
**CITY OF NOVATO
SINGLE AUDIT AND RELATED REPORTS
FOR THE YEAR ENDED
JUNE 30, 2019**

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**CITY OF NOVATO
SINGLE AUDIT AND RELATED REPORTS
FOR THE YEAR ENDED JUNE 30, 2019**

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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

To the City Council
City of Novato, California

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Novato, California, as of and for the year ended June 30, 2019, and the related notes to the financial statements, which collectively comprise the City of Novato's basic financial statements, and have issued our report thereon dated February 1, 2021.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the City of Novato'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 of Novato's internal control. Accordingly, we do not express an opinion on the effectiveness of the City of Novato'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 have not been identified. However, as described in the accompanying schedule of findings and questioned costs, we did identify certain deficiencies in internal control that we consider to be material weaknesses and 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 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 as items 2019-001 through 2019-003 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 deficiencies described in the accompany schedule of findings and questioned costs as items to be significant deficiencies: 2019-004 through 2019-005.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City of Novato'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 instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying schedule of findings and questioned costs as items 2019-006 through 2019-008.

City of Novato's Response to Findings

City of Novato's responses to the findings identified in our audit is described in the accompanying schedule of findings and questioned costs. City of Novato'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 entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Sacramento, California
February 1, 2021



INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE FOR EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY THE UNIFORM GUIDANCE

To the City Council
City of Novato, California

Report on Compliance for Each Major Federal Program

We have audited the City of Novato's compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on each of the City of Novato's major federal programs for the year ended June 30, 2019. City of Novato's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with federal statutes, regulations, and the terms and conditions of its federal awards applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the City of Novato's major federal programs based on our audit of the types of compliance requirements referred to above. 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 the audit requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Those standards and the Uniform Guidance 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 Novato'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 on compliance for each major federal program. However, our audit does not provide a legal determination of the City of Novato's compliance.

Opinion on Each Major Federal Program

In our opinion, the City of Novato, complied, in all material respects, with the types of 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, 2019.

Other Matters

The results of our auditing procedures disclosed instances of noncompliance which are required to be reported in accordance with the Uniform Guidance and which are described in the accompanying schedule of findings and questioned costs as items 2019-007 through 2019-008. Our opinion on each major federal program is not modified with respect to this matter.

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

Report on Internal Control over Compliance

Management of the City of Novato is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the City of Novato's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, 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 Novato'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. *A significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

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 material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Report on Schedule of Expenditures of Federal Awards Required by the Uniform Guidance

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of City of Novato, as of and for the year ended June 30, 2019, and the related notes to the financial statements, which collectively comprise City of Novato's basic financial statements. We issued our report thereon dated February 1, 2021, which contained unmodified opinions on those financial statements. Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the basic financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by the Uniform Guidance and is not a required part of the basic 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 basic 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 basic financial statements or to the basic 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 basic financial statements as a whole.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.



Sacramento, California
February 1, 2021

**CITY OF NOVATO
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2019**

| <u>Federal Grantor/Pass-Through Grantor Program</u> | <u>Federal CFDA Number</u> | <u>Pass-Through Entity Identifying Number/ Grant Number</u> | <u>Federal Expenditures</u> |
|--|------------------------------------|---|---------------------------------|
| U.S Department of Justice | | | |
| Direct Awards: | | | |
| Bulletproof Vest Partnership Program | 16.607 | BA-3A00S-SM01 | \$ 8,656 |
| Edward Byrne Memorial Justice Assistance Grant Program | 16.738 | JAG 653-13 | <u>137,094</u> |
| Total U.S. Department of Justice | | | <u>145,750</u> |
| U.S Department of Transportation | | | |
| Passed-Through State of California Department of Transportation: | | | |
| Highway Planning and Construction | 20.205 | BHLS-5361(023) | 116,759 |
| Highway Planning and Construction | 20.205 | STPL-5361(027) | 556,545 |
| Highway Planning and Construction | 20.205 | STPL-5361(028) | <u>1,324</u> |
| Total Highway Planning and Construction | | | <u>674,628</u> |
| State and Community Highway Safety | 20.600 | PT19077 | 44,901 |
| Minimum Penalties for Repeat Offenders for Driving While Intoxicated | 20.608 | - | <u>18,400</u> |
| Total U.S. Department of Transportation | | | <u>737,929</u> |
| U.S Department of Homeland Security | | | |
| Direct Awards: | | | |
| Homeland Security Grant Program | 97.067 | - | <u>45,916</u> |
| Total U.S. Department of Homeland Security | | | <u>45,916</u> |
| Total Expenditures of Federal Awards | | | \$ <u>929,595</u> |

