

CITY OF FOUNTAIN VALLEY  
Fountain Valley, California

Single Audit Report on Federal Awards

Year ended June 30, 2012

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Single Audit Report on Federal Awards  
Year ended June 30, 2012

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City Council  
City of Fountain Valley, California

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

Independent Auditor's Report

We have audited the basic financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Fountain Valley as of and for the year ended June 30, 2012, which collectively comprise the City's basic financial statements and have issued our report thereon dated January 14, 2013. 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.

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 no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

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

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.

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Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above. However, we identified certain deficiencies in internal control over financial reporting, described in the accompanying Schedule of Findings and Questioned Costs as items 2012-01 and 2012-02 that we consider to be significant deficiencies in internal control over financial reporting. A significant deficiency is a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit the attention of those charged with governance.

The City's written responses to the significant deficiencies identified in our audit have not been subjected to the audit procedures applied in the audit of financial statements and, accordingly, we express no opinion on them.

We noted certain matters that we reported to management of the City in a separate letter dated January 14, 2013.

This report is intended solely for the information of the City Council, management of the City of Fountain Valley, federal awarding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

*Mayer Hoffman McCann P.C.*

Irvine, California  
January 14, 2013



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City Council  
City of Fountain Valley, California

**REPORT ON COMPLIANCE WITH REQUIREMENTS THAT COULD HAVE A  
DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM, INTERNAL  
CONTROL OVER COMPLIANCE AND ON THE SCHEDULE OF EXPENDITURES  
OF FEDERAL AWARDS IN ACCORDANCE WITH OMB CIRCULAR A-133**

Independent Auditor's Report

Compliance

We have audited the compliance of the City of Fountain Valley (the City), California, with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of the City's major federal programs for the year ended June 30, 2012. The City's major federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to its major federal program is the responsibility of the City's management. Our responsibility is to express an opinion on the City's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the City's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the City's compliance with those requirements.

In our opinion, the City of Fountain Valley complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2012.

Internal Control Over Compliance

The management of the City of Fountain Valley is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the City's internal control over compliance with requirements that could have a direct and material effect on a major federal program to determine the auditing procedures for the purpose of

expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the City's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A material weakness in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above. However, we identified certain deficiencies in internal control over compliance, described in the accompanying Schedule of Findings and Questioned Costs, as item 2012-03 that we consider to be a significant deficiency in internal control over compliance. A significant deficiency is a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit the attention of those charged with governance.

#### Schedule of Expenditures of Federal Awards

We have audited the financial statements of the governmental activities, business-type activities, each major fund, and the aggregate remaining fund information of the City of Fountain Valley as of and for the year ended June 30, 2012, and have issued our report thereon dated January 14, 2013. Our audit was performed for the purpose of forming our opinions on the financial statements that collectively comprise the City of Fountain Valley's basic financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain other procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of expenditures of federal awards is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

The City's written responses to the significant deficiencies identified in our audit have not been subjected to the audit procedures applied in the audit of financial statements and, accordingly, we express no opinion on them.

City Council  
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This report is intended for the information and use of the City Council, management of the City of Fountain Valley, federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

*Mayer Hoffman McCann P.C.*

Irvine, California  
March 7, 2013 except for the Schedule of Expenditures of Federal Awards as to which the date is  
January 14, 2013

CITY OF FOUNTAIN VALLEY  
Schedule of Expenditures of Federal Awards  
Year ended June 30, 2012

Federal Grantor/ Pass-Through Grantor <u>Program Title</u>	Federal Domestic Assistance <u>Number</u>	Program Identification <u>Number</u>	Federal Share of Program <u>Expenditures</u>	Payments to <u>Subrecipients</u>
<b>U.S. Department of Housing and Urban Development</b>				
Direct Assistance:				
Community Development Block Grant	14.218	B-11-MC-06-0550	\$ 384,234	47,463
<b>U.S. Department of Transportation</b>				
Passed-through the California Department of Transportation:				
Highway Planning and Construction	20.205	RPSTPLE-5341(029)	342,721	-
Highway Planning and Construction	20.205	RPSTPLE-5341(030)	408,767	-
Subtotal			<u>751,488</u>	<u>-</u>
<b>U.S. Department of Transportation</b>				
Direct Assistance:				
State and Community Highway Safety	20.600	PT1101	17,707	-
State and Community Highway Safety	20.600	20059	41,122	-
Passed-through the City of Anaheim:				
State and Community Highway Safety - Avoid The 26	20.608	AL1325	3,188	-
Subtotal			<u>62,017</u>	<u>-</u>
<b>U.S. Department of Energy</b>				
Direct Assistance:				
Energy Efficient Conservation Block Grant (ARRA)	81.128	SC0003377	502,202	-
<b>U.S. Department of Homeland Security</b>				
Passed-through California Emergency Management Agency:				
Hazard Mitigation Grant Program	97.039	FEMA 1810-DR-CA	25,435	-
Passed-through the County of Orange:				
Emergency Management Performance Grant	97.111	059-00000	8,630	-
Subtotal			<u>34,065</u>	<u>-</u>
Total			<u>\$ 1,734,006</u>	<u>47,463</u>

