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## 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

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### *Independent Auditor's Report*

To the Honorable City Council  
City of Beaumont

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We have audited, 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, the financial statements of the governmental activities, business-type activities, each major fund, and the aggregate remaining fund information of the City of Beaumont (the City) as of and for the year ended June 30 2020, and the related notes to the financial statements, which collectively comprise the City's basic financial statements, and have issued our report thereon dated January 4, 2021.

### ***Internal Control over Financial Reporting***

In planning and performing our audit of the financial statements, we considered the City'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's internal control. Accordingly, we do not express an opinion on the effectiveness of the City's internal control.

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 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*, we identified certain deficiencies in internal control that we consider to be significant deficiencies.

### MEMBERS

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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 City's financial statements will not be prevented, or detected and corrected on a timely basis. 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 identified deficiencies in internal control over financial reporting, described in the accompanying *Schedule of Findings* as items 2020-001, 2020-002, 2020-003, 2020-004, and 2020-005, that we consider to be significant deficiencies.

### ***Compliance and Other Matters***

As part of obtaining reasonable assurance about whether the City'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 no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

### ***City of Beaumont's Response to Findings***

The City of Beaumont's response to the findings identified in our audit is described in the accompanying *Schedule of Findings*. The City of Beaumont'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.

### ***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 City'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 City's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

*Rogers, Anderson, Malody & Scott, LLP.*

San Bernardino, California  
January 4, 2021

## City of Beaumont

### Schedule of Findings Year Ended June 30, 2020

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#### A. Current Year Findings

##### Finding 2020-001- Cash Disbursements Process – Segregation of Duties

###### Criteria

Adequate segregation of duties between vendors' approvals, addition of authorized vendors into the payable system, and maintenance of vendors' accounts and files is a very important factor because the responsibilities for purchasing, receiving, recording into the accounting system, and disbursement should be separated as much as possible to create the best system of controls.

###### Condition and Context

During our audit, we noted that the Senior Accountant approves vendor changes and also has access to change vendor information. Upon further review, we identified that several other employees in the finance department also have access to change vendor information.

###### Effect

The lack of segregation of duties related to vendor files maintenance and cash disbursements processes could result in erroneous, fictitious, and/or fraudulent vendor payments.

###### Recommendation

We recommend that the Finance Department segregates the responsibilities for approving vendors and adding/editing vendors information into the system and perform a regular risk assessments review to identify where segregation of duties issues need to be corrected.

###### Management Response to Finding

The City concurs with this finding and has initiated corrective action. Effective December 1, 2020, the budget specialist position, which is not part of the payable process, will complete the entry of new vendors and have access to modify vendor records. The senior accountant over accounts payable will complete the review and approval of new vendors but will not have access to add or modify vendor records in the accounting system.

Staff directly involved in payment transactions will no longer have access to add or modify vendor records.

Additionally, audit logs that identify any changes in vendor records, including identifying the individual that made the change will be reviewed monthly to identify the changes in vendors and to verify the staff member who made the change.

## City of Beaumont

### Schedule of Findings Year Ended June 30, 2020

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#### A. Current Year Findings (continued)

##### Finding 2020-002- Payroll Process – Segregation of Duties

###### Criteria

A strong payroll internal control system can generally be implemented to cover potential threats of error and misappropriation with a reasonable effort. Payroll controls should include the following:

- Comparison of actuals to budget information and the review of any unexpected variances;
- Close review and supervision of reports prepared for filing with federal and state taxing authorities; and
- Separation of the payroll functions of employment, timekeeping, payroll preparation, and record-keeping;
- Review of change reports for each payroll period by personnel outside the payroll function with verification of changes.

###### Condition and Context

During our audit, we noted that the Administrative Services Manager processes payroll and has access to change employees' data including pay rates.

###### Effect

The lack of segregation of duties between payroll processes and human resources related functions could result in fictitious employees, or unapproved personnel rate changes.

###### Recommendation

We recommend that the Finance Department segregates the payroll processing function from the employee data changes function and to perform regular risk assessments reviews to identify where segregation of duties issues need to be addressed in the payroll process.

###### Management Response to Finding

The control procedure used by the City to process any changes in employee pay requires approval by the Director of Administration. That change is only prompted by a conditional job offer, satisfactory performance evaluation or an MOU contract obligation. That change is documented on an employee payroll change notice. These forms are submitted as part of the bi-weekly payroll packet that is reviewed by a senior accountant in the Finance Department. An audit report feature within the Paychex system named Employee Change Report is also submitted as part of the bi-weekly payroll packet, and is used to ensure all changes have the appropriate documentation attached.

