

Revision to Agenda Item #1

- Revising Attachment A – Draft Victorville Annual Comprehensive Financial Report for Fiscal Year Ended June 30, 2022 page 120 of the report (page 152 of the agenda) correcting the formatting of the data for presentation under the SCLAA Enterprise Fund section.
- Adding Attachment E – Government Auditing Standards (GAS) Letters for Draft ACFR, Water District, and Southern California Logistics Airport Authority reports for Fiscal Year Ended June 30, 2022 to provide additional information.

ATTACHMENT A
Draft City of Victorville Annual
Comprehensive Financial Report
(ACFR) for Fiscal Year Ended June 30,
2022
REVISIONS

**CITY OF VICTORVILLE
NOTES TO BASIC FINANCIAL STATEMENTS
JUNE 30, 2022**

NOTE 22 LEASES

General Fund

The General Fund, acting as lessor, leases buildings and land under long-term, noncancelable lease agreements. The leases expire at various dates through 2123 and provide for renewal options ranging from 1 year to 55 years. Certain leases provide for increases in future minimum annual rental payments based on a defined percent in the contract or increases in the Consumer Price Index, subject to certain minimum increases.

During the year ended June 30, 2022, the General Fund recognized \$154,930 and \$48,879 in lease revenue and interest revenue, respectively, pursuant to these contracts.

SCLAA Enterprise Fund

The SCLAA, acting as lessor, leases buildings and land under long-term, non-cancelable lease agreements. The leases expire at various dates through 2056 and provide for renewal options ranging from 1 year to 55 years. During the year ended June 30, 2022, the SCLAA recognized \$8,251,728 and \$1,524,013 in lease revenue and interest revenue, respectively, pursuant to these contracts.

Certain leases provide for increases in future minimum annual rental payments based on a defined percent in the contract or increases in the Consumer Price Index, subject to certain minimum increases. Lease revenue comprises a majority of the SCLAA's operating revenues, therefore, this activity is considered to be the principal operation of the SCLAA. Total future minimum lease payments to be received under lease agreements are as follows:

<u>Year Ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2023	\$ 7,662,011	\$ 1,462,845	\$ 9,124,856
2024	6,868,119	1,374,054	8,242,173
2025	6,021,790	1,278,378	7,300,168
2026	6,165,361	1,252,066	7,417,427
2027	6,236,410	1,159,686	7,396,096
2028-2032	26,252,464	3,870,687	30,123,151
2033-2037	12,252,870	1,797,082	14,049,952
2038-2042	3,753,055	1,157,998	4,911,053
2043-2047	4,323,812	725,707	5,049,519
2048-2052	3,622,056	325,329	3,947,385
2053-2056	1,354,975	52,136	1,407,111
Total	<u>\$ 84,512,923</u>	<u>\$ 14,455,968</u>	<u>\$ 98,968,891</u>

Sanitary Enterprise Fund

The Sanitary Enterprise Fund, acting as lessor, leases a land under a long-term, noncancelable lease agreement. The lease expires in 2069 and provides for increases in future minimum annual rental payments based on increases in the Consumer Price Index, subject to certain minimum increases. During the year ended June 30, 2022, the Sanitary Enterprise Fund recognized \$58,722 and \$57,607 in lease revenue and interest revenue, respectively, pursuant to this contract.

ATTACHMENT 0

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Government Auditing Standards Letter
and Management Responses for the
Draft City of Victorville Annual
Comprehensive Financial Report
(ACFR) for Fiscal Year Ended June 30,
2022

MANAGEMENT RESPONSES TO GAS LETTER

2022-001

Material Weakness – Pension Amounts

Condition: Amounts recorded in the general ledger for the pension deferred outflows and inflows of resources and pension expense and amounts allocated to governmental activities, business-type activities, and enterprise funds for these amounts did not agree individually or in total to the City's calculated pension amounts.

