

CITY OF BEAUMONT
MANAGEMENT REPORT
AND
AUDITOR'S COMMUNICATION LETTER

June 30, 2011

CITY OF BEAUMONT

JUNE 30, 2011

TABLE OF CONTENTS

Transmittal Letter 1

Required Communication 3

**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 Audit Standards** 6

Current Year Recommendations:

Material Weakness:

 2011-1 Deficit unassigned fund balance in general fund..... 8

Significant Deficiencies:

 2011-2 Deficit fund balances in major governmental funds..... 8

 2011-3 Deficit cash balance in general fund..... 8

 2011-4 Deficiencies in internal control over cash receipts 9

 2011-5 Deficiencies in internal control over cash disbursements..... 10

 2011-6 Deficiencies in the employee advances and employee computer
 loan program..... 10

Compliance or Other Matters:

 2011-7 Failed to submit the fiscal year 09-10 Agency's Annual Report
 to the respective legislative body within six months after the end
 of the Agency’s fiscal year 11

 2011-8 5 Year Implementation Plan 11

Status of Prior Year Recommendations..... 12



MOSS, LEVY & HARTZHEIM LLP

CERTIFIED PUBLIC ACCOUNTANTS

PARTNERS

RONALD A LEVY, CPA
CRAIG A HARTZHEIM, CPA
HADLEY Y HUI, CPA

COMMERCIAL ACCOUNTING & TAX SERVICES

9107 WILSHIRE BLVD. SUITE 500
BEVERLY HILLS, CA 90210
TEL: 310.273.2745
FAX: 310.670.1689
www.mlhcpas.com

GOVERNMENTAL AUDIT SERVICES

5800 E. HANNUM, SUITE E
CULVER CITY, CA 90230
TEL: 310.670.2745
FAX: 310.670.1689
www.mlhcpas.com

August 1, 2012

To the City Council
of the City of Beaumont
Beaumont, California

In planning and performing our audit of the financial statements of the governmental activities, business-type activities, each major fund, and the aggregate remaining fund information of the City of Beaumont, California (City), as of and for the fiscal year ended June 30, 2011, in accordance with auditing standards generally accepted in the United States of America, we considered the City's internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control. Accordingly, we do not express an opinion on the effectiveness of the City'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 significant deficiencies or material weaknesses and therefore, there can be no assurance that all such deficiencies have been identified. However, as discussed below, we identified certain deficiencies in internal control that we consider to be significant deficiencies and material weaknesses.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or 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 deficiency presented in the current year recommendations section as finding 2011-1 to be a material weakness.

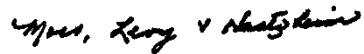
A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies presented in the current year recommendations section as findings 2011-2 through 2011-6 to be significant deficiencies.

During our audit, we noted certain other matters involving internal controls and their operations, compliance, or other matters, and are submitting, for your consideration, related recommendations designed to help the City make improvements and achieve operational efficiencies. These observations are described in the current year recommendations section as findings 2011-7 and 2011-8. Our comments reflect our desire to be of continuing assistance to the City.

The City's written responses to the findings identified in our audit are described in the current year recommendations section. We did not audit the City's responses and, accordingly, we express no opinion on them. In addition, we would be pleased to discuss the recommendations in further detail at your convenience, to perform any additional study of these matters, or to assist you in implementing these recommendations.

We have included in this report a summary of communications with the City Council as required by professional auditing standards as well as an Auditor's report on internal control as required under Government Auditing Standards. We would like to thank the City's management and staff for the courtesy and cooperation extended to us during the course of our engagement. The accompanying communications and recommendations are intended solely for the information and use of the City Council and management, and is not intended to be and should not be used by anyone other than these specified parties.

Very truly yours,



MOSS, LEVY & HARTZHEIM, LLP
Culver City, CA
August 1, 2012



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August 1, 2012

To the City Council
of the City of Beaumont
Beaumont, California

We have audited the financial statements of the governmental activities, the business type activities, each major fund, and the aggregate remaining information of the City of Beaumont (City) for the fiscal year ended June 30, 2011. Professional standards require that we provide you with the information about our responsibilities under auditing standards generally accepted in the United States of America, and *Government Auditing Standards* as well as certain information related to the planned scope and timing of our audit. We have communicated such information in our letter to you dated July 25, 2011. Professional standards also require that we communicate to you the following information related to our audit.