**City of Beaumont**

**Schedule of Findings  
Year Ended June 30, 2020**

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**A. Current Year Findings (continued)**

**Finding 2020-002- Payroll Process – Segregation of Duties (continued)**

Management Response to Finding (continued)

Effective October 20, 2020, the employee payroll change notice will be signed by the Director of Administration. In the absence of the Director of Administration, the Director of Finance will approve any changes. These approval forms will be submitted as part of the bi-weekly payroll packet that is reviewed by a senior accountant in the Finance Department prior to submittal. While the senior accountant initialed the employee payroll change form in the past, a signature line was added for ease of identification. The Administrative Services Manager has also begun to attach the back page of the employee evaluation, conditional job offer, MOU page or an email directing the pay rate change.

An audit feature is available within the Paychex system currently utilized by the City. The audit feature allows for a report of all pay changes processed within defined time periods. This audit report will be reviewed quarterly by the Finance Department to determine if all pay changes have the required approvals.

## City of Beaumont

### Schedule of Findings Year Ended June 30, 2020

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#### A. Current Year Findings (continued)

##### Finding 2020-003- Payroll Process – Personnel Action Forms

###### Criteria

A strong payroll internal control system can generally be implemented to cover potential threats of error and misappropriation with a reasonable effort. Payroll controls should include the following:

- Comparison of actuals to budget information and the review of any unexpected variances;
- Close review and supervision of reports prepared for filing with federal and state taxing authorities; and
- Separation of the payroll functions of employment, timekeeping, payroll preparation, and record-keeping;
- Review of change reports for each payroll period by personnel outside the payroll function with verification of changes.

###### Condition and Context

During our audit, we noted that several personnel action forms were not approved by the employee or appropriate supervising personnel.

###### Effect

Changes to personnel records such as wages increases, promotions, status changes, etc., need to be documented in a Personnel Action Form with formal acknowledgment by the employee and a supervisory personnel as well. Failure to formally document the changes substantially increases the risk of unauthorized changes in payroll data such as pay rates, hours worked, etc., which significantly weakens internal control.

###### Recommendation

We recommend that the Finance Department have all personnel action forms signed by the affected employee and by a supervisory personnel as well; and to perform regular risk assessments reviews to identify where lacks of internal controls issues in the payroll process need to be addressed.

###### Management Response to Finding

Management concurs that employee payroll change forms have not been signed by employees and supervisors. Effective October 20, 2020, all employee change forms will be required to be signed by the employee and a supervisory position.

As noted in the finding above, these documents are only completed in conjunction with a conditional job offer, satisfactory performance evaluation or an MOU contract obligation. The copy of the form is routed to the employee for their record. The form is included as part of the bi-weekly payroll file and reviewed by a senior accountant in the Finance Department.

**City of Beaumont**

**Schedule of Findings  
Year Ended June 30, 2020**

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**A. Current Year Findings (continued)**

**Finding 2020-003- Payroll Process – Personnel Action Forms (continued)**

Management Response to Finding (continued)

Management notes that mitigating controls have been in existence, in that while employee payroll change forms have not been signed by employees and supervisors, employee pay modifications generally occur at an anniversary date and an evaluation that is signed by the employee and supervisor usually precedes any modification in pay. In those instances where an evaluation is not completed, the personnel policies of the City provide that an employee is entitled to a merit increase. As a result, increases in pay are driven by policies and procedures of the City and can be tied to the employee's anniversary date.

## City of Beaumont

### Schedule of Findings Year Ended June 30, 2020

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#### A. Current Year Findings (continued)

##### Finding 2020-004 Segregation of Duties for Business Licenses Process

###### Condition:

During our audit, lack of segregation of duties was noted in the City's Business Licenses process. The permit technician, who accepts payments for business licenses, has the ability to issue and distribute business licenses. There is no independent reconciliation of the business licenses issued from the HdL system with the amounts collected and posted in the Incode cash receipts system.

This finding was previously reported in 2019 as finding 2019-001 and in 2018 as finding 2018-005 - Segregation of Duties for Business Licenses Process.

###### Criteria:

The same individual should not have access to the payments from customers and the ability to issue business licenses unless an appropriate mitigating control has been implemented.

###### Cause:

The City does not perform an independent reconciliation for business licenses between the HdL system and the Incode cash receipts system due to system reporting limitations within Incode that were not evident prior to purchasing the system.