Criteria or specific requirement: The pension deferred outflows and inflows of resources and pension expense should be recorded in the general ledger at amounts that agree to the CalPERS provided amounts for the miscellaneous defined benefit pension plan and to the calculated amounts utilizing the CalPERS tool for the safety cost-sharing defined benefit pension plan. The amounts allocated to City funds should follow the City's historical policy for allocating such amounts, which is based on the current year CalPERS contributions by fund.

Effect: The pension deferred outflows and inflows of resources and pension expense were materially misstated, which resulted in an overall decrease to pension expense of approximately \$2.4 million, increase to deferred outflows of \$19.8 million and increase to deferred inflows of \$17.5 million.

Cause: The City made errors when generating the journal entry to record the pension deferred outflows and inflows of resources and pension expense.

Repeat Finding: This finding is a repeat of a finding in the immediately prior year.

Recommendation: We recommend the City implement policies and procedures to ensure the accurate recording of pension amounts in all funds.

Views of responsible officials and planned corrective actions:

With the additional staff added in FY21/22, there was insufficient training which took place and resulted in reconciliation errors in City amounts versus auditors' amounts. After meeting with the auditors to review the reconciliation steps and ending balances, it was determined a step was incorrectly omitted which caused the reconciliation to the incorrect table in the actuarial valuation and the City has since corrected the reconciliation processes. Implementation of a three-tier review process is now in place and additional staff will be properly trained in FY22/23 as part of our cross-training procedures.

As part of the FY 23-24 budgeting process, the City's Executive Management Team will be requesting the addition of an Internal Auditor position to the Table of Organization to help to identify potential audit issues on an ongoing basis, prior to the external auditing process.

2022-002

Material Weakness – Capital Assets

Condition: During our review of capital assets, we noted (1) construction in progress projects that were complete or had been cancelled and required reclassification to other capital asset categories or expensing; (2) recording missing capital asset additions; (3) removal of a project included in construction in progress for which the goods had not yet been received that required reclassification to prepaid expenditures. In addition, the City had restatements to beginning equity to record capital asset additions to prior years. The capital asset restatements also resulted in a restatement to recognize the SCLAA's liability due to tenants for rental credits owed from tenant capital improvements made and contributed to SCLAA.

Criteria or specific requirement: When capital projects are complete and meet the City's capitalization policy, these projects should be moved to the appropriate asset category, such as infrastructure, and depreciated over the life of the asset. Projects that do not meet the City's capitalization policy should not be recorded as construction in progress and should be expensed as incurred. When projects are cancelled and the asset is no longer usable, the project should be expensed. In addition, all expenses/expenditures that meet the City's capitalization policy should be capitalized. When goods have not yet been received, the City should record a prepaid asset instead of a capital asset. Capital assets contributed from tenants should be recognized as capital contributions and a capital asset addition in the year the assets are contributed. Any corresponding liability due to tenants from donating these capital improvements should be recognized as the liability is incurred.

Effect: Audit adjustments had a net impact to decrease capital assets \$4.5 million, decreasing expenses/expenditures \$2.7 million and increase prepaid items \$4.2 million. The restatement increased capital assets \$8.2 million, recorded accumulated depreciation of \$201 thousand, and recognized a \$756 thousand liability for rental credits from tenant capital improvements made and contributed to the SCLAA.

Cause: The City did not sufficiently follow the year-end closing procedures to identify the above errors. In addition, the SCLAA did not review lease agreements for capital improvement and rental credit terms to consider the impact on the general ledger.

Repeat Finding: This particular finding was not noted in the immediately prior year; however, findings related to audit adjustments for capital assets were noted in the immediately prior year.

Recommendation: We recommend the City implement policies and procedures to review capital assets at year-end for appropriate classification and review leases for capital improvement and rental credit terms.

Views of responsible officials and planned corrective actions:

- (1) City personnel reconciling capital assets will review with departments at minimum twice a year as well as reviewing budget to actual for projects and notices of completion in city council agenda items to catch all completed projects. Additionally, staff will question departments regarding all projects residing in the Construction in Progress coding with no activity for at least four months to ensure that project is still continuing forward or if it needs to move to "Idle

Assets” to be completed in the future or expensed if project has been discontinued and/or did not result in an asset.