Significant Audit Findings

Qualitative Aspects of Accounting Practices

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by the City are described in Note 1 to the financial statements. As discussed in Note 1 of the notes to the basic financial statements, two new accounting pronouncements were adopted during the fiscal year. The new pronouncements are Governmental Accounting Standards Board (GASB) Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions* and Statement No. 59, *Financial Instruments Omnibus*. The implementation of GASB Statement No. 54 had an effect on the financial statements, whereas Statement No. 59 did not. We noted no transactions entered into by the City during the fiscal year for which there is a lack of authoritative guidance or consensus. All significant transactions have been recognized in the financial statements in the proper period.

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimates affecting the City's financial statements were:

Management's estimate of the funding progress for CALPERS is based on CALPERS's estimate, the funding progress of Other Postemployment Benefits (OPEB) is based on an actuarial report prepared by a third party, the collectability of receivables (including accounts, notes and loans receivable, and advances to RDA), the estimated historical cost of capital assets and the estimated useful life of the capital assets were based on historical data and industry guidelines. We evaluated the key factors and assumptions used to develop these estimates in determining that they are reasonable in relation to the financial statements taken as a whole.

Difficulties Encountered in Performing the Audit

We encountered no significant difficulties in dealing with management in performing and completing our audit.

Corrected and Uncorrected Misstatements

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management. Management has corrected all such misstatements. \$1,057,894 of the misstatements detected as a result of audit procedures and corrected by management were material, either individually or in the aggregate, to the financial statements taken as a whole. Audit journal entries aggregating \$1,057,894 were for accounts payable, notes receivable, cash, advances to other funds, and deferred revenue.

Disagreements with Management

For purposes of this letter, professional standards define a disagreement with management as a financial accounting, reporting, or auditing matter, whether or not resolved to our satisfaction, that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

Management Representations

We have requested certain representations from management that are included in the management representation letter dated August 1, 2012.

Management Consultations with Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the City's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Other Audit Findings or Issues

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the City's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

Other Information in Documents Containing Audited Financial Statements

With respect to the supplementary information accompanying the financial statements, we made certain inquiries of management and evaluated the form, content, and methods of preparing the information to determine that the information complies with accounting principles generally accepted in the United States of America, the method of preparing it has not changed from the prior period, and the information is appropriate and complete in relation to our audit of the financial statements. We compared and reconciled the supplementary information to the underlying accounting records used to prepare the financial statements or to the financial statements themselves.

The City's General Fund had a deficit unassigned fund balance of \$10,871,054 at June 30, 2011. It is uncertain whether the \$22,380,000 advances to the Beaumont Redevelopment Agency will be collectible due to the dissolution of the Redevelopment Agency. The City's general fund continues to rely on overhead reimbursement and services payments from various CFDs within the City to balance its budget. The City, in its 2012-13 budget, also used a one-time transfer of \$2 million from its Equipment Replacement Fund to help balance the budget. It is uncertain if the City will be able to; 1) balance its general fund budget if such revenues are no longer available, and 2) reduce the deficit without additional revenue sources or expenditure cuts.

This information is intended solely for the information and use of the City Council and Management of the City and is not intended to be and should not be used by anyone other than these specified parties.

Very truly yours,



MOSS, LEVY & HARTZHEIM, LLP
Culver City, CA
August 1, 2012



MOSS, LEVY & HARTZHEIM LLP

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INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

To the City Council
of the City of Beaumont
Beaumont, California

We have audited the accompanying financial statements of the governmental activities, business-type activities, each major fund, and the aggregate remaining fund information of the City of Beaumont, California (City) as of and for the fiscal year ended June 30, 2011 and have issued our report thereon dated August 1, 2012. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

Management of City of Beaumont is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered City of Beaumont's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of City of Beaumont's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the City of Beaumont's internal control over financial reporting.

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 significant deficiencies or material weakness and therefore, there can be no assurance that all such deficiencies have been identified. However, as discussed below, we identified certain deficiencies in internal control that we consider to be 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 deficiency described in this report to be material weakness, as item 2011-1.

