with the compliance 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 instances of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as items 2012-01, 2012-02, and 2012-03.

Internal Control Over Compliance

Management of the City of Hesperia 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 Hesperia's internal control over compliance with the requirements that could have a direct and material effect on a major federal program to determine the 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 Hesperia'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, or detected and corrected, on a timely basis.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies, or material weaknesses. We identified one deficiency in internal control over compliance that we consider to be a material weakness at Finding Number 2012-01.

The City of Hesperia'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 Hesperia'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, each major fund, and the aggregate remaining fund information of the City of Hesperia as of and for the year ended June 30, 2012, and have issued our report thereon dated January 29, 2013, which contained unqualified opinions on those financial statements. Our audit was conducted for the purpose of forming our opinions on the financial statements that collectively comprise the City of Hesperia's financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, 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.

The purpose of this report is solely to describe the scope of our testing of compliance with the types of compliance requirements applicable to each of the City of Hesperia's major programs and our testing of internal control over compliance and the results of our testing, and to provide an opinion on the City of Hesperia's compliance but not to provide an opinion on the effectiveness of the City of Hesperia's internal control over compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the City of Hesperia's compliance with requirements applicable to each major program and its internal control over compliance. Accordingly, this report is not suitable for any other purpose.

White Nelson Nick Evans LLP

March 26, 2013
Carlsbad, California

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
AND
SCHEDULE OF FINDINGS AND QUESTIONED COSTS**

CITY OF HESPERIA
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

June 30, 2012

Federal Grantor / Pass - Through Grantor / Program	Catalog of Federal Domestic Assistance Number	Program Identification Number	Federal Expenditures
<u>U.S. Department of Housing and Urban Development: *</u>			
Community Development Block Grant - Entitlement	14.218	B-11-MC-06-0578	\$ 525,184
Community Development Block Grant - Entitlement	14.218	B-10-MC-06-0578	<u>174,731</u>
Total U.S. Department of Housing and Urban Development			<u>699,915</u>
<u>U.S. Department of Justice:</u>			
Passed through County of San Bernardino:			
Edward Byrne Memorial Justice Assistance Grant Program	16.738	2011-DJ-BX-2642	<u>25,717</u>
<u>U.S. Department of Commerce: *</u>			
Investments for Public Works and Economic Development Facilities	11.300	07-01-06139	<u>1,484,884</u>
<u>U.S. Department of Transportation: *</u>			
Passed through California Department of Transportation:			
Highway Planning and Construction	20.205	06L2305452009	1,206,963
Highway Planning and Construction	20.205	06LY605452009	981,943
Highway Planning and Construction	20.205	065452010LY1030	1,402,079
Highway Planning and Construction	20.205	065452010Q64031	510,529
Highway Planning and Construction	20.205	065452010HY1030	<u>329,096</u>
Total U.S. Department of Transportation			<u>4,430,610</u>
<u>U.S. Department of Homeland Security:</u>			
Assistance to Firefighters Grant	97.044	EMW-2011-FO-0947	<u>23,960</u>
TOTAL EXPENDITURES OF FEDERAL AWARDS			<u><u>\$ 6,665,086</u></u>

* - Major Program

See 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* and Independent Auditors' Report on Compliance with Requirements That Could Have a Direct and Material Effect on Each Major Program and on Internal Control Over Compliance in Accordance with OMB Circular A-133 and on the Schedule of Expenditures of Federal Awards (pages 1 through 5) and Notes to Schedule of Expenditures of Federal Awards (page 7).

CITY OF HESPERIA
NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
June 30, 2012

1. GENERAL:

The accompanying Schedule of Expenditures of Federal Awards only presents the activity of federal award programs of the City of Hesperia (the "City"), and, therefore, does not present the financial position or results of operations of the City. The City's reporting entity is defined in Note 1 to the City's financial statements. All financial assistance received directly from federal agencies and federal financial assistance passed through other government agencies to the City is included in the accompanying schedule.

2. BASIS OF ACCOUNTING:

The activity of the City's federal award programs are recorded in special revenue funds of the City. The City utilizes the modified accrual basis of accounting for the special revenue fund types as described in Note 1 to the City's financial statements. Accordingly, the accompanying Schedule of Expenditures of Federal Awards is presented using the modified accrual basis of accounting.

See 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* and Independent Auditors' Report on Compliance with Requirements That Could Have a Direct and Material Effect on Each Major Program and on Internal Control Over Compliance in Accordance with OMB Circular A-133 and on the Schedule of Expenditures of Federal Awards (pages 1 through 5).