- (2) In performing reconciliation of the assets currently in the Construction in Progress (CIP) account as part of the review process, staff discovered an asset which had been completed in FY2020-21 but was still recorded as “CIP”. Staff immediately capitalized the item and brought this to the attention of the supervisor who contacted auditors to make them aware.
- (3) With the implementation of GASB87, staff did not have procedures already in place to capture portions of a lease which had rental credits for tenant improvements to be completed. Staff has now incorporated this as part of the review of all new leases so any future lease agreements with embedded rental credits or other tenant improvement lease payment reductions are recognized as capital improvements when appropriate. Additionally, staff will discuss new leases with departments to ensure that any non-lease revenue is properly recorded.

As part of the FY 23-24 budgeting process, the City’s Executive Management Team will be requesting the addition of an Internal Auditor position to the Table of Organization to help to identify potential audit issues on an ongoing basis, prior to the external auditing process

2022-003

Material Weakness – Grants Receivable, Revenues, Expenditures/Expenses and Unavailable Revenue

Condition: The City has various projects that are grant funded on a reimbursement basis, which means that the City incurs the cost and then requests for reimbursement from the funding source. During our audit, we reviewed these projects and had numerous inquiries when grant receivables did not equal the unreimbursed eligible expenditures. This led to numerous adjustments to correct the balances.

In addition, the Victorville Water District (District) received federal funds under the American Rescue Plan Act (ARPA) that were utilized for payment of past due utility bills resulting from the pandemic. The City recorded these amounts in a governmental fund instead of the District’s enterprise fund that received the benefit.

Criteria or specific requirement: Grant receivables should be equal to the eligible project expenditures less any amounts previously reimbursed by the grantor. For governmental funds, deferred inflows of resources, unavailable revenues, should be recorded instead of revenue when those amounts are received after the City’s availability period, which is 60 days. In addition, in the cases when revenues must be returned if not utilized, cash received should be offset by unearned revenue.

Grant revenues and expenses should be recorded in the fund that received the benefit.

Effect: Approximate changes in the general ledger balances due to the adjustments are as follows: net decrease in receivables of \$13.4 million, net decrease in deferred inflows of resources, unavailable

revenues, and unearned revenues of \$12.5 million, and a net decrease in revenues of \$803 thousand. In addition, the City had a restatement of \$591 thousand to record unearned revenue for amounts collected that must be returned to ratepayers if not utilized. This also resulted in an audit adjustment of \$635 thousand to record revenues and expenses in the District and remove these revenues and expenditures from the City's governmental special revenue fund.

Cause: The City did not perform an analysis on each project to verify the balances in these accounts prior to commencement of the audit procedures. The City recorded the cash received in the District's enterprise fund; however, all revenues and expenditures/expenses were recorded in a City governmental special revenue fund.

Repeat Finding: This finding is a repeat of a finding in the immediately prior year.

Recommendation: We recommend the City implement policies and procedures to review all project activity and verify the amounts recorded for grants receivable and deferred inflows of resources, unavailable revenues, are accurate prior to the commencement of the audit. In addition, we recommend the District implement policies and procedures to ensure all grant revenues and expenditures are recorded in the fund that received the benefit

Views of responsible officials and planned corrective actions:

The city has procedures set up to review and ensure that each project and org is reconciled at the end of the year. Unfortunately, due to the large amount of grants, there were some that had activity posted to them after personnel had reconciled and these did not get reviewed again prior to audit. Staff is working on a schedule and posting access to ensure unauthorized or unreviewed entries are not allowed to back date into the prior fiscal year while staff works on reconciliation for audit.