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 this report to be significant deficiencies, as items 2011-2 through 2011-6.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed two instances of noncompliance that are required to be reported under Government Auditing Standards and which are described in this report, as items 2011-7 and 2011-8.

The City's responses to the findings identified in our audit are described in this report. We did not audit the City's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the City council, management, and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Very truly yours,



Moss, Levy & Hartzheim LLP
Culver City, California
August 1, 2012

CURRENT YEAR RECOMMENDATIONS

Material Weakness

2011-1 Finding – Deficit unassigned fund balance in general fund:
In preparation of the financial statements, we noted that the general fund had a deficit unassigned fund balance of \$10,871,054 at June 30, 2011.

Effect:

With a material deficit amount in unassigned fund balance, it is an indication that the City has significant deficit spending in its general operation. With successive years of operating deficits this causes a financial hardship on the City. The general fund is the operating fund of the City and with a potential RDA advances that can't be collected. The City will not have the working capital to operate.

Recommendation:

We recommend the City develop a management action plan to eliminate or reduce the deficit unassigned fund balances and deficit spending.

Management's Response:

The City has instituted a hiring freeze and done an overall review of all operating expenditures with department heads to capture additional savings. In addition, the City has reviewed and adjusted its operating and capital expenditure programs to reduce any deficit spending.

Significant Deficiencies

2011-2 Finding – Deficit fund balances in major governmental funds:
In preparation of the financial statement, we noted that a deficit fund balance of \$20,247,435 exists in the Community Redevelopment Capital Projects fund and a deficit fund balance of \$752,698 exists in the Capital Improvement Capital Project Fund.

Effect:

The funds with a deficit fund balance are in effect borrowing from City funds with positive fund balances. If the City continues to rely on borrowing to finance current operations, the City will eventually experience severe fiscal problems.

Recommendation:

We recommend the City develop a management action plan to reduce or eliminate the deficit fund balances and deficit spending.

Management's Response:

The Community Redevelopment Capital Projects fund no longer exists since the dissolution by the State Legislature. A receivable in the General Fund, that funded the RDA capital projects, is expected to be repaid from future property tax revenue.

2011-3 Finding – Deficit cash balance in general fund:
During the review of the trial balance, we noted that the general fund had a deficit cash balance which resulted in borrowing cash from the Community Facilities Capital Project Fund as of June 30, 2011.

Effect:

Funds with deficit cash balances are borrowing cash from restricted capital project funds for activities that are not designated by the capital project fund. In the event that the City does not obtain cash flows to support operations, the City could become insolvent. There

could also be some compliance impact if the City is borrowing funds for operating and they are not intended for that purpose.

CURRENT YEAR RECOMMENDATIONS (Continued)

Significant Deficiencies (Continued)

2011-3 Finding – Deficit cash balance in general fund: (Continued)

Recommendation:

We recommend the City attempt to ensure that that no funds have deficit cash balances at the fiscal year end and develop a management action plan to reduce or eliminate the deficit spending.

Management’s Response:

The repayment of the receivable from the redevelopment agency capital projects fund of approximately \$22 million will eliminate the inter-fund borrowing. The City’s cash flow plan eliminates the need for any additional inter-fund borrowing.

2011-4 Finding – Deficiencies in internal control over cash receipts:

During our review and testing of the internal control of cash receipts, we noted the following deficiencies:

- a) There was a lack of segregation of duties at the Community Center. The person who receives cash also enters cash receipts into the system, reconciles cash receipts to the daily reports, and prepares deposit slips.
- b) Manual cash receipt books at the Community Center were not used in sequence.
- c) There was insufficient supporting documentation for several items tested at the Community Center, such as copy of pink slips of receipts that should be attached to the manual cash receipt books.
- d) There was a lack of reconciliation procedures.

Effect:

Without adequate segregation of duties over cash receipts and an established system to reconcile the cash receipts, misappropriation of funds may occur. Additionally, it is difficult to verify the accuracy of the amount charged or received from the customer, as well as effective control if receipt books are not properly used in sequence. Also, when sufficient supporting documentation is not obtained or retained, an embezzlement of funds could occur and go undetected.

Recommendation:

We recommend that the City ensure there is sufficient segregation of duties over receiving payments, recording cash receipts, reconciling cash receipts to daily reports, and preparing deposit slips. The City also needs to ensure that manual cash receipt books are properly used and that all cash receipting procedures are performed to reduce the likelihood of a misappropriation of funds. Additionally, the City should establish a centralized system to reconcile all cash receipts and ensure all supporting documentation is obtained or retained.