See accompanying Notes to the Schedule of Expenditures of Federal Awards.



CITY OF FOUNTAIN VALLEY

Notes to the Schedule of Expenditures of Federal Awards

Year ended June 30, 2012

(1) Summary of Significant Accounting Policies Applicable to the Schedule of Expenditures of Federal Awards

(a) Scope of Presentation

The accompanying schedule presents only the expenditures incurred by the City of Fountain Valley that are reimbursable under federal programs of federal awards. For the purposes of this schedule, federal awards include federal awards received directly from a federal agency, as well as federal funds received indirectly by the City from a non-federal agency or other organization. Only the portion of program expenditures reimbursable with such federal funds are reported in the accompanying schedule. Program expenditures in excess of the maximum federal reimbursement authorized or the portion of the program expenditures that were funded with state, local or other non-federal funds are excluded from the accompanying schedule.

(b) Basis of Accounting

The expenditures included in the accompanying schedule were reported on the modified accrual basis of accounting. Under the modified accrual basis of accounting, expenditures are recognized when the City becomes obligated for payment as a result of the receipt of the related goods and services. Expenditures reported include any property or equipment acquisitions incurred under the federal program.

(c) Subrecipients

During the fiscal year ended June 30, 2012, the City disbursed \$47,463 to subrecipients, utilizing funds provided by the U.S. Department of Housing and Urban Development Community Development Block Grant.

CITY OF FOUNTAIN VALLEY

Schedule of Findings and Questioned Costs

Year ended June 30, 2012

(A) Summary of Auditors' Results

1. An unqualified opinion was issued by the auditors on the financial statements of the auditee.
2. No material weaknesses in internal control over financial reporting with respect to the financial statements of the auditee were reported. However, there were two significant deficiencies in internal control over financial reporting with respect to the financial statements of the auditee that were reported.
3. The audit disclosed no noncompliance which is material to the financial statements of the auditee.
4. No material weaknesses and one significant deficiency in internal control over the major program of the auditee were reported.
5. An unqualified report was issued by the auditors on compliance for major programs.
6. The audit disclosed one audit finding required to be reported under paragraph .510(a) of OMB Circular A-133.
7. The major programs of the auditee were CFDA No. 14.218 Community Development Block Grant and CFDA No. 81.128 Energy Efficient Conservation Block Grant (ARRA).
8. The dollar threshold used to distinguish Type A and Type B programs was \$300,000.
9. The auditee did not meet the criteria to be classified as a low risk auditee for the year ended June 30, 2012 for purposes of major program determination.

(B) Findings Related to the Financial Statements which are Required to be Reported in Accordance with Generally Accepted Government Auditing Standards

(2012-01) Capital Asset Recordkeeping

During our audit, we noted the following errors in the capital asset records maintained by the City:

- Certain Water Fund projects were not moved out of construction in progress when completed
- A sewer improvement project was not capitalized
- There were errors noted in the depreciation calculations due to the lack of detail in the Water Fund records

CITY OF FOUNTAIN VALLEY

Schedule of Findings and Questioned Costs

Year ended June 30, 2012

(Continued)

(2012-01) Capital Asset Recordkeeping (continued)

Recommendation

We recommend that the City carefully evaluate project expenditures each year to determine amounts to be capitalized. The City should also create a detailed listing of capital assets for the Water Fund which will assist in the accurate calculation of depreciation.

Management's Comments Regarding Corrective Action Planned

A key position within the department has been unfilled for several years; this position would be the lead on capital assets. The position has since been filled and updating and maintaining our fixed asset schedules will be a priority for this individual.

