



**Date:** October 29, 2015

**TO:** LOCSD Board of Directors

**FROM:** Kathy A. Kivley, General Manager

**SUBJECT:** **Agenda Item 11G – Board Meeting Date: November 5, 2015**  
Audit Findings FY 2013/2014

**President**

R. Michael Wright

**Vice President**

Marshall E. Ochylski

**Directors**

Charles A. Cesena  
Jon-Erik E. Storm  
Louis G. Tornatzky

**General Manager**

Kathy A. Kivley

**District Accountant**

Michael L. Doyle

**Fire Chief**

Robert Lewin

**Battalion Chief**

Phill Veneris

**DESCRIPTION**

Attached are the District's Audit Findings for FY 2013/2014.

**SUMMARY OF STAFF RECOMMENDATION**

Staff recommends that the Board adopt the following motion:

***Motion: I move that the Board receive and file the revised Audit Findings with detailed statements regarding the District's Corrective Action Plan for the FY 2013/2014.***

**DISCUSSION**

This item was originally presented in September 2015. Subsequent to that presentation, the Board requested a further clarification regarding the District plan of action to handle the specific findings, what occurred to cause the finding, staff involvement or lack of involvement and other specifics surrounding the District's action that resulted in the finding. Attached is the document with all the specifics as requested by the Board of Directors.

Also included are the findings from the prior audit (FY 2012/2013) and any comments regarding the District's corrective action where necessary.

Attachment: Audit Findings FY 2013/2014

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## **Finding 2014-1** **Other Post-employment Benefits (OPEB)**

**Criteria:**

The District must either use the services of an actuarial or use the alternative measurement method for employers with fewer than one hundred plan members as stated in GASB Statement No. 45

**Condition:**

During our examination of other post-employment benefits, we noted that the spreadsheet used to estimate the OPEB liability did not follow the GASB Statement No. 45 alternative measurement method no did the District contract for an actuary.

**Cause:**

Staff turnover and management oversight

**Effect**

A lack of knowledge of the correct balances as of June 30, 2014, could likely result in misstatement of the balance.

**Recommendation:**

The District should either contract with an actuary to obtain its OPEB liability or perform the standard alternative measurement method for employers with fewer than one hundred plan members as followed by GASB Statement No. 45

**District's Corrective Action Plan**

Because the current District Accountant, Mike Doyel, could not locate the information within the existing financial records for the District, Mr. Doyel requested a copy of the prior formula used by the previous District Accountants, Dale Flynn and Ampy Haber from the auditors. This formula was forwarded by the auditors to Mr. Doyel for his use. Mr. Doyel prepared the information using that formula and the auditor determined the formula was incorrect. All adjustments were completed according to the auditor's direction.

## **Finding 2014-2** **Compensated Absences**

**Criteria:**

Vacation and sick hours were not available for June 30, 2014.

**Condition:**

During our examination of compensated absences, we noticed that the reported balances were the same as the prior year. Upon further investigation, it was discover that the payroll system can only run an hours report for the current rate and could not provide a reliable report as of June 30, 2014.

**Cause:**

Staff turnover caused the knowledge of the payroll systems limited reporting for compensated absences to be lost when the former employee left.

**Effect:**

A lack of knowledge of the compensated absences balance as of June 30, 2014, could likely result in a misstatement of the balance,

**Recommendation:**

The District should create either a formal accounting procedures manual to ensure that staff and management is cross trained in the payroll system so that staff turnover does not cause of loss of important historical data.



**District's Corrective Action Plan:**

For FY 2013/2014, the prior District Accountant (Ms. Flynn) terminated her employment without notice on June 16, 2014. Neither the Administrative Accounting Assistant III nor the General Manager were aware of the software restrictions regarding accruals (compensated absences) and the necessity for printing the report as of Monday, June 23, 2014, as Friday, June 20, 2014, was the final pay date for FY 2013/2014. The present District Accountant (Mike Doyel) has been in contact with the software developer and has been informed of the limitations of the payroll software. The District Accountant is now fully aware of when the reports for compensated absences will be available and that it must be printed off at the end of the fiscal year immediately after the final payroll is run for that fiscal year. The current payroll software is considered a live system and only allows the District to run this information as the date of each payroll. The District Accountant has made the proper notation on the calendar for future reference.

