

**CITY OF PEORIA, ARIZONA
COUNCIL COMMUNICATIONS**

CC: 10C
Amend No. _____

Date prepared: November 4, 2010

Council Meeting Date: December 7, 2010

TO: Carl Swenson, City Manager
THROUGH: Susan Thorpe, Deputy City Manager *ST*
FROM: Brent Mattingly, Chief Financial Officer *Bm*
SUBJECT: Fiscal Year 2010 Comprehensive Annual Financial Report, Single Audit, and Management Letter

RECOMMENDATION:

That Council receive and file the Comprehensive Annual Financial Report, Single Audit, and Management Letter for the fiscal year ended June 30, 2010.

SUMMARY:

We are pleased to submit to you the Comprehensive Annual Financial Report (CAFR) of the City of Peoria, Arizona for the fiscal year ended June 30, 2010. The report was prepared by the Finance Department. The basic financial statements, combining fund financial statements, related footnotes and other supplementary information have been examined by an independent firm of Certified Public Accountants, Heinfeld, Meech & Co., P.C., whose report is included within. The examination satisfies Article VI, Section 7, of the City Charter, which requires an annual audit of all accounts of the City by an independent certified public accountant. Additionally, the administration of Federal financial assistance received by the City directly from Federal agencies, or passed through to the City by the State of Arizona or other governmental entities during fiscal year 2010 was tested by Heinfeld, Meech & Co., P.C. for compliance with applicable laws and regulations.

Responsibility for the accuracy of the presented data and the completeness and fairness of the presentations, including all disclosures, rests with the City. We believe the data is accurate in all material respects and is presented in a manner which fairly sets forth the financial position and results of operations of the City. Furthermore, we believe that all disclosures necessary to enable the reader to gain an understanding of the City's financial activity have been included.

The CAFR is presented in three sections. An Introductory Section includes the table of contents, transmittal letter, principal officials and organization chart. The Financial

CITY CLERK USE ONLY:

- Consent Agenda
- Carry Over to Date: _____
- Approved
- Unfinished Business (Date heard previous: _____)
- New Business

ORD. # _____ RES. # _____
LCON# _____ LIC. # _____
Action Date: _____

Section includes the independent auditor's report, management's discussion and analysis highlighting significant aspects of financial operations during the fiscal year, the government-wide financial statements, the fund financial statements, including fund combining statements, and related notes and other supplementary information. The Statistical Section includes a number of tables of unaudited data depicting the financial history of the City, as well as demographic and other miscellaneous statistics, generally presented on a multi-year basis. As part of this agenda package, each City Council member received a copy of the Comprehensive Annual Financial Report for the fiscal year ended June 30, 2010.

These financial statements have been prepared in accordance with accounting standards generally accepted in the United States of America for local governments as prescribed by the Governmental Accounting Standards Board (GASB) and the American Institute of Certified Public Accountants (AICPA). Staff believes the CAFR meets the standards and requirements of the Governmental Accounting Standards Board in the presentation of financial data, exhibits, and footnote disclosures.

Additionally, the City is required to have an independent audit of Federal financial assistance received by the City from Federal agencies, or passed through to the City by the State of Arizona or other governmental entities during the fiscal year (the "Single Audit"). The standards governing Single Audit engagements require the independent auditor to report not only on the fair presentation of the financial statements, but also on the government's internal controls and compliance with legal requirements having a direct impact and material impact on major programs, with special emphasis on internal controls and compliance requirements involving the administration of major federal awards. The reports from Heinfeld, Meech & Co., P.C. are included in the City of Peoria, Arizona's separately issued Single Audit Report, copies of which have been provided to Council.

As part of the audit process, the auditors also prepare a management letter as a separate report. A copy of the management letter for the fiscal year ended June 30, 2010, is included with this agenda item. The management letter presents the auditor's comments and recommendations intended to improve the internal controls and operating efficiencies of the City. Staff responses to the auditor's recommendations are included in the body of the management letter.

ATTACHMENTS:

1. 2010 Comprehensive Annual Financial Report
2. 2010 Single Audit Report
3. 2010 Management Letter
4. 2010 SAS114 Letter

CONTACT:

Dan Leahy, Accounting Supervisor, x7023

**CITY OF PEORIA, ARIZONA
MANAGEMENT LETTER
YEAR ENDED JUNE 30, 2010**



HEINFELD, MEECH & CO., P.C.
CERTIFIED PUBLIC ACCOUNTANTS

3033 N. Central Avenue, Suite 300
Phoenix, Arizona 85012
Tel (602) 277-9449
Fax (602) 277-9297

Honorable Mayor and Members of the City Council
City of Peoria, Arizona

In planning and conducting our single audit of City of Peoria, Arizona for the year ended June 30, 2010, we performed the following as required by *Government Auditing Standards* (GAS) and Office of Management and Budget (OMB) Circular A-133:

- Considered the City's internal control over financial reporting,
- Tested internal controls over its major federal programs, and
- Tested compliance with certain provisions of laws, regulations, contracts, and grant agreements that could have a direct and material effect on the City's financial statements and major federal programs.