CITY OF NOVATO
NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2019

NOTE 1: REPORTING ENTITY

The accompanying Schedule of Expenditures of Federal Awards presents the activity of all federal financial assistance programs of the City of Novato. The City of Novato reporting entity is defined in Note 1 of the City's Comprehensive Annual Financial Report. All federal awards received directly from federal agencies as well as federal awards passed through other government agencies are included on the schedule. When federal awards were received from a pass-through entity, the Schedule of Expenditures of Federal Awards shows, if available, the identifying number assigned by the pass-through entity.

NOTE 2: BASIS OF ACCOUNTING

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of the City and is presented on accounting principles generally accepted in the United States of America. The information in this schedule is presented on the accrual basis of accounting and in accordance with requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance).

NOTE 3: RELATIONSHIP TO FINANCIAL STATEMENTS

The amounts reported in the accompanying Schedule of Expenditures of Federal Awards agree, in all material respects, to amounts reported within the City's basic financial statements. Federal award revenues are reported principally in the City's financial statements as intergovernmental revenues in the governmental funds.

NOTE 4: CLAIMS

The City of Novato has received federal grants for specific purposes that are subject to review and audit by the Federal Government pass-through entity. Although such audits could result in expenditure disallowance under grant terms, any required reimbursements are not expected to be material which have not already been recorded.

NOTE 5: INDIRECT COSTS

The City elected not to use the 10% de minimus indirect cost rate, and did not charge indirect costs to federal grants during the year ended June 30, 2019.

**CITY OF NOVATO
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2019**

SECTION I - SUMMARY OF AUDITOR'S RESULTS

Financial Statements

| | |
|---|------------|
| Type of auditor's report issued: | Unmodified |
| Internal control over financial reporting: | |
| Material weakness(es) identified? | Yes |
| Significant deficiency(ies) identified | Yes |
| Noncompliance material to financial statements noted? | No |

Federal Awards

| | |
|--|---------------|
| Internal control over major programs: | |
| Material weakness(es) identified? | No |
| Significant deficiency(ies) identified? | None reported |
| Type of auditor's report issued on compliance for major programs: | Unmodified |
| Any audit findings disclosed that are required to be reported in accordance with section 200.516 of the Uniform Guidance | No |
| Identification of Major Programs: Highway Planning and Construction, 20.205 | |
| Dollar threshold used to distinguish between type A and type B programs: | \$750,000 |
| Auditee qualified as low-risk auditee? | No |

CITY OF NOVATO
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (continued)
FOR THE YEAR ENDED JUNE 30, 2019

SECTION II - FINANCIAL STATEMENT FINDINGS

Findings relating to the financial statements which are required to be reported in accordance with Generally Accepted *Government Auditing Standards*.

Finding 2019-001: Financial Close (Material Weakness)

Criteria

An effective internal control system and timely financial reporting provides reasonable assurance for the safeguarding of assets, the reliability of financial information, and compliance with laws and regulation.

Condition

During the performance of the audit, processes utilized for closing and financial reporting of financial activity for the fiscal year were not effective, which contributed to the delayed accounting close of the City's trial balances and unpreparedness for the audit. The year-end audit for the June 30, 2019 fiscal year-end began in October 2019. Over the course of a year, the auditors received 8 versions of the trial balance to be audited. For each version received, it was audited as if it was the City's final representation of year-end figures. However, audit schedules and reconciliations received each time were either lacking or not prepared accurately resulting in numerous journal entries to be proposed to each version of the trial balance. The City's final trial balance was provided in August 2020. Approximately 30 journal entries were proposed and posted to the final trial balance for audit. Specific financial statement areas that required adjustment included:

- *Cash & investments* - See material weakness 2019-002.
- *Accounts receivable* - The City does not have a formal reconciliation process for accounts receivable. Several journal entries to correct receivables were proposed.
- *Capital assets* - The City provided the auditors various capital asset schedules as support for the balances recorded in the general ledger. However, none of them agreed and a proper reconciliation was not performed. In addition, per review of the asset listing we identified a disposed asset that was not a true deletion and capital asset additions that were not included.
- *Interfund receivables and payables* - There were no changes to balances from the prior year indicating that no reconciliation had been performed.
- *Accrued payroll, taxes, and benefits* - Upon performance of cash reconciliations, it was identified that payroll liabilities were getting double posted. See cash material weakness 2019-002.
- *Compensated absences* - The journal entry to true-up the compensated absences liability was not recorded and the reconciliation did not agree.
- *Net pension liability* - The initial entry to record the net pension liability did not take into account balances being held in fund 601 - Equipment Maintenance. Therefore, total balances were overstated.
- *Long-term debt* - Accreted interest on the City's capital appreciation bonds was not recorded. The City entered into a new loan agreement with PG&E that was not recorded.
- *Unearned revenue* - The City does not have procedures in place to reconcile unearned revenue. A majority of the unearned revenue is related to parks and recreation. There were errors in reconciling related revenue from the City's BlueRec system to the general ledger.
- *Deposits* - Deposits held by the City were not reconciled. See material weakness 2019-003.
- *Marin Valley Mobile Country Club (MVMCC) cash to accrual adjustments* - Accrual adjustments to record MVMCC's activity were not posted.
- *Revenues and expenses* - Various reclassification entries and mis-postings were identified.

CITY OF NOVATO
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (continued)
FOR THE YEAR ENDED JUNE 30, 2019

- *Property taxes* - Property tax revenue was unable to be reconciled to the confirmation received by \$171,901.

Cause

Due to personnel turnover and the implementation of a new accounting system in 2018, the City did not have adequate controls in place to ensure accounting records were closed timely and accurately. Further, the City lacked documentation of significant operational and accounting processes.

Effect

The financial statements as presented to the auditors contained material misstatements that required adjustments.

Recommendation

We recommend that the City institute a program to methodically identify and document its significant operational and accounting processes. Documenting a process involves identifying and gaining an understanding of the events or transactions that trigger performance of the process, the automated or manual procedures used in performing the process, the person(s) or position(s) responsible for performing the procedures, the source documents used or generated, the procedures for approval and review and correction of any errors detected, and the financial or operational entries or reports summarizing the result of the process.

We recommend the City develop checklists or other guidance documents over the City's closing process to ensure all closing entries are captured in the City's general ledger in a timely manner, and supporting schedules agree and reconcile to respective account balances prior to the trial balance being provided for the audit.

View of Responsible Officials

Management agrees that personnel turnover in "key" positions within the Finance Department over the past 36 months, have had a significant impact on the city's financial accounting processes and procedures. More specifically, key turnover in the Finance Manager and Accounting Supervisor positions countered succession planning efforts, resulting in delays in and incomplete implementation of the new accounting system (New World). These factors contributed to required adjustments that followed the presentation of financial statements to the auditors.

Management would like to acknowledge the implementation of the new accounting system was not supported nor did it include a redesign of previous accounting procedures and processes that would have integrated the old processes into the new system, thus allowing for a full use of the new system and effectively guide the year-end close.

The current City's administration recognized the need for immediate attention to this condition as it was preparing for the FY18/19 audit; as a result, the City hired several professional finance consultants and a professional accounting audit firm to assist with the year-end close process; preparation of the pre-requisite journal entries and development of standard operating financial policies and procedures to be implemented in order to expedite the delayed year-end close process. The City is currently developing new financial procedures, processes and documentation protocols to support the timely preparation of financial statements. The City has engaged a qualified audit firm that specializes in governmental accounting and financial reporting to assist with the project management and implementation of financial policies and procedures redesign. In addition, the city has hired new accounting staff that will be assisting in the development of the new financial policy and procedure redesign.

CITY OF NOVATO
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (continued)
FOR THE YEAR ENDED JUNE 30, 2019

Finding 2019-002: Cash and Investments (Material Weakness)

Criteria

Certain deficiencies in the internal control system over financial reporting could adversely affect an entity's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements.