The District is working on preparing a detailed manual/schedule of job duties to be performed by the District Accountant consistent with the outline within his employment agreement

**Finding 2014-3**

**Management Override of Internal Controls**

**Criteria:**

The District's internal control processes should be able to process receipts, payroll, disbursements, etc. and result in the transactions getting accurately reported into the general ledger. In order to maintain proper segregation of duties, the General Manager should not be directly making journal entries to QuickBooks. **(The District uses MIP Sage Abra Financial Accounting Software. The District does not use QuickBooks.)**

**Condition:**

During our examination of account balances in the general ledger, we noticed that it was difficult to follow and trace the accounting from one account to another due to the large amount of journal entries made, many of which were cancelling a previous entry. The regular internal control process over receipts, payroll, disbursements, etc. should be able to result in correctly recorded transactions. Also, we found that many adjusting journal entries were made directly into QuickBooks by the General Manager.

**Cause:**

Staff turnover and weaknesses in the reporting internal controls.

**Effect:**

Staff turnover and weaknesses in the reporting internal controls. The general ledger is difficult to follow and trace balances. In addition, management's override of the internal controls creates a lack of proper segregation of duties which could result in a misstatement in the financial statements and conceal any misappropriation of assets.

**Recommendation:**

The District's internal controls should be strong enough to ensure that the recording of transactions to the general ledger are proper and correct and without the need for adjusting journal entries to correct or reverse previous journal entries. All journal entries should be made only by the District accountant and they should be printed and filed with an approval signature of the review performed by the General Manager.

**District's Corrective Action Plan:**

In reconciling the financial software staff found numerous discrepancies' in the bankruptcy, liabilities, reserves, bank statements, etc. from prior years. There were extensive discussion with the District Accountant by the current District General Manager. These discussions were regarding all potential journal entries with the District Accountant prior to making any changes or entering any journals. Because of the inadequacies of the prior use of the financial system and the preparation of most information for the auditors from worksheets, the MIP System was not fully utilized. The reserve balances, identifications, cash and fund balances did not match with the prior year audit and these differences were noted in the budget document for FY 14/15. Numerous adjustments were required short of discarding all the information from previous years. The new District Accountant for FY 2014/2015 authorized and reviewed all the journals relative to the operations. The General Manager was asked by the District Accountant to input journal entries into the accounting software (MIP) because of the magnitude of the corrections that were required to ensure the account balances were correct in the General Ledger (GL). The District Accountant reviewed all Journal Entries prior to posting to the GL. The District Accountant enters all Journals.

**Finding 2014-4**

**Bank Statement Reconciliations**

**Criteria:**

The District should reconcile the cash accounts to the general ledger on a timely basis.

**Condition:**

When we examined the cash accounts during fieldwork, the bank reconciliations were not completed until months after the end of the fiscal year.

**Cause:**

District oversight and staff turnover.

**Effect:**

The District's cash and expenses or revenue in various accounts were overstated or understated until reconciliations were done.

**Recommendation:**

The District should ensure that all bank statements are reconciled in a timely manner.

**District's Corrective Action Plan:**

The MIP financial software was implemented in FY 2005/2006. The MIP financial system software contains a bank reconciliation application. Because of lack of knowledge and understanding the prior District Accountants' (Ampy Haber & Dale Flynn) never implemented this module. For FY 2013/2014 neither District Accountant reconciled the bank accounts on a monthly basis using the financial system. Recently the District Accountant, Mike Doyel, discussed the lack of bank reconciliation through the system with Ms. Haber. Ms. Haber stated that was intentional because it was too difficult and time consuming to use the system. The bank reconciliations are currently complete through the bank reconciliation software in the MIP system. In order to utilize the MIP software to its fullest potential it was necessary for the current District Accountant to perform bank reconciliations dating back to when the software was first installed at the District 2005/2006. This was a tremendously huge undertaking and one in which was accomplished with very few suspense items (or unreconciled items) by the close of FY 2014. The bank reconciliations are now being performed exclusively in the MIP software and not in Excel or another method. There has been recommendations made to the Payroll Software developer for assistance with the Payroll bank account reconciliation as currently it is only possible to reconcile as a total as opposed to reconciling each individual check. This discussion is ongoing and should be resolved by the end of FY 2015/2016. Bank reconciliations are being conducted on a monthly basis using the MIP software.

**Finding 2014-5**  
**Fund Balance and Fund Accounting**

**Criteria:**

In order to qualify as a proprietary fund type, a fund must be supported by some kind of fees for services.

**Condition:**

The Refuse Fund has cash and fund balance remaining as of June 30, 2014, despite the fact that the Solid Waste Franchise Agreement was sold to the County during the year.

**Cause:**

District oversight.

**Effect:**

The District is understating cash in its other funds.

**Recommendation:**

The District should bring an action item to the Board in order to decide where the remaining assets should be transferred to.