Additionally, with the new American Rescue Plan Act (ARPA) revenue received in Fiscal Year 2021 and 2022, the city implemented a utility assistance plan to help those who fell behind on their residential water and sanitation payments as a result of COVID-19. Staff did not realize that this needed to be recorded in the appropriate enterprise accounts as revenue from other governments instead of treating it like a governmental grant for that program. Since all other ARPA programs to date are government related, this issue should not come up again. Staff has made note of this in the grant reconciliation procedures for any future grants as part of the audit review.

As part of the FY 23-24 budgeting process, the City's Executive Management Team will be requesting the addition of an Internal Auditor position to the Table of Organization to help to identify potential audit issues on an ongoing basis, prior to the external auditing process

Government Auditing Standards Letter
and Management Responses for the
Draft Victorville Water District
Financial Reports for Fiscal Year
Ended June 30, 2022

Victorville Water District

Schedule of Findings and Responses

June 30, 2022

2022-001

Material Weakness – Pension Amounts

Condition: The City's Miscellaneous, agent multiple-employer defined benefit pension plan administered by the California Public Employees' Retirement System (CalPERS), includes employees of the District. The City of Victorville allocates pension plan amounts to the District based on pension contributions for the year. Amounts recorded in the District's general ledger for the pension deferred outflows and inflows of resources and pension expense did not agree individually or in total to the CalPERS provided amounts and the City's calculated allocation.

Criteria or specific requirement: The pension deferred outflows and inflows of resources and pension expense should be recorded in the general ledger at amounts that agree to the CalPERS provided amounts for the miscellaneous defined benefit pension plan. The amounts allocated to the District should follow the City's historical policy for allocating such amounts, which is based on the current year CalPERS contributions by fund.

Effect: The pension deferred outflows and inflows of resources and pension expense were materially misstated, which resulted in an overall decrease to pension expense of approximately \$307 thousand, increase to deferred outflows of resources of approximately \$4.7 million and increase to deferred inflows of resources of approximately \$4.4 million.

Cause: The District made errors when generating the journal entry to record the pension deferred outflows and inflows of resources and pension expense.

Repeat Finding: This finding is a repeat of a finding in the immediately prior year.

Recommendation: We recommend the District implement policies and procedures to ensure the accurate recording of pension amounts in all funds.

Views of responsible officials and planned corrective actions:

With the additional staff added in FY21/22, there was insufficient training which took place and resulted in reconciliation errors in City amounts versus auditors' amounts. After meeting with the auditors to review the reconciliation steps and ending balances, it was determined a step was incorrectly omitted which caused the reconciliation to the incorrect table in the actuarial valuation and the City has since corrected the reconciliation processes. Implementation of a three-tier review process is now in place and additional staff will be properly trained in FY22/23 as part of our cross-training procedures.

As part of the FY 23-24 budgeting process, the City's Executive Management Team will be requesting the addition of an Internal Auditor position to the Table of Organization to help to identify potential audit issues on an ongoing basis, prior to the external auditing process.

2022-002

Material Weakness – Capital Assets

Condition: During our review of capital assets, we noted a construction in progress project that was cancelled and required expensing.

Criteria or specific requirement: When projects are cancelled and the asset is no longer usable, the project should be expensed.

Effect: The audit adjustment had a net impact to decrease capital assets and increase expenses by \$1.4 million.

Cause: The District did not sufficiently follow the year-end closing procedures to identify the above error.

Repeat Finding: This particular finding was not noted in the immediately prior year; however, findings related to audit adjustments for capital assets were noted in the immediately prior year.

Recommendation: We recommend the District implement policies and procedures to review capital assets at year-end for appropriate classification.

Views of responsible officials and planned corrective actions:

City personnel reconciling capital assets will review with departments at minimum twice a year as well as reviewing budget to actual for projects and notices of completion in city council agenda items to catch all completed projects. Additionally, staff will question departments regarding all projects residing in the Construction in Progress coding with no activity for at least four months to ensure that project is still continuing forward or if it needs to move to "Idle Assets" to be completed in the future or expensed if project has been discontinued and/or did not result in an asset.