CITY OF HESPERIA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

For the year ended June 30, 2012

A. Summary of Audit Results:

1. The independent auditors' report expresses an unqualified opinion on the financial statements of the City of Hesperia.
2. There were nine material weaknesses (Finding Numbers 2012-04 through 2012-12) disclosed during the audit of the financial statements for the City of Hesperia.
3. There were no instances of noncompliance material to the financial statements of the City of Hesperia disclosed during the audit.
4. One material weakness in internal control over major federal award programs disclosed during the audit is reported in Finding Number 2012-01.
5. The independent auditors' report on compliance for each major federal award program for the City of Hesperia expresses an unqualified opinion.
6. Audit findings that are required to be reported in accordance with Section 510(a) of OMB Circular A-133 are reported in this Schedule. See Finding Numbers 2012-01 through 2012-03.
7. The programs tested as major programs include:
 - U.S. Department of Housing and Urban Development – Community Development Block Grant – Entitlement (B-11-MC-06-0578) and Community Development Block Grant – Entitlement (B-10-MC-06-0578) – CFDA #14.218
 - U.S. Department of Commerce – Investments for Public Works and Economic Development Facilities – (07-01-06139) – CFDA 11.300
 - U.S. Department of Transportation – Highway Planning and Construction – (06L2305452009), (06LY605452009), (065452010LY1030), (065452010Q64031), (065452010HY1030) – CFDA 20.205
8. The threshold for distinguishing types A and B programs was \$300,000.
9. The City of Hesperia was determined to be a high-risk auditee.

See 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* and Independent Auditors' Report on Compliance with Requirements That Could Have a Direct and Material Effect on Each Major Program and on Internal Control Over Compliance in Accordance with OMB Circular A-133 and on the Schedule of Expenditures of Federal Awards (pages 1 through 5).

CITY OF HESPERIA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS
(CONTINUED)

For the year ended June 30, 2012

FINDINGS AND QUESTIONED COSTS - MAJOR PROGRAM

Finding Number 2012-01– Material Weakness in Internal Control

Program: U.S. Department of Commerce – Investments for Public Works & Economic Development Facilities (07-01-06139) – CFDA #11.300

U.S. Department of Transportation – Highway Planning and Construction (06L2305452009, 06LY605452009, 065452010LY1030, 065452010Q64031, 065452010HY1030) – CFDA #20.205

Statement of Condition: During our reconciliation of expenditures funded by federal grants reported in the Schedule of Expenditures of Federal Awards (SEFA) to grant agreements and the general ledger, we noted expenditures included in the SEFA that were reported incorrectly as federal expenditures in the current year. The expenditures reported were for prior year expenditures that were not included in the prior year OMB Circular A-133 audit.

Criteria: Section 310(b) OMB Circular A-133 states the Schedule of Expenditures of Federal Awards “shall provide total Federal awards expended for each individual Federal program”.

Effect: The City could be penalized for its noncompliance with program compliance requirements.

Questioned Costs: None Noted.

Recommendation: We recommend that the City review its procedures for gathering information related to grants to ensure that amounts reported in the SEFA are complete and reported in the proper year.

Management Response: The two grant funded projects, Industrial Park Lead Track and the Rancho Undercrossing, had expenditures in prior fiscal years which were included on the trial balance reports provided to the auditors but not included on a schedule in the format desired by the auditors used to create the Schedule of Expenditures of Federal Award (SEFA) for those years in the Single Audit report. As such, the auditors did not examine those expenditures, in the context of the Single Audit during the year the expenditures were incurred. Going forward, management will improve the reporting of federal grant expenditures on the SEFA by ensuring that such expenditures are included on the SEFA for the year the expenditures were incurred.

See 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* and Independent Auditors’ Report on Compliance with Requirements That Could Have a Direct and Material Effect on Each Major Program and on Internal Control Over Compliance in Accordance with OMB Circular A-133 and on the Schedule of Expenditures of Federal Awards (pages 1 through 5).

CITY OF HESPERIA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS
(CONTINUED)

For the year ended June 30, 2012

FINDINGS AND QUESTIONED COSTS - MAJOR PROGRAM (CONTINUED):

Finding Number 2012-02 – Reporting

Program: U.S. Department of Housing and Urban Development – Community Development Block Grant – Entitlement (B-11-MC-06-0578) – CFDA #14.218

Statement of Condition: The results of our test work indicated that the City did not file the Federal Cash Transactions Reports (SF-425) by the required deadline.