Conditions

- There was a failure to accurately and timely perform bank reconciliations for the June 30, 2019 fiscal year.
- The June 30, 2019 final bank reconciliation had an unidentified difference of \$65,681.
- The adjustment to record investments at fair market value at year-end was not recorded properly. The fair market value of the investments per their statements did not agree to the general ledger.
- The City maintains a pooled cash fund which accounts for all of the funds' cash and investment balances. The pooled cash equity fund did not agree to the funds' cash balances indicating that journal entries related to cash were not properly being recorded. Further, we noted balances relating to interest were recorded in the pooled cash fund but should have been allocated to the various funds.
- The City had various funds with negative cash balances indicating that other funds' had paid for expenditures. The trail to determine the proper payment of those expenditures was lacking. Numerous transfers were made between funds without adequate support.

Cause

The overall process for cash and investment reconciliations was not being completed properly. Bank reconciliations were not being prepared or reviewed timely. Unfamiliarity with the financial accounting system lead to inconsistencies in how transactions were being recorded.

Effect

Untimely preparation and review of bank reconciliations increases the risk that errors could go undetected. Cash and investment balances as presented are not reflective of their true balances.

Recommendation

We recommend the City review their cash and investment reconciliation procedures to ensure timely and accurate completion. Cash and investment reconciliations review should include tests of mechanical accuracy and tracing of items on the reconciliation to relevant source documents.

View of Responsible Officials

Management agrees that personnel turnover in "key" positions within the Finance Department over the past 36 months, have had a significant impact on the city's financial accounting processes and procedures. These personnel changes were disruptive to regular and timely bank reconciliations and the accurate recording of accounting entries related to cash and investments.

The current City administration recognized this issue and the need for immediate attention to this condition as it was preparing for the FY18/19 audit and has hired finance consultants to assist with completing the backlog of bank reconciliations. Additionally, the Finance Department has initiated the redesign of the accounting, reporting and reconciliation procedures, which is scheduled to be completed by the end of FY20/21. The City has also hired new accounting staff that will be assisting in the development of the new financial policy and procedure redesign.

CITY OF NOVATO
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (continued)
FOR THE YEAR ENDED JUNE 30, 2019

Finding 2019-003: Deposits (Material Weakness)

Criteria

Certain deficiencies in the internal control system over financial reporting could adversely affect an entity's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements.

Condition

Deposits held in Trust (Fund 120) - Of the \$334,000 of deposits outstanding, approximately \$154,000 or 46% is comprised of items from 2009 and prior. We noted one item from 1996 totaling \$75,000 or 22% of the total deposit balance.

Restricted Revenue Fund (Fund 240) - Of the \$1.5 million of deposits outstanding, approximately \$825,000 or 54% is comprised of items from 2009 and prior. Of the \$825,000 aged items, \$471,000 or 57% is comprised of items from 1973-2000. Further, the City was not able to provide source documents supporting current year transactions recorded in the Restricted Revenue fund. Four transactions, totaling a reduction of deposits of \$277,000 were selected for testing and unable to be supported.

Cause

There is not proper oversight or management of deposits. No determination has been made as to whether old items are still subject to restrictions, nor has it been determined if the City is required to return the funds to the payer/developer.

For the restricted revenue fund, the transactions were recorded through journal entries by prior Finance staff. The journal entries were supported by internal spreadsheets for which there are no source documents.

Effect

Depending on the resolution of the deposits, the City's revenues could potentially be misstated. City funds may have been used to fund projects for which deposits were being held.

Recommendation

We recommend that the City perform a thorough review and reconciliation of these deposit accounts to determine if monies are owed to developers, or if these deposits were provided to the City as non-refundable contributions in which case the City should have recorded the amounts into revenue.

View of Responsible Officials

As indicated in the City's response to Finding 2019-001, the same personnel issues have impacted the Finance Department's ability to operate efficiently. The City agrees with the finding and the following actions are being implemented and expect to be resolved for fiscal year 2020:

- The City will prioritize the review of Deposits held in Trust starting with those deposits more than three years, and confirm whether there is a need for the deposits to be maintained.
- The City will evaluate the funds held in the Restricted Revenue Fund (Fund 240) and determine the appropriate disposition of these funds. The City will conduct regular analysis of accounts with no activity for the purpose of ensuring timely disposition of funds and subsequent closing of obsolete funds.