As part of the FY 23-24 budgeting process, the City's Executive Management Team will be requesting the addition of an Internal Auditor position to the Table of Organization to help to identify potential audit issues on an ongoing basis, prior to the external auditing process

2022-003

Material Weakness – Grant Revenues and Expenses

Condition: The District received federal funds under the American Rescue Plan Act (ARPA) that were utilized for payment of past due utility bills resulting from the pandemic. The City recorded these amounts in a governmental fund instead of the District's enterprise fund that received the benefit.

Criteria or specific requirement: Grant revenues and expenses should be recorded in the fund that received the benefit.

Effect: This resulted in an audit adjustment of \$635 thousand to record revenues and expenses in the District.

Cause: The District recorded the cash received in the District's enterprise fund; however, all revenues and expenditures/expenses were recorded in a City governmental special revenue fund.

Repeat Finding: This finding is not a repeat finding.

Recommendation: We recommend the District implement policies and procedures to ensure all grant revenues and expenditures are recorded in the fund that received the benefit.

Views of responsible officials and planned corrective actions:

With the new American Rescue Plan Act (ARPA) revenue received in Fiscal Year 2021 and 2022, the city implemented a utility assistance plan to help those who fell behind on their residential water and sanitation payments as a result of COVID-19. Staff did not realize that this needed to be recorded in the appropriate enterprise accounts as revenue from other governments instead of treating it like a governmental grant for that program. Since all other ARPA programs to date are government related, this issue should not come up again. Staff has made note of this in the grant reconciliation procedures for any future grants as part of the audit review.

As part of the FY 23-24 budgeting process, the City's Executive Management Team will be requesting the addition of an Internal Auditor position to the Table of Organization to help to identify potential audit issues on an ongoing basis, prior to the external auditing process

Government Auditing Standards Letter
and Management Responses for the
Draft Southern California Logistics
Airport Authority Financial Reports for
Fiscal Year Ended June 30, 2022

SCLAA

Schedule of Findings and Responses

June 30, 2022

2022-001

Material Weakness – Pension Amounts

Condition: The City's Miscellaneous, agent multiple-employer defined benefit pension plan administered by the California Public Employees' Retirement System (CalPERS), includes employees of the SCLAA. The City of Victorville allocates pension plan amounts to the SCLAA based on pension contributions for the year. Amounts recorded in the SCLAA's general ledger for the pension deferred outflows and inflows of resources and pension expense did not agree individually or in total to the CalPERS provided amounts and the City's calculated allocation.

Criteria or specific requirement: The pension deferred outflows and inflows of resources and pension expense should be recorded in the general ledger at amounts that agree to the CalPERS provided amounts for the miscellaneous defined benefit pension plan. The amounts allocated to the SCLAA should follow the City's historical policy for allocating such amounts, which is based on the current year CalPERS contributions by fund.

Effect: The pension deferred outflows and inflows of resources and pension expense were materially misstated, which resulted in an overall decrease to pension expense of approximately \$56 thousand, increase to deferred outflows of resources of approximately \$1.2 million and increase to deferred inflows of resources of approximately \$1.2 million.

Cause: The SCLAA made errors when generating the journal entry to record the pension deferred outflows and inflows of resources and pension expense.

Repeat Finding: This finding is a repeat of a finding in the immediately prior year.

Recommendation: We recommend the SCLAA implement policies and procedures to ensure the accurate recording of pension amounts in all funds.

Views of responsible officials and planned corrective actions:

With the additional staff added in FY21/22, there was insufficient training which took place and resulted in reconciliation errors in City amounts versus auditors' amounts. After meeting with the auditors to review the reconciliation steps and ending balances, it was determined a step was incorrectly omitted which caused the reconciliation to the incorrect table in the actuarial valuation and the City has since corrected the reconciliation processes. Implementation of a three-tier review process is now in place and additional staff will be properly trained in FY22/23 as part of our cross-training procedures.

As part of the FY 23-24 budgeting process, the City's Executive Management Team will be requesting the addition of an Internal Auditor position to the Table of Organization to help to identify potential audit issues on an ongoing basis, prior to the external auditing process.