###### Effect:

Business licenses could be issued without a corresponding cash receipt being recorded in the City's general ledger and ultimately deposited into the City's bank account.

###### Recommendation:

We recommend the City implement a procedure to generate reports from the HdL business license program, periodically (i.e. daily, weekly, monthly), and have someone independent of the business license issuance and collection functions review and reconcile the amounts from these reports to the revenues posted in the City's general ledger. In addition, the permit and fees process should be integrated into the accounting software to limit the number of manual entries posted to the general ledger system.

###### Management's Response:

Reports of transactional activity will be generated from the HdL business license system that details business license collection activity. An Accounting Technician in the Finance Division will compare these reports to the deposits submitted to the Finance Department and entered into the City's general ledger. This reconciliation will be completed weekly. Any discrepancies will be brought to the attention of the Administrative Services Manager for resolution. Effective February 1, 2021, the Finance Department will complete a reconciliation of funds collected from business license activity to the license activity in the HdL system.



## City of Beaumont

### Schedule of Findings Year Ended June 30, 2020

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#### A. Current Year Findings (continued)

##### Finding 2020-005 Overhead Cost Allocation

###### Condition:

The City allocates certain General Fund costs (administration, maintenance, etc.) to the Sewer Enterprise, Gas Tax, Transit Enterprise, and the Community Facilities District (CPD) Fund. The amounts are based on calculations included in schedules maintained by the Finance Department. Currently, the City is not allocating and recovering any of its indirect costs to federal (or state) grants. While the City completed a cost allocation study in April 2016 and has implemented the cost allocation of administrative costs to the various funds within the City, the City has not had a formal Cost Allocation Plan performed for charging of its costs to federally funded projects.

This finding was previously reported in 2019 as finding 2019-002 and in 2018 as finding 2018-007 – Overhead Cost Allocation.

###### Criteria:

Cost allocation plan methodologies should be thoroughly documented for transparency purposes, and updates to the plans should be done periodically in accordance with best practices.

###### Cause:

The City does have a formal cost allocation plan to allocate internal costs, and the plan developed internally is not sufficient to claim indirect costs against federal (and state) grant programs.

###### Effect:

The City could potentially be utilizing allocation methods which result in either less administrative costs or excessive administrative costs being allocated than would be allowable if detailed cost allocation studies were performed on a periodic basis, and in accordance with federal grant requirements. Costs that could be reimbursable from other than local sources may be able to be claimed if adequately supported. For federal awards, the City may elect to use the 10 percent of Modified Total Direct Cost (MTDC) de Minimis indirect rate to recover indirect costs as part of your federal grant budgets. If the City elects to use the 10 percent de Minimis rate, the Uniform Guidance requires that the City use Modified Total Direct Costs as the cost base. MTDC means all direct salaries and wages, applicable fringe benefits, materials and supplies, services, travel, and up to the first \$25,000 of each sub award (regardless of the period of performance of the sub awards under the award).

###### Recommendation:

We recommend the City perform a full cost allocation study of administrative costs to ensure the detailed methodology for the allocation of administrative costs is reasonable and appropriate, based on the current circumstances, and that the methodology is clearly defined and documented. A plan should be prepared in accordance with the Uniform Guidance in the event the City wishes to allocate and claim the indirect costs against federal (and state) grant programs. Due to the complexity involved in developing a well-supported and reasonable indirect cost plan, the City should evaluate the cost of outsourcing this study as opposed to the use of internal staff time.

**City of Beaumont**

**Schedule of Findings  
Year Ended June 30, 2020**

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**A. Current Year Findings (continued)**

**Finding 2020-005 Overhead Cost Allocation (continued)**

Management's Response:

While the City completed a cost allocation study in April 2016 and has implemented the cost allocation of administrative costs to the various funds within the City, further work is necessary to fully comply with this recommendation. The City has not yet completed the cost allocation for indirect costs to federal and state grant programs. Management intends to re-evaluate its cost allocation strategy and hire an external professional to assist the City in completing the cost allocation process. There has been no progress on this finding since the last audit.

**City of Beaumont**

**Schedule of Findings  
Year Ended June 30, 2020**

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**B. Prior Year Findings**

**Findings 2019-001 Segregation of Duties for Business Licenses Process**

Status:

Finding has not been implemented. See repeat finding at 2020-004.

**Findings 2019-002 Overhead Cost Allocation**

Status:

Finding has not been implemented. See repeat finding at 2020-005.

**Finding 2019-003 Unauthorized Wire Transfers**

Status:

Implemented.