

**CITY OF SAN RAFAEL
MEMORANDUM ON INTERNAL CONTROL
AND
REQUIRED COMMUNICATIONS
FOR THE YEAR ENDED JUNE 30, 2014**

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**CITY OF SAN RAFAEL
MEMORANDUM ON INTERNAL CONTROL
AND
REQUIRED COMMUNICATIONS**

For The Year Ended June 30, 2014

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MEMORANDUM ON INTERNAL CONTROL

To the City Council of
the City of San Rafael, California

We have audited the basic financial statements of the City of San Rafael for the year ended June 30, 2014, and have issued our report thereon dated September 29, 2014. Our opinions on the basic financial statements and this report, insofar as they relate to San Rafael Sanitation District (District), are based solely on the report of other auditors. In planning and performing our audit of the basic financial statements of the City of San Rafael, 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 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.

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.

Our consideration of internal control was for the limited purpose described in the first 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. In addition, because of inherent limitations in internal control, including the possibility of management override of controls, misstatements due to error or fraud may occur and not be detected by such controls. Given the limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Included in the Schedule of Other Matters are recommendations not meeting the above definitions that we believe to be of potential benefit to the City.

This communication is intended solely for the information and use of management, City Council, others within the organization, and agencies and pass-through entities requiring compliance with *Government Auditing Standards*, and is not intended to be and should not be used by anyone other than these specified parties.

A handwritten signature in black ink that reads 'Maze & Associates' in a cursive, stylized font.

Pleasant Hill, California
September 29, 2014

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CITY OF SAN RAFAEL
MEMORANDUM ON INTERNAL CONTROL

SCHEDULE OF OTHER MATTERS

NEW GASB PRONOUNCEMENTS OR PRONOUNCEMENTS NOT YET EFFECTIVE

The following comment represents new pronouncements taking affect in fiscal year 2014-15. We have cited them here to keep you abreast of developments:

GASB 68 - Accounting and Financial Reporting for Pensions (an amendment of GASB 27)

This Statement will have material impact on the City's financial statements. The primary objective of this Statement is to improve accounting and financial reporting by state and local governments for pensions.

This Statement establishes standards for measuring and recognizing liabilities, deferred outflows of resources, and deferred inflows of resources, and expense/expenditures. For defined benefit pensions, this Statement identifies the methods and assumptions that should be used to project benefit payments, discount projected benefit payments to their actuarial present value, and attribute that present value to periods of employee service.

In financial statements prepared using the economic resources measurement focus and accrual basis of accounting, a single or agent employer that does not have a special funding situation is required to recognize a liability equal to the net pension liability. The net pension liability is required to be measured as of a date no earlier than the end of the employer's prior fiscal year (the measurement date), consistently applied from period to period.

Note disclosure and required supplementary information requirements about pensions also are addressed. Distinctions are made regarding the particular requirements for employers based on the number of employers whose employees are provided with pensions through the pension plan and whether pension obligations and pension plan assets are shared.

The following are the major impacts:

- This Statement requires the liability of employers and nonemployer contributing entities to employees for defined benefit pensions (**net pension liability**) to be measured as the portion of the present value of projected benefit payments to be provided through the pension plan to current active and inactive employees that is attributed to those employees' past periods of service (**total pension liability**), less the amount of the pension plan's **fiduciary net position**.
- Actuarial valuations of the total pension liability are required to be performed at least every two years, with more frequent valuations encouraged. If a valuation is not performed as of the measurement date, the total pension liability is required to be based on update procedures to roll forward amounts from an earlier actuarial valuation (performed as of a date no more than 30 months and 1 day prior to the employer's most recent year-end).
- The actuarial present value of projected benefit payments is required to be attributed to periods of employee service using the entry age actuarial cost method with each period's service cost determined as a level percentage of pay. The actuarial present value is required to be attributed for each employee individually, from the period when the employee first accrues pensions through the period when the employee retires.

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SCHEDULE OF OTHER MATTERS

GASB 69 – Government Combinations and Disposals of Government Operations

This Statement establishes accounting and financial reporting standards related to government combinations and disposals of government operations. As used in this Statement, the term *government combinations* includes a variety of transactions referred to as mergers, acquisitions, and transfers of operations.

GASB 71 - Pension Transition for Contributions Made Subsequent to the Measurement Date—an amendment of GASB Statement No. 68

The objective of this Statement is to address an issue regarding application of the transition provisions of Statement No. 68, Accounting and Financial Reporting for Pensions. The issue relates to amounts associated with contributions, if any, made by a state or local government employer or non-employer contributing entity to a defined benefit pension plan after the measurement date of the government's beginning net pension liability.

Statement 68 requires a state or local government employer (or non-employer contributing entity in a special funding situation) to recognize a net pension liability measured as of a date (the measurement date) no earlier than the end of its prior fiscal year. If a state or local government employer or non-employer contributing entity makes a contribution to a defined benefit pension plan between the measurement date of the reported net pension liability and the end of the government's reporting period, Statement 68 requires that the government recognize its contribution as a deferred outflow of resources. In addition, Statement 68 requires recognition of deferred outflows of resources and deferred inflows of resources for changes in the net pension liability of a state or local government employer or non-employer contributing entity that arise from other types of events. At transition to Statement 68, if it is not practical for an employer or non-employer contributing entity to determine the amounts of all deferred outflows of resources and deferred inflows of resources related to pensions, paragraph 137 of Statement 68 required that beginning balances for deferred outflows of resources and deferred inflows of resources not be reported.