**District's Corrective Action Plan:**

The District transferred the Solid Waste function to the County of San Luis Obispo effective January 1, 2014. The advisory committees and the Board of Directors have had some discussion regarding the Reserves remaining within the Solid Waste fund and also discussions regarding the potential transfer to support other funds. It is the intention of the Board to discuss the balance of funds within the 650 fund during FY 2015/2016.

**Finding 2014-6**  
**Disbursements**

**Criteria:**

District's policy requires two signatures for every check issued.

**Condition:**

One of the twenty-five checks examined during our disbursements testing only had one signature.

**Cause:**

District oversight.

**Effect:**

A lack of compliance with internal control procedures could cause a material misstatement in the financial statements or possible misappropriation of assets.

**Recommendation:**

The District should ensure that all checks are signed as per District purchasing policy and when a final review of the checks is performed, they should be checked for proper signatures.

**District's Corrective Action Plan:**

The check dated March 27, 2014 issued to PRP Companies in the amount of \$541.07 was signed by one of the Board Members. The signature missing was the General Manager. This occurred while District Accountant Dale Flynn was reviewing the items and authorizing release of the payments. Administrative Accounting Assistant III, reviews all disbursements prior to placing in an envelope for mailing after both the General Manager and Board Member have executed the checks.

**Finding 2014-7**  
**Payroll Timecards**

**Criteria:**

All timecards should be reviewed in order to ensure the time was actually worked and is properly reported. Employees do not receive overtime pay for calls during the normal work hours.

**Condition:**

One of the twenty-five employees tested during our payroll test received overtime pay for work done during the normal work hours.

**Cause:**

District oversight.

**Effect:**

A misappropriation of assets as the employee was paid at the higher overtime rate for normal work hours.

**Recommendation:**

The District should ensure that all timecards are reviewed and approved by an appropriate supervisor to ensure hours are reported to the correct codes.

**District's Corrective Action Plan:**

For payroll period November 11, 2013 through November 24, 2013 payroll was performed and audited by the then District Accountant Ampy Haber. One utilities employee was erroneously paid for 4 hours of overtime. At that time there was no payroll reconciliation performed to see if the electronic timecards were correct. For the pay period February 3, 2014 through February 16, 2014, a second utilities employee was erroneously coded for 4 hours of overtime. The Interim District Accountant Dale Flynn was performing all the payroll functions. Apparently there was no reconciliation performed of the payroll to discover this error.

The timecard transfers, cash transfers, check payments, direct deposits and other payroll functions are performed by the Admin Accounting Assistant III since the untimely departure of the Accountant in June 2014. The General Manager authorizes all cash transfer and payment of all benefits for payroll. The General Manager prepares the CalPERS worksheets per employee based on check detailed analysis report. This worksheet verifies the correct Employee and Employer contribution. This allows staff to identify any hour or pay discrepancy pay period. The salary information is input per employee into each employees account in the CalPERS system. All contribution dollar totals input per employee are calculated automatically based on bi-weekly salary and PERS rates in the PERS system. The PERS system also requires a verification of total hours worked.

Recording dollar contributions by both the employee and employer is the same for both retirement and deferred compensation. The General Manager authorizes the necessary transfers for the CalPERS payments based on the final report generated by the CalPERS system. The final District CalPERS reconciliation must match the final CalPERS report. Any difference are reconciled. The retirement information together with ACH information all related to payroll is detailed on form per fund, reconciled and forwarded to the District Account for cash transfers in the MIP accounting system and review of the journal to insure accuracy. The information on this form must balance with the payroll disbursements. It is the District Accountant responsibility to prepare the appropriate MIP journals for distribution. Staff implemented this process, separation of duties and internal controls after the departure of prior staff in June 2014.

**Finding 2014-8**  
**Petty Cash**

**Criteria:**

The District policy is that petty cash should not be used for purchases over \$50.

**Condition:**

Two of the petty cash purchases we examined were for purchases were in excess of the District's \$50 limit.



**Cause:**

District oversight.

**Effect:**

A potential misappropriation of assets.

**Recommendation:**

The District should ensure that all users of petty cash are aware of the District's policies.

**District's Corrective Action Plan:**

The District previously discovered this mistake and took corrective action. On July 2, 2013, prior to the arrival of current District Accountant and General Manager and under the authorization of the Ampy Haber, District Account, the Fire Department made a purchase from Grover Beach Post Office using petty cash of \$64.08. On June 19, 2014, after the untimely departure without notice of the Interim District Accountant Dale Flynn, when reimbursing the petty cash for Fire Department, the General Manager discovered the petty cash purchase from Michael Tindell Low Cost Signs of \$172.00 by Fire exceeded the policy. The Fire Department was reminded regarding the existing policy.