CITY OF NOVATO
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (continued)
FOR THE YEAR ENDED JUNE 30, 2019

Finding 2019-004: Grant Accounting (Significant Deficiency)

Criteria

Certain deficiencies in the internal control system over financial reporting could adversely affect an entity's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements.

Condition

The City's grant revenues, expenditures, receivables, and unearned revenue are not being properly reconciled for financial reporting purposes at year-end.

Cause

It appears there is not enough formalized communication between the various departments who manage grants and the Finance Department who is responsible for financial reporting at year-end. A formal reconciliation of grants was not being performed.

Effect

There were numerous errors identified to properly match grant revenues, expenditures, unearned revenue, and receivables within a fiscal year.

Recommendation

We recommend the City implement a grants administration policy. With assistance from department heads/grant managers, summarized grant information and program information should be provided to the Finance Department such as:

- Copies of grant agreements and budgets
- Copies of material expenditures with proper approvals of coding and application
- Copies of reimbursement requests submitted
- Monitoring of grant cash flow

The Finance Department should then be able to prepare a reconciliation of grant revenues, expenditures, unearned revenue, cash received, and receivables for fiscal year-end.

View of Responsible Officials

Management agrees that personnel turnover in "key" positions within the Finance Department over the past 36 months, have had a significant impact on the city's financial accounting processes and procedures. In addition, another impact resulted from the changeover in accounting systems described in our response to Finding 2019-001. That is, with the turnover of personnel, it became even more difficult to implement accounting processes and procedures to adequately account for all aspects of the various grant programs maintained by the City. As these programs often involve complex terms and regulations, the Finance Department was not staffed or trained to fully integrate these requirements into the General Ledger accounting and reporting.

As a result, the tasks of accounting for grants and reporting to the Grantor agencies became decentralized. The principal burden of this activity was left primarily to the Departments of Public Works, Community Development and Police and the various Program Managers of those grants. To be clear, the accounting and reporting has continued to be done at the Department level but the incorporation of that data was not fully recognized in the City-wide accounting system on a consistent and timely basis.

The current City administration recognizes this issue and has hired consultants to assist with developing a comprehensive system that links the base accounting and reporting at the Department level and integrating it with the City's accounting system. The goal is to provide not only comprehensive accounting and reporting by grant, but also more readily support the work of the Department management of grants by providing accurate and timely accounting of all grant activity.

CITY OF NOVATO
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (continued)
FOR THE YEAR ENDED JUNE 30, 2019

Finding 2019-005: Financial Reporting and Journal Entries (Significant Deficiency)

Criteria

Certain deficiencies in the internal control system over financial reporting could adversely affect an entity's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements.

Condition

During our test of controls over journal entries, we noted 4 out of 37 had no evidence of the preparer; 7 journal entries had no evidence of review and approval; and 2 did not have adequate supporting documentation.

Quarterly financial reports were not being presented to Council on a consistent basis. The only reports being presented were investment reports.

Cause

Due to personnel turnover, the City did not have adequate controls in place to ensure journal entries were being properly posted and supported.

Due to lack of proper procedures and controls, financial reports were not able to be produced.

Effect

Risks exist that incorrect and unsupported journal entries could be posted.

City Council is not being informed of the financial status of the City in order to make informed decisions.

Recommendation

We recommend that controls be put into place for the preparation, approval, and posting of journal entries.

In order to provide improved financial oversight to the City, we recommend that financial reports including detailed financial statement information be presented on a consistent basis to the City Council, at a minimum on a quarterly basis.

View of Responsible Officials

The City concurs with the finding and agree with the recommendation. The Finance Department will comply with the City ordinances, policies and regulations and present timely and detailed reports to the City Council for oversight and transparency. The City Manager will ensure the compliance of all laws and ordinances applicable to City's governance.

The City will implement controls to ensure accuracy and completeness of journal entries. The City will follow its written policy regarding the creation and review of journal entries. The Finance Director has already started and will continue to ensure that journal entries are being properly performed to include detailed and proper documentation, accuracy and approval.

CITY OF NOVATO
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (continued)
FOR THE YEAR ENDED JUNE 30, 2019

Finding 2019-006: SB 341 Successor Agency Compliance (Compliance)

Criteria

Senate Bill (SB 341) requires that all successor entities, starting with fiscal year ended June 30, 2014, comply with annual report requirements within six months after the end of each fiscal year. The annual report must be posted to the City's website and contain all of the required items as described in the Health and Safety Code Section 34176.1 beginning with subsection (f).