Management’s Response:

The “Incode” electronic cash receipting system has been implemented at the Community Center and the same procedures used at City Hall are now being used at the Community Center.

CURRENT YEAR RECOMMENDATIONS (Continued)

Significant Deficiencies (Continued)

2011-5 Finding – Deficiencies in internal control over cash disbursements:
During our review and testing of the internal control of cash disbursements, we noted that there was a lack of control and oversight over debit and credit card usage due to the absence of City formal written policies. Furthermore, we also noted that there was not sufficient supporting documentation (receipts) from City credit card holders.

Effect:

The absence of formal written policies over credit cards and debit cards usage increases the risk of fraud which could lead to an increased likelihood of misappropriation of funds. Without sufficient supporting documentation, it is difficult to ascertain whether purchases were for the City's benefit.

Recommendation:

We recommend that the City establish written policies and procedures in regards to the credit card and debit card usage. Additionally, the City should obtain/retain adequate supporting documentation, including detailed receipts stating the purpose of the purchases, prior to processing for payment for credit card bills.

Management's Response:

Our Human Resources department will prepare a policy on the use of credit/debit cards and cardholders will be required to submit receipts prior to payment as part of the policy.

2011-6 Finding – Deficiencies in the employee advances and employee computer loan program:
During our review of receivables, it was noted that there was neither a written policy for administration of, nor an agreement between the City and employees who are enrolled in, the employee computer loan program and for employee advances. We also noted that there was not sufficient supporting documentation presented for employee advances. Additionally, the employee computer loan program payment schedule prepared by the Accounting Department was not reconciled to the accounting records.

Effect:

Without a written policy or agreement between the City and employees enrolled in the employee computer loan program and for employee advances, there is no administrating instruction nor is there a binding contract to ensure the collectability of loans given. Moreover, without adequate supporting documentation and reconciliation procedures, there is an increased risk of misappropriation of funds.

Recommendation:

We recommend that the City establish policies and procedures for the employee advances and employee computer loan program, as well as written agreements with employees who are enrolled in the program to reduce the risk of uncollectible receivables. Also, the City should ensure that periodic reconciliations are prepared.

Management's Response:

The Human Resources Department is currently preparing computer loan and payroll advance policies and reconciliations will be done on a periodic basis.

CURRENT YEAR RECOMMENDATIONS (Continued)

Other Matters

2011-7 Finding - Failed to submit the fiscal year 09-10 Agency's Annual Report to the respective legislative body within six months after the end of the Agency's fiscal year:

During the compliance audit for the Redevelopment Agency (Agency), we noted that the Agency failed to submit their fiscal year 09-10 Agency's Annual Report to the respective legislative body within six months after the end of the Agency's fiscal year. Furthermore, the Agency failed to file the Agency's Financial Transactions Report & Housing Activity Report to the State before the required deadline.

Criteria:

Section 33080.1 of the California Health and Safety Code requires that Redevelopment Agencies must present an annual report to its legislative body and the SCO within six months of the end of a fiscal year.

Effect:

The Agency is not in compliance with the Health and Safety Code section 33080.1 of the state report filing requirement.

Recommendation:

The Agency should provide their employees with sufficient training regarding state reporting requirements.

Management's Response:

Agency staff is aware of the filing requirement and will attempt to file all reports timely.

2011-8 Finding - 5 year Implementation Plan:

During the compliance audit for the Redevelopment Agency, we noted that, for the fiscal year ended June 30, 2011, the Agency had not adopted its 5 year implementation plan by the required due date per the California Health and Safety Code.

Criteria:

Section 33490 of the California Health and Safety Code requires that Redevelopment Agencies produce and approve timely an Implementation Plan for each project area every 5 years.

Effect:

The Agency is not in compliance with the Health and Safety Code for implementation dates of required reports.

Recommendation:

The Agency should address this issue timely in the future.

Management's Response:

Due to the California State Legislature's dissolution of redevelopment agencies, the City feels this Implementation Plan is not necessary and it will not be done.

STATUS OF PRIOR YEAR RECOMMENDATIONS

None reported.