Criteria: The applicable federal code (24 CFR 84.52) states, “HUD requires recipients to submit the Federal Financial Reports no later than 30 days after the end of each specified reporting period for quarterly and semi-annual reports, and 90 calendar days after the project of the grant period end date”.

Effect: The City may be penalized or fined for its noncompliance with program compliance requirements.

Questioned Cost: None noted.

Recommendation: We recommend that the City establish procedures to ensure that the required reports are filed on a timely basis. The performance of these procedures should be documented to ensure compliance.

Management Response: The Community Development Block Grant (CDBG) requires quarterly financial reporting (SF-425) to the U.S. Department of Housing and Urban Development (HUD). During the FY 2010-11 audit, management was made aware that the SF-425 reports were not submitted. Management was made aware of this finding after the FY 2011-12 first quarter SF-425 report was due and thus this became a finding for FY 2011-12. Management corrected this finding in FY 2011-12 and has maintained compliance for all quarterly SF-425 repost filings since.

See 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* and Independent Auditors’ Report on Compliance with Requirements That Could Have a Direct and Material Effect on Each Major Program and on Internal Control Over Compliance in Accordance with OMB Circular A-133 and on the Schedule of Expenditures of Federal Awards (pages 1 through 5).

CITY OF HESPERIA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS
(CONTINUED)

For the year ended June 30, 2012

FINDINGS AND QUESTIONED COSTS - MAJOR PROGRAM (CONTINUED):

Finding Number 2012-03 – Reporting

Program: U.S. Department of Housing and Urban Development – Community Development Block Grant – Entitlement (B-11-MC-06-0578) – CFDA #14.218

Statement of Condition: The results of our test work indicated that the City did not file the Section 3 Annual Summary Report (Form HUD-60002) within the required deadline.

Criteria: The applicable federal code (24 CFR 135.90) states, “Where the program providing the section 3 covered assistance requires submission of an annual performance report, the section 3 report will be submitted with that annual performance report.” Grantees must submit their annual performance report within 90 days after the end of a grantee’s program year as required by HUD as part of their year-end reporting.

Effect: The City may be penalized or fined for its noncompliance with program compliance requirements.

Questioned Cost: None noted.

Recommendation: We recommend that the City establish procedures to ensure that the required reports are filed on a timely basis. The performance of these procedures should be documented to ensure compliance.

Management Response: The Community Development Block Grant (CDBG) requires annual filing of the Consolidated Annual Performance and Evaluation Report (CAPER) and the electronic PR03 report within 90 days after the end of the program year or June 30, 2012. The paper copy of the CAPER was stamped ‘Received September 28, 2012’ by CDBG’s office in Los Angeles which was the 90th day after June 30, 2012. However, the electronically filed PR03 report was filed October 1, 2012. Management will implement procedures to ensure that the PR03 report is filed along with the CAPER for future timely filings.

See 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* and Independent Auditors’ Report on Compliance with Requirements That Could Have a Direct and Material Effect on Each Major Program and on Internal Control Over Compliance in Accordance with OMB Circular A-133 and on the Schedule of Expenditures of Federal Awards (pages 1 through 5).

CITY OF HESPERIA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS
(CONTINUED)

For the year ended June 30, 2012

FINDINGS - FINANCIAL STATEMENT AUDIT

MATERIAL WEAKNESSES

Finding Number 2012-04: Satellite Cash Receipts

Condition: During our audit it was noted that the cash receipts received at the police department that are given to the City are not reconciled to the police department receipt log. There is also no reconciliation between cash received and receipts issued for customer payments and services provided at the Animal Control division. Also, there is no evidence of approval of write-offs of Fire District accounts receivables and the accounting software (QuickBooks) at Animal Control and Code Compliance Divisions allows the user to delete or skip receipt numbers.

Recommendation: We recommend that cash receipts in all departments be reconciled to their respective receipt log sub ledger for services, money received and the services provided. To help mitigate receipts from being skipped or deleted a receipt log should be kept that can be reconciled to the QuickBooks software.

Management Response: Management is working to extend the use of the City's financial system receivables module, by adding terminals and additional software licenses to the various satellite offices.

Finding Number 2012-05: Water Overdraft

Condition: During our audit it was noted that accounts payable did not include an amount payable for the water overdraft in the basin.

Recommendation: We recommend that accounts payable be reviewed by management for all possible liabilities at year end.