Condition

The City did not post the required annual report for the fiscal year ended June 30, 2019 by the deadline of December 31, 2019.

Cause

There were various accounting issues such as accounting schedules not properly reconciling to the general ledger which caused delays in the completion of the 2019 annual audit.

Effect

The posting of the annual financial report is past its due date.

Recommendation

As noted in recommendation 2019-001, we recommend the City strive to close the year-end with properly prepared reconciliations within 3 - 4 months after year-end in order to complete the annual financial audit timely.

View of Responsible Officials

The City's Finance Department will implement regular reconciliations of accounts and develop year-end closing process with an appropriate delegation of duties and clearly defined oversight. The City has hired new accounting staff, and along with our consultants, will train staff on reconciliations of accounts and year end closing process. The City will implement procedures to ensure general ledger account balances are reconciled accurately and timely. The Finance Department will utilize a monthly year end closing list.

CITY OF NOVATO
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (continued)
FOR THE YEAR ENDED JUNE 30, 2019

SECTION III - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

Findings and questioned costs for Federal Awards, which includes audit findings defined in section 200.516 of the Uniform Guidance.

Finding 2019-007: Federal Grants Procedures Manual (Uniform Guidance Compliance)

Criteria

On May 17, 2017, the Office of Management and Budget (OMB) issued an addendum to Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards (Uniform Guidance)* allowing nonfederal entities an additional year to implement the Uniform Guidance procurement requirements and the entity must document the decision to utilize the extension.

Condition

The City has not updated the Federal Grant Procedures manual for compliance with the Uniform Guidance as required for the fiscal year.

Cause

City management was not aware of the Uniform Guidance requirements and implementation dates.

Effect

The City's procurement policies and procedures are not in compliance with the Uniform Guidance.

Recommendation

We recommend the City review the Uniform Guidance procurement requirements and update the Federal Grant Procedures manual for compliance with the Uniform Guidance.

View of Responsible Officials

The City will implement procedures to ensure that the City's Federal Grant Procedures manual will be updated to comply with OMB's Uniform Guidance procurement requirements and will document the decision to utilize the extension.

CITY OF NOVATO
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (continued)
FOR THE YEAR ENDED JUNE 30, 2019

Finding 2019-008: Financial Reporting Timeliness (Uniform Guidance Compliance)

Criteria

In accordance with CFR section 200.512 of the Uniform Guidance, the audit must be completed and the data collection form and reporting package must be submitted to the Federal Audit Clearinghouse within the earlier of 30 calendar days after receipt of the auditor's report(s), or nine months after the end of the audit period. In accordance with OMB Memo M-20-26, and due to the coronavirus pandemic, an extension of six months beyond the normal due date was granted for submission of the audit, data collection form, and reporting package.

Condition

The 2019 Single Audit reporting package and data collection form have not been submitted to the Federal Audit Clearinghouse by the original deadline of March 31, 2020, nor the extended deadline of December 31, 2020.

Cause

There were various accounting issues such as accounting schedules not properly reconciling to the general ledger which caused delays in the completion of the 2019 annual audit.

Effect

The filing of the Single Audit Reporting package and data collection form is past the due date.

Recommendation

As noted in recommendation 2019-001, we recommend the City strive to close the year-end with properly prepared reconciliations within 3 - 4 months after year-end in order to complete the annual financial audit timely.

View of Responsible Officials

The City acknowledges that the reporting package and data collection for the year ended June 30, 2019 was not submitted to the Federal Audit Clearinghouse by the due date. Completion of the audit was delayed due to staffing issues in the Finance Department. Steps have been initiated or are planned to address the identified issues to ensure that such delays will not be recurring.