(2012-02) Accrued Utility Receivables

We noted errors in the recording of utility receivables. One error was caused by an incorrect meter reading that resulted in an inflation of water consumed by a governmental agency. The error was detected and corrected on the customer bill and in the accounting system. However, the report that was archived for retention purposes still had the incorrect information. The archive file was not replaced when the system was corrected. When the archived files were pulled for the purposes of manually creating the year end accrual, the incorrect report was used and this resulted in an overstatement in the manual accruals used for year end. We also noted that certain bills related to the fiscal year ended June 30, 2012 were billed but not recorded as receivables prior to the start of the audit.

Recommendation

We recommend that the Customer Service and Finance departments reconcile the utility billing module to the general ledger to ensure that receivables are properly accrued prior to the start of the audit.

Management's Comments Regarding Corrective Action Planned

This is the first time an error of this type has been made and procedures will be put into place to ensure that reports that are archived are the final reports. The employee generating the reports will go back into the archived files once the billing process is complete and confirm that all reports within the archive are correct.

CITY OF FOUNTAIN VALLEY

Schedule of Findings and Questioned Costs

Year ended June 30, 2012

(Continued)

(C) Findings and Questioned Costs for Federal Awards.

(2012-03) Procedures Associated With Payroll Charges to Federal Programs

Federal Agency: U.S. Department of Housing and Urban Development

CFDA No.: 14.218

Federal Award Program No.: B-11-MC-06-0550

Federal Award Year: 2012

Control Category: Allowable costs, payroll

Questioned Costs: \$0

Condition

During our testing of payroll costs recorded as CDBG grant expenditures, we noted that payroll costs are charged to federal programs were based on budgeted amounts.

Criteria

OMB Circular A-87 Appendix B §8(h)(4) provides that charges to Federal awards for salaries and wages be based on payrolls documented in accordance with generally accepted accounting principles. Also, OMB Circular A-87 Appendix B §8(h)(5) provides that employees who work on multiple activities should support their time with personnel activity reports or equivalent documentation that reflect an after-the-fact determination of actual time expended.

Cause

The City uses budgeted allocations to charge employee payroll expenses throughout different funds and federal programs during the fiscal year. The City has employed this methodology for numerous years and believes the allocations are accurate based on the City's knowledge and understanding of personnel activity in relation to federal program administration.

Effect

Although the budgeted amounts did not differ significantly from the actual costs incurred, this practice is not accepted by federal granting agencies and could result in the recording of charges that were different than the actual costs incurred.

CITY OF FOUNTAIN VALLEY

Schedule of Findings and Questioned Costs

Year ended June 30, 2012

(Continued)

(2012-03) Procedures Associated With Payroll Charges to Federal Programs (continued)

Recommendation

We recommend management require all employees charging their time to a federal grant indicate their actual time spent on the grant on their timecards. For employees who charge 100% of their time to a federal grant they should provide a signed certification at least semi-annually that all their tasks relate to the purpose of the federal grant.

Management's Response Regarding Corrective Action Taken or Planned

The City of Fountain Valley has received Community Development Block Grant (CDBG) funding since 1974 almost 40 years, in that time frame the City has become confident with calculating the amount of staff time needed to properly administer and manage various projects and activities funded with CDBG funds. CDBG regulations require annual planning of each project that is to be carried out during the year. For each activity an estimate of the amount of staff time needed to complete that activity is completed. The total amount of staff hours are then budgeted for the activity. Certain activities such as Administration and Public Services are limited by CDBG regulations to the amount of funding that can allocated. Administration is limited to 20% of the annual allocation and Public Services is limited to 15%.

In many cases the hours charged to CDBG related activities do not cover the actual time spent on the administration of the activities. An example would be the Public Service Agency Grant Program; this program budget is limited to 15% of the annual CDBG allocation. It has been a direction of the City Council to allocate the entire 15% of the allocation to local non-profit agencies to assist the low and moderate income City residents. The administration of this program must come from the general administration or other funding sources such as General Fund or Housing Authority. The CDBG Code Enforcement is similar, last year the Code Enforcement Officer processed 598 residential cases in CDBG designated areas which equaled 40% of her caseload while only 461 hours or 22% of her time was charged to CDBG. Over the last few years CDBG funding has been reduced. In response the amount of staff time has been reduced as well including the elimination of staff positions allocated to CDBG activities

Although the City would prefer to get a full cost recovery for the staff time in CDBG projects, the City recognizes the value of assisting its low and moderate income residents. The City is willing to leverage its CDBG funds with other funding sources to achieve its goals.

CITY OF FOUNTAIN VALLEY  
Summary Schedule of Prior Audit Findings  
Year ended June 30, 2012

(2011-1) Community Development Block Grant – Reporting

This comment has been resolved.