2022-002

Material Weakness – Capital Assets

Condition: During our review of capital assets, we noted (1) construction in progress projects that were complete and required reclassification to other capital asset categories and (2) restatements to beginning equity to record capital asset additions and corresponding accumulated depreciation to prior years. These corrections also resulted in a restatement to recognize the SCLAA's liability due to tenants for rental credits owed from tenant capital improvements made and contributed to SCLAA.

Criteria or specific requirement: When capital projects are complete and meet the SCLAA's capitalization policy, these projects should be moved to the appropriate asset category, such as infrastructure, and depreciated over the life of the asset. In addition, all expenses that meet the SCLAA's capitalization policy should be capitalized. Capital assets contributed from tenants should be recognized as capital contributions and a capital asset addition in the year the assets are contributed. Any corresponding liability due to tenants from donating these capital improvements should be recognized as the liability is incurred.

Effect: \$102 thousand was reclassified from construction in progress to infrastructure and total restatements resulted in a \$8.2 million increase to capital assets, \$201 thousand increase to accumulated depreciation, and a \$756 thousand liability for rental credits from tenant capital improvements made and contributed to the SCLAA.

Cause: The SCLAA did not sufficiently follow the year-end closing procedures to identify the above errors. In addition, the SCLAA did not review lease agreements for capital improvement and rental credit terms to consider the impact on the general ledger.

Repeat Finding: This particular finding was not noted in the immediately prior year; however, findings related to audit adjustments for capital assets were noted in the immediately prior year.

Recommendation: We recommend the SCLAA implement policies and procedures to review capital assets at year-end for appropriate classification and review leases for capital improvement and rental credit terms.

Views of responsible officials and planned corrective actions:

- (1) In performing reconciliation of the assets currently in the Construction in Progress (CIP) account as part of the review process, staff discovered an asset which had been completed in FY2020-21 but was still recorded as "CIP". Staff immediately capitalized the item and brought this to the attention of the supervisor who contacted auditors to make them aware.

- (2) With the implementation of GASB87, staff did not have procedures already in place to capture portions of a lease which had rental credits for tenant improvements to be completed. Staff has now incorporated this as part of the review of all new leases so any future lease agreements with embedded rental credits or other tenant improvement lease payment reductions are recognized as capital improvements when appropriate. Additionally, staff will discuss new leases with departments to ensure that any non-lease revenue is properly recorded.

As part of the FY 23-24 budgeting process, the City's Executive Management Team will be requesting the addition of an Internal Auditor position to the Table of Organization to help to identify potential audit issues on an ongoing basis, prior to the external auditing process

2022-003

Material Weakness – Grant Revenues and Receivables

Condition: The SCLAA had receivables recorded at year-end that had been received. Revenue was recorded a second time instead of reducing the receivable.

Criteria or specific requirement: Cash received for grants receivable should be applied to the receivable balance and should not be recorded a second time as revenue.

Effect: This resulted in audit adjustments that increased expenditures \$76 thousand, reduced receivables \$386 thousand and decreased revenue \$308 thousand.

Cause: The SCLAA recorded the cash received as revenue instead of a reduction to the receivable.

Repeat Finding: This finding is not a repeat finding.

Recommendation: We recommend the SCLAA implement policies and procedures to ensure that grant receipts are applied to receivable balances when appropriate.

Views of responsible officials and planned corrective actions:

As SCLAA is an enterprise fund, all revenue must be recognized when the expense is incurred so staff records the revenue to match the expense and debits an unearned revenue account. This account must be reversed at the start of the following year so as not to overstate the revenue when it comes in. Staff has revised the procedures for grant review to include this step for all enterprise grant accounts.

As part of the FY 23-24 budgeting process, the City's Executive Management Team will be requesting the addition of an Internal Auditor position to the Table of Organization to help to identify potential audit issues on an ongoing basis, prior to the external auditing process