Consequently, if it is not practical to determine the amounts of all deferred outflows of resources and deferred inflows of resources related to pensions, contributions made after the measurement date of the beginning net pension liability could not have been reported as deferred outflows of resources at transition. This could have resulted in a significant understatement of an employer or non-employer contributing entity's beginning net position and expense in the initial period of implementation.

This Statement amends paragraph 137 of Statement 68 to require that, at transition, a government recognize a beginning deferred outflow of resources for its pension contributions, if any, made subsequent to the measurement date of the beginning net pension liability. Statement 68, as amended, continues to require that beginning balances for other deferred outflows of resources and deferred inflows of resources related to pensions be reported at transition only if it is practical to determine all such amounts.

The provisions of this Statement are required to be applied simultaneously with the provisions of Statement 68.

**CITY OF SAN RAFAEL
MEMORANDUM ON INTERNAL CONTROL**

STATUS OF PRIOR YEAR SIGNIFICANT DEFICIENCIES

2013 - 1: Reconciliation of Worker's Compensation Claims Paid

Criteria: The City should ensure that workers' compensation claim-related payments are consistent with its claim files.

Condition: The City's workers' compensation claims are administered by a third-party administrator. The administrator processes claims payments on behalf of the City and sends the City a monthly activities report. While the City reconciles the worker's compensation bank account to checks issued, payments made out from the account are not compared to claim files.

Cause: Following staffing changes and reductions, the City ceased its review of payments initiated by the third-party administrator from the workers' compensation bank account.

Effect: Disbursements not authorized by the City could be made out from the account.

Recommendation: To ensure that only payments authorized by the City are made out from the workers' compensation bank account, the City should reconcile payments made to claim files. Alternately, the City can request a Service Organization Control (SCO) report from the third-party administrator. A SCO report provides information regarding the service organization's controls and effectiveness of the controls.

Management Response: The City's Human Resources Office will reconcile payments initiated by the third-party administrator from the workers' compensation bank account to the City's internal claim files on a quarterly basis.

Current Year Status: The claim files provided by the third party are now compared to and reconciled with the payments made from account each month.

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REQUIRED COMMUNICATIONS

September 29, 2014

To the City Council of
the City of San Rafael, California

We have audited the basic financial statements of the City of San Rafael for the year ended June 30, 2014. Professional standards require that we communicate to you the following information related to our audit under generally accepted auditing standards and, *Government Auditing Standards* and OMB Circular A-133.

Significant Audit Findings

Accounting Policies

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by the City of San Rafael are described in Note 1 to the financial statements. The following Governmental Accounting Standards Board (GASB) pronouncements became effective, but did not have a material effect on the financial statements:

GASB 66 – *Technical Corrections—2012—an amendment of GASB Statements No. 10 and No. 62*

GASB 70 -- *Accounting and Financial Reporting for Nonexchange Financial Guarantees*

The following pronouncements became effective, and required a format change in the financial statements and a restatement and certain nomenclature revisions in the footnotes accompanying the financial statements.

GASB 65 – *Items Previously Reported as Assets and Liabilities*

This Statement establishes accounting and financial reporting standards that reclassify certain items that were previously reported as assets and liabilities as deferred outflows of resources or deferred inflows of resources, and certain items that were previously reported as assets and liabilities recognizes as outflows of resources or inflows of resources.

This Statement also provides other financial reporting guidance related to the impact of the financial statement elements deferred outflows of resources and deferred inflows of resources, such as changes in the determination of the major fund calculations and limiting the use of the term *deferred* in financial statement presentations.

Statement No. 63 established the financial statement presentation for deferred inflows and deferred outflows, and Statement No. 65 makes other changes and defines certain transactions subject to this new presentation.

Unusual Transactions, Controversial or Emerging Areas

We noted no transactions entered into by the City during the 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.

Estimates

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 estimate(s) affecting the City's financial statements was (were):

- *Management's estimate of the depreciation:* is based on useful lives determined by management. These lives have been determined by management based on the expected useful life of assets as disclosed in Note 1. We evaluated the key factors and assumptions used to develop the depreciation estimate and determined that it is reasonable in relation to the basic financial statements taken as a whole.
- *Accrued compensated absences:* are estimated using accumulated unpaid leave hours and hourly pay rates in effect at the end of the fiscal year. We evaluated the key factors and assumptions used to develop the accrued compensated absences and determined that it is reasonable in relation to the basic financial statements taken as a whole.
- *Estimated Fair Value of Investments:* As of June 30, 2014, the primary government of the City, held approximately \$56 million of cash and investments, as measured by fair value. Fair value is essentially market pricing in effect as of June 30, 2014. These fair values are not required to be adjusted for changes in general market conditions occurring subsequent to June 30, 2014.

Disclosures

The financial statement disclosures are neutral, consistent, and clear.

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 clearly trivial, and communicate them to the appropriate level of management. Management has corrected all/certain such misstatements. In addition, none of the misstatements detected as a result of audit procedures and corrected by management were material, either individually or in the aggregate, to each opinion unit's financial statements taken as a whole.

Disagreements with Management

For purposes of this letter, a disagreement with management is 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 a management representation letter dated September 29, 2014.

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 governmental unit'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 Accompanying the 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.

With respect to the required supplementary information accompanying the financial statements, we applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We did not express an opinion nor provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

The Introductory and Statistical Sections included as part of the Comprehensive Annual Financial Report have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we did not express an opinion nor provide any assurance on them.

This information is intended solely for the use of 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,

Maze & Associates