**CITY OF NOVATO
SCHEDULE OF PRIOR YEAR FINDINGS
JUNE 30, 2019**

Finding 2018-001: Financial Close (Material Weakness)

Condition

During the performance of the audit, we noted that processes utilized for closing and financial reporting of financial activity for the fiscal year were not effective, which contributed to the delayed accounting close of the City's trial balances and unpreparedness for the audit. Approximately 20 journal entries were proposed and posted subsequent to providing the trial balance for audit. Auditors had to perform additional procedures over testing of account balances after receiving additional journal entries. Specific financial statement areas that required adjustment included:

- *Cash & investments* - See significant deficiency 2018-002.
- *Accounts receivable* - Through our testing of subsequent cash receipts, four out of thirty-four items totaling \$554,281 should have been accrued into accounts receivable. In addition, the City does not perform a reconciliation of accounts receivable. As the City records receipts on a cash basis during the year, accounts receivable is adjusted to accrual at year-end. The adjustment provided to the auditors did not agree to the general ledger. An unidentified difference of \$118,609 existed. In addition, various reclassifying and adjusting journal entries were provided to the auditors subsequent to the trial balance being provided for audit.
- *Capital assets* - The City provided the auditors three different capital asset schedules as support for the balances recorded in the general ledger. However, none of them agreed and a reconciliation was not performed. In addition, per review of the asset listing we identified a disposed asset that was incorrectly included on the listing. We also noted an error in the calculation of beginning accumulated depreciation.
- *Accounts payable* - Subsequent to receiving the trial balance for audit, the City identified three additional accruals that needed to be recorded to the general ledger.
- *Compensated absences* - The journal entry to true-up the compensated absences liability was not recorded.
- *Long-term debt* - Accreted interest on the City's capital appreciation bonds was not recorded.
- *Fund balance* - Three of the City's funds' beginning fund balance did not agree to the prior year audited financial statements.

Recommendation

We recommend the City develop checklists or other guidance documents over the City's closing process to ensure all closing entries are captured in the City's general ledger in a timely manner, and supporting schedules agree and reconcile to respective account balances prior to the trial balance being provided for the audit.

Status

Not implemented. See 2019-001.

CITY OF NOVATO
SCHEDULE OF PRIOR YEAR FINDINGS (continued)
JUNE 30, 2019

Finding 2018-002: Cash and Investments (Significant Deficiency)

Conditions

- Bank reconciliations did not have evidence of review by the Finance Director.
- Through our testing of the June 30, 2018 bank reconciliations, we identified two transactions that had cleared the bank as of June 30, 2018 but were not recorded as such. The items were included in the bank reconciliation as outstanding items and not posted to the general ledger.
- The adjustment to record investments at fair market value at year-end was not recorded properly. The fair market value of the investments per their statements did not agree to the general ledger.
- The City maintains a pooled cash fund which accounts for all of the funds' cash and investment balances. We noted balances relating to interest were also recorded in the pooled cash fund but should have been allocated out to the individual funds.

Recommendation

We recommend the City review their cash and investment reconciliation procedures to ensure timely and accurate completion. Cash and investment reconciliations review should include tests of mechanical accuracy and tracing of items on the reconciliation to relevant source documents.

Status

Not implemented. See 2019-002 - downgraded to material weakness.

Finding 2018-003: Deposits (Significant Deficiency)

Condition

Deposits held in Trust (Fund 120) - Of the \$256,000 of deposits outstanding, approximately \$140,000 or 54% is comprised of items from 2008 and prior. We noted one item from 1996 totaling \$75,000 or 29% of the total deposit balance.

Restricted Revenue Fund (Fund 240) - Of the \$1.8 million of deposits outstanding, approximately \$760,000 or 39% is comprised of items from 2008 and prior. Of the \$760,000 aged items, \$468,000 or 24% is comprised of items from 1973-1999.

Recommendation

We recommend that the City perform a thorough review and reconciliation of these deposit accounts to determine if monies are owed to developers, or if these deposits were provided to the City as non-refundable contributions in which case they City should have recorded the amounts into revenue.

Status

Not implemented. See 2019-003 - downgraded to material weakness.

CITY OF NOVATO
SCHEDULE OF PRIOR YEAR FINDINGS (continued)
JUNE 30, 2019

Finding 2018-004: SB 341 Successor Agency Compliance (Compliance)

Condition

The City did not post the required annual report for the fiscal year ended June 30, 2018 by the deadline of December 31, 2018.

Recommendation

As noted in recommendations 2018-001, we recommend the City strive to close the year-end with properly prepared reconciliations within 3 - 4 months after year-end in order to complete the annual financial audit timely.

Status

Not implemented. See 2019-006.