**Finding 2014-9**  
**Capital Assets**

**Criteria:**

The District policy is to capitalize assets purchased over \$5,000 and with a useful life of at least 2 years.

**Condition:**

In our review of the Board Meeting Minutes and in our repairs and maintenance account search, we identified one purchase of ECG Monitor/Defibrillator Machine for \$32,487 that was expensed as a repairs and maintenance expense rather than properly recorded as a capital addition.

**Cause:**

District oversight.

**Effect:**

A lack of compliance with internal control procedures could cause a material misstatement in the financial statements.

**Recommendation:**

When invoices are coded to repairs and maintenance expense, the employee coding the item and the person reviewing the coding should always assess if the item would be better recorded as a capital addition or a repair.

**District's Corrective Action Plan:**

The District Accountant, Mike Doyel, is correcting the capital expenditure to bring it in line with District Policy. The General Ledger code used for this expense has been renamed to avoid this error occurring in the future. This corrective action will require Adjusting Journal Entries which will cause the Statement of Net Position as well as the Balance Sheet for 2013/2014 to be restated for Fund 301. The entry was posted to a General Ledger account named Capital Expenditures and Accessories.

**Prior year audit findings.**

**Finding 2013-1**  
**Disbursements – Employee Debit Cards**

**Criteria:**

All disbursements should have an approval signature authorizing the payment.

**Condition:**

During our examination of the District's Service Employee Debit Card purchase process, we noted that there was no signature authorizing the payment for one of the ten expenditures tested. Upon further investigation, we found that when the disbursement was processed, a temporary employee had made errors that were caught and corrected but in the check reprocessing, the General Manager's signature of approval was missing.

**Cause:**

District oversight.

**Effect:**

A lack of internal control procedures approving the disbursement of reprocessed expenditures of District funds could result in a misappropriation of assets.

**Recommendation:**

The District should revise the internal controls over the reprocessing of expenditures by requiring all expenditures, original or reprocessed, have signed authorization by the General Manager or supervisor. The supervisor or General Manager's signature would give evidence that the supervisor reviewed the refund and approved its issuance.

**Current Status:**

This was an audit finding for FY 2012/2013. Implemented.

**Finding 2013-2**  
**Compensated Absences**

**Criteria:**

Vacation and sick hours earned and used by each employee must be documented and updated with each payroll processed in order to monitor compliance with the terms of employment, and to quantify accrual of payroll liabilities accurately.

**Condition:**

During our payroll testing procedures we found that there was no formal method of tracking accrued compensated hours earned or used

**Cause:**

District oversight.

**Effect:**

A lack of internal control procedures could cause a misstatement in the financial statements or result in a misappropriation of assets.

**Recommendation:**

The District should calculate and document the compensated absences balances for all employees, and update it as hours are earned, and when hours are used in order to determine that the District is in compliance with the employment agreements, to calculate the accrued vacation balance for annual reporting purposes, and to ensure that all employees follow personnel policies and procedures.

**Current Status:**

Not implemented, see Finding 2014-1. This finding was for FY 2012/2013. This information was never provided by the previous District Accountant Ampy Haber to any person even through it was a finding in the FY 2012/2013 audit. The District Accountant (Dale Flynn) was apparently unaware of the issue and did not provide this information to current staff. Current staff, Administrative Accountant Assistant III and General Manager were unaware of the limitations of the payroll software. The District has taken the appropriate corrective action by printing the detailed Uncompensated Absences Report at the end of the Fiscal Year 2014/2015.

**Finding 2013-3**  
**Construction in Progress (CIP) in the Wastewater Fund**

**Criteria:**

The District should periodically review for impaired capital assets.

**Condition:**

The Wastewater Fund has \$22,067,856 in construction costs expended on a wastewater treatment plant project that was stopped in November 2005. Due to the stoppage of the project and with the responsibility for a new successor project having been transferred to the County under special legislation AB 2701, the amount shown above may no longer represent its true value and may be materially impaired.

**Cause:**

The District's Board of Director's stopped the project and the District's bankruptcy case led to a freeze in the assets involved.

**Effect:**

The District's capital assets are likely overstated, however, under AB 2701, the County has not requested a transfer or valued the associated assets.

**Recommendation:**

The District should assess the value of these assets and work with the County to determine if any remaining assets of value should be transferred to the County's project. The remaining construction in progress needs to either be written off or reduced in value to remove the condition of impairment.

**Current Status:**

This is a finding from the FY 2012/2013 audit. All of the CIP related to the Wastewater Fund has been written off. See Notes to Financial Statements.