Management Response: Annually, the City (Water District) buys/leases make-up water from other agencies/owners of unused free production allowance to meet the needs of the District's customers. The Water Year is from October 1 to September 30 whereas the City's fiscal year begins July 1 to June 30; meaning, $\frac{3}{4}$ of the Water Year is overlapped by the fiscal year. Furthermore, the Watermaster will determine the District's actual make-up obligation in February or March following the close of the previous Water Year. Expenditures related to the makeup obligations are made after the close of the audited fiscal year.

Management must calculate the District's estimated make-up obligation and accrue $\frac{3}{4}$ of the obligation to the fiscal year being audited. The City will examine future water lease obligations for accrual.

See 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* and Independent Auditors' Report on Compliance with Requirements That Could Have a Direct and Material Effect on Each Major Program and on Internal Control Over Compliance in Accordance with OMB Circular A-133 and on the Schedule of Expenditures of Federal Awards (pages 1 through 5).

CITY OF HESPERIA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS
(CONTINUED)

For the year ended June 30, 2012

FINDINGS - FINANCIAL STATEMENT AUDIT (CONTINUED)

MATERIAL WEAKNESSES (CONTINUED)

Finding Number 2012-06: Adjustments to Fund Balance

Condition: During our audit it was noted that there were multiple instances where entries were directly coded to fund balance.

Recommendation: We recommend management reconcile fund balance at year end to ensure that no current year activity is posted to fund balance.

Management Response: Management normally does not adjust the fund balance account of a fund in the City's financial system. However, the required closing journal entries necessitated posting entries to fund balance accounts to correct prior mispostings. No other alternatives were available to make the corrections.

Finding Number 2012-07: Retentions Payable

Condition: During our audit it was noted that amounts were included in retentions payable that had previously been paid to the contractors.

Recommendation: We recommend the City verify the nature of retention accounts with the bank prior to booking a liability.

Management Response: Management records retention liabilities owed to contractors in the City's financial system. In this particular case, the contractor secured a letter of credit with a bank to serve as the contract retention. Management will review all future retention requirements of each project to evaluate if a liability should be recorded on the City's financial system.

Finding Number 2012-08: Disposal of Fixed Assets

Condition: During our audit it was noted that the City did not remove from its fixed asset records and the general ledger existing pipe that was subsequently replaced with new pipe as part of the City's pipeline replacement project.

Recommendation: We recommend the Accounting Department meet with the Engineering Department on a yearly basis to reconcile fixed asset additions and deletions.

See 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* and Independent Auditors' Report on Compliance with Requirements That Could Have a Direct and Material Effect on Each Major Program and on Internal Control Over Compliance in Accordance with OMB Circular A-133 and on the Schedule of Expenditures of Federal Awards (pages 1 through 5).

CITY OF HESPERIA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS
(CONTINUED)

For the year ended June 30, 2012

FINDINGS - FINANCIAL STATEMENT AUDIT (CONTINUED)

MATERIAL WEAKNESSES (CONTINUED)

Finding Number 2012-08: Disposal of Fixed Assets (CONTINUED)

Management Response: When fixed assets, valued at \$5,000 or more, are purchased or disposed, management records the activity in its fixed asset inventory. Since FY 2001-02 the City has been engaged in a water pipeline replacement program replacing old steel pipe with larger non-steel pipe, which presented a challenge in estimating the appropriate dollar value of assets to be removed. Older pipeline inventory records lack sufficient detail of specific location of the old steel pipe. As the pipeline replacement program has completed the replacement of approximately half of the old steel pipe, management has established a format to dispose of these assets over the remaining estimated 10-year replacement period.

Finding Number 2012-09: Land Held for Resale

Condition: During our audit it was noted that the City did not adjust its accounting records for the parcels of land held for resale that were either given to the Successor Agency or were used on the Rancho Interchange.

Recommendation: We recommend the City adjust its accounting records for transfers of assets.

Management Response: Management's response to this finding is twofold. ABx1 26 required the dissolution of the Hesperia Community Redevelopment Agency (HCRA) on February 1, 2012. At that time, the assets of the former HCRA were transferred to the Successor Agency of the HCRA, of which, included land holdings. The accounting records for the land transfer should have been adjusted to reflect market value versus the value of the former HCRA.

The second part of this finding is the result of the Rancho Interchange project requiring a portion of a City-owned parcel. The City entered into an agreement with SANBAG during the last quarter of Fiscal Year 2011-12 for the construction of the project. Although still owned by the City and prior to the commencement of construction, the City's auditor directed management to adjust the fixed asset inventory to reduce the carrying value of the parcel for the portion to be used for the project in FY 2012-13.

