



**DATE:** December 13, 2016  
**TO:** Mayor and City Council  
**FROM:** Acting Director of Finance

**SUBJECT**

Transmittal of the Comprehensive Annual Financial Report for the Year Ended June 30, 2016; and of the Memorandum on Internal Control and Required Communications

**RECOMMENDATION**

That the Council adopts the attached Resolution (Attachment II) to receive and file the City's Comprehensive Annual Financial Report (CAFR) and the Memorandum on Internal Control and Required Communications for the fiscal year ended June 30, 2016.

**BACKGROUND**

The City's independent external auditor, Maze and Associates, has completed its audit of the City's financial records for the fiscal year ended June 30, 2016. Maze was selected as the City's independent external audit firm in early 2011 after a thorough proposal review process. Maze and Associates has over twenty-eight years of municipal auditing experience with more than 200 government agencies. In addition to the audited financial statements, the auditors have completed and provided the required *Memorandum on Internal Control and Required Communications*. The City's Comprehensive Annual Financial Report (CAFR) represents all funds of the City, including the General Fund, Water, Sewer, Airport, and all other enterprise and special revenue funds.

Auditing standards require auditors to formally communicate the results directly to the agency's governing body. The purpose being to establish direct and effective two-way communication with the Council and staff, to convey audit matters, the scope of work, difficulties, adjustments to financial statements, or any possible disagreements with management.

**DISCUSSION**

**Comprehensive Annual Financial Report** – Staff is pleased to report that, as in previous years, the auditor's opinion on the financial statements for fiscal year 2016 is without

exception and is unmodified (formerly referred to as “unqualified”). That is, the auditor’s report is not restricted (modified) in any manner, nor does it take exception with any of the information contained in the City’s financial statements. While a modification (known before as a qualification) or exception is not necessarily detrimental, the ability to report that the City’s financial statements continue to earn a “clean opinion” is a positive statement about the City’s financial management and oversight.

Staff will be submitting the fiscal year 2016 CAFR to the Government Finance Officers Association (GFOA) award program, which is a prestigious national award recognizing conformance with the highest standards for preparation of local government financial reports. The City of Hayward has received this award for the last twenty-nine consecutive years.

**Communication Letters from Auditors** – The *Required Communications* letter is intended to identify any communication issues and present new accounting standards pronouncements that may affect the audit. The auditor did not report any difficulties in performing the audit or any disagreements with management.

The second letter presented to management is the *Memorandum on Internal Control*. This letter has two major objectives: (1) to advise the governing body or City Council of any significant deficiencies or material weaknesses in the City’s systems of internal financial controls; and (2) to communicate to the Council any opportunities for improved controls or efficiencies that the auditors noted during the course of their audit. This letter may also advise the Council of upcoming accounting regulations, which may affect the City’s financial records. Staff’s responses to the auditor’s comments and recommendations are noted in the Letter.

#### FY 2016 Finding

The audit identified one Significant Deficiency relating to access to specific areas of the City’s general ledger system. A significant deficiency is a deficiency, or a combination of deficiencies, in internal controls that if ignored could, but in this case did not, lead to a material misstatement. A significant deficiency is less severe than a material weakness, yet important enough that it needs to be communicated to Council formally. As seen in the Recommendation portion of Finding 2016-01 of Attachment III, controls have been put into place to mitigate the risks identified in the conditions prior to the completion of the audit.

*2016-01 Access to Vendor and Employee Databases* The audit noted that two employees who processed payroll also had access to the employee database. In addition, there were several employees, who were not responsible for processing payroll or disbursements, that had access to the employee or vendor database.

The City agrees that this condition existed at the time of the interim audit. In the months between the interim and final phases of the audit, the City changed access for many of the employees noted during audit testing. As noted in the Management Response, of **Attachment III** in the area where exceptions remained, specifically in the payroll area, additional controls have been implemented to detect any errors that could cause a misstatement in the affected areas.

### FY 2015 Finding

As part of the audit protocol, the auditor includes findings from the previous fiscal year (fiscal year 2015) to allow for a final management response and, if cleared, to confirm that the findings are no longer valid. Of the item noted surrounding bank reconciliations (Finding 2015-01), the audit noted that one bank reconciliation was completed and reviewed over 60 days after the month end. In addition, a few of the bank reconciliations had no date indicating when the preparation or review process took place. Furthermore, the City had only reconciled its investment accounts once in fiscal year 2016. During the final phase of the audit in October 2016, the auditors noted that the reconciliations of bank and investment accounts were performed timely.

The City agrees that these conditions existed in June during the interim phase of the audit, but have since changed procedures to prevent future reoccurrences.

### **FISCAL IMPACT**

There is no direct fiscal impact resulting from the approval of the annual audit.

### **PUBLIC CONTACT**

On September 28, 2016, Maze & Associates presented to the Council Budget and Finance Committee an overview of the fiscal year 2016 audit process and the role of the external auditor. On November 16, 2016, staff presented a preliminary, unaudited fiscal year 2016 General Fund summary to the Council Budget and Finance Committee.

*Prepared by and Recommended by:* Dustin Claussen, Acting Director of Finance

Approved by:



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Kelly McAdoo, City Manager