See 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* and Independent Auditors' Report on Compliance with Requirements That Could Have a Direct and Material Effect on Each Major Program and on Internal Control Over Compliance in Accordance with OMB Circular A-133 and on the Schedule of Expenditures of Federal Awards (pages 1 through 5).

CITY OF HESPERIA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS
(CONTINUED)

For the year ended June 30, 2012

FINDINGS - FINANCIAL STATEMENT AUDIT (CONTINUED)

MATERIAL WEAKNESSES (CONTINUED)

Finding Number 2012-10: Note Receivable

Condition: During our audit it was noted that the City did not record a note receivable from the Hesperia Recreation and Park District to the City for the Park District's share of the construction costs of the Civic Plaza Park.

Recommendation: We recommend the City record receivables for such cost sharing arrangements at the time the receivable arises.

Management Response: In 2008 the City and Park District constructed the Civic Plaza Park and informally agreed to split the costs equally. The Park District made some payments but eventually stopped. The City and Park District entered into a written agreement in 2011, whereby the Park District would remit annual payments to the City over a 10 year period. Due to the Park District's inconsistent repayment history, it was determined that the receivable was not reliable for inclusion on the FY 2010-11 financial statements. During FY 2011-12 the park district made its first and only scheduled payment prompting this finding. The Park District has since failed to remit payment to the City causing management to continue to question the collectability of the note.

Finding Number 2012-11: Matching Revenues and Expenditures for Grants

Condition: During our audit it was noted that there were multiple instances where the City is not accruing for expenses incurred and recognizing revenue earned relating the Industrial Lead Rail Track Project and the Rancho Road Undercrossing Project.

Recommendation: We recommend the City implement a process in which the responsible departments communicate on a regular basis in order to accrue the federal expenditures and revenues on a timely basis

Management Response: Management concurs with the auditor recommendation and will improve coordination among the various departments working with grants. Regarding the Rancho Road Undercrossing Project city staff encountered difficulty dealing with changing requirements by CalTrans which has caused management to modify schedules previously given to the City's auditor.

See 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* and Independent Auditors' Report on Compliance with Requirements That Could Have a Direct and Material Effect on Each Major Program and on Internal Control Over Compliance in Accordance with OMB Circular A-133 and on the Schedule of Expenditures of Federal Awards (pages 1 through 5).

CITY OF HESPERIA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS
(CONTINUED)

For the year ended June 30, 2012

FINDINGS - FINANCIAL STATEMENT AUDIT (CONTINUED)

MATERIAL WEAKNESSES (CONTINUED)

Finding Number 2012-12: Schedule of Expenditures of Federal Awards (SEFA)

Condition: As previously noted in Finding Number 2012-01, during our reconciliation of expenditures funded by federal grants reported in the SEFA (prepared by the City) to grant agreements and the general ledger, we noted expenditures for multiple grant programs included in the SEFA that were reported incorrectly as federal expenditures in the current year. The expenditures reported were for prior year expenditures that were not included in the prior year OMB Circular A-133 audit.

Recommendation: We recommend the City review its procedures for gathering information related to grants to ensure that amounts reported in the SEFA are complete and reported in the correct year.

Management Response: Management agrees with the finding that expenditures were inadvertently not included on prior SEFAs thus not allowing the City's auditor the opportunity to review those expenditures in the context of the Single Audit, in the year incurred. This finding is the same as #2012-01, but as #2012-01 pertains to the major program, #2012-12 pertains to the financial statement audit.

See 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* and Independent Auditors' Report on Compliance with Requirements That Could Have a Direct and Material Effect on Each Major Program and on Internal Control Over Compliance in Accordance with OMB Circular A-133 and on the Schedule of Expenditures of Federal Awards (pages 1 through 5).

CITY OF HESPERIA

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS

AND QUESTIONED COSTS

For the Year ended June 30, 2012

Finding Number 2011-01 – City did not file the Consolidated Annual Performance and Evaluation Report (CAPER) by the required deadline.

This finding has been corrected.

Finding Number 2011-02 – City did not file the Federal Cash Transactions Reports (SF-425) for all quarters during the fiscal year.

This finding has been corrected.

Finding Number 2011-03 – City did not verify that entities were not suspended or debarred or otherwise excluded prior to entering into a covered transaction.

This finding has been corrected.

See 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* and Independent Auditors' Report on Compliance with Requirements That Could Have a Direct and Material Effect on Each Major Program and on Internal Control Over Compliance in Accordance with OMB Circular A-133 and on the Schedule of Expenditures of Federal Awards (pages 1 through 5).