Any audit findings that are required to be reported by GAS and OMB Circular A-133 have been included in the City's Single Audit Reporting Package for the year ended June 30, 2010. Our audit disclosed internal control weaknesses and instances of noncompliance with laws, regulations, contracts, and grant agreements that did not meet that reporting criteria. Management should correct these deficiencies to ensure that it fulfills its responsibility to establish and maintain adequate internal controls and comply with laws, regulations, contracts, and grant agreements. Those audit findings and our related recommendations are briefly described in the accompanying summary.

This letter is intended solely for the information of City of Peoria, Arizona's Honorable Mayor, Members of the City Council and City management and is not intended to be and should not be used by anyone other than the specified party. However, this letter is a matter of public record, and its distribution is not limited.

We have already discussed these findings and suggestions with City personnel and we will be pleased to discuss them in further detail at your convenience, to perform any additional study of these matters, or to assist you in implementing the recommendations.

Sincerely,



HEINFELD, MEECH & CO., P.C.
Certified Public Accountants

October 15, 2010

**CITY OF PEORIA, ARIZONA
MANAGEMENT LETTER
YEAR ENDED JUNE 30, 2010**

FEDERAL COMPLIANCE

ARRA – Challenge Grant

For one of the three Section 1512 reports reviewed, the report was submitted online at www.federalreporting.gov two days late.

According to Section 1512 of the American Recovery and Reinvestment Act of 2009, all ARRA related reports are due no later than ten calendar days after each calendar quarter in which the City receives the assistance award funded in whole or in part.

Community Development Block Grant Cluster

For one of four quarterly cash transaction reports reviewed, the report was submitted to the U.S. Department of Housing and Urban Development (HUD) eight days past the 90 day deadline.

Federal cash transaction reports must be submitted to HUD no later than 90 days after the end of the program quarter.

Section 8 Housing Vouchers Program

The Public Housing Agency (PHA) did not have a depository agreement with its financial institution in the form required by HUD in effect for the entire fiscal year. The PHA entered into a depository agreement with their financial institution on April 14, 2010.

The PHA must enter into a depository agreement with its financial institution to serve as a safeguard for federal funds and provide third party rights to HUD.

PAYROLL

For one of 40 employees' payroll reviewed for a specific pay period, the employee (who was paid out of the General Fund) received a \$160 communication allowance during the pay period; however, the City could not provide documentation to support why the employee was paid that amount.

More care should be taken to maintain documentation that supports all amounts paid to employees.



City of Peoria

8401 West Monroe Street, Peoria, Arizona 85345

CITY OF PEORIA
MANAGEMENT LETTER
YEAR ENDED JUNE 30, 2010
CITY RESPONSES

FEDERAL COMPLIANCE

ARRA – Challenge Grant

Staff had interpreted the 10 day requirement to be 10 business days. We are now aware that it is 10 calendar days. Quarterly reporting deadlines have been scheduled on staff calendars to make sure all ARRA reports are filed within the required time frame. It should be noted that the Bureau of Reclamation accepted the report in question without negative comment to the City.

Community Development Block Grant Cluster

Quarterly reporting deadlines have been scheduled with the appropriate staff in order to meet the required reporting deadlines. It should be noted that HUD accepted the report with no question or comment.

Section 8 Housing Vouchers Program

The Public Housing Authority (PHA) did have a depository agreement in place, but it did not include all the interested parties. As part of a review of the PHA by HUD staff, they suggested the depository agreement be revised. The new depository agreement amenable to all HUD requirements was put in place in April 2010 so the issue is now resolved. A copy of the depository agreement is on file at the PHA.

PAYROLL

Documentation was provided to the auditors from the employee file approving the communication allowance based on the Council Policy. However, the documentation did not include the actual dollar amount of the allowance. According to Council Policy CP 2-4 the amount for communication allowances is set through the budget process. In the future when communication allowances are added or changed, the documentation for the file will include the dollar amount that is effective at the time of the entry. This could be included on the Personnel Action Form (PAF) or be an attachment from the Budget department indicating the approved amount. We will review personnel files to make sure allowances are documented.



HEINFELD, MEECH & CO., P.C.
CERTIFIED PUBLIC ACCOUNTANTS

3033 N. Central Avenue, Suite 300
Phoenix, Arizona 85012
Tel (602) 277-9449
Fax (602) 277-9297

November 17, 2010

To the Honorable Mayor and Members of the City Council
City of Peoria, Arizona

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of City of Peoria for the year ended June 30, 2010, and have issued our report thereon dated October 15, 2010. Professional standards require that we provide you with the following information related to our audit.

Our Responsibilities under Auditing Standards Generally Accepted in the United States of America, Government Auditing Standards, and OMB Circular A-133

As stated in our engagement letter our responsibility, as described by professional standards, is to express opinions about whether the financial statements prepared by management with your oversight are fairly presented, in all material respects, in conformity with accounting principles generally accepted in the United States of America. Our audit of the financial statements does not relieve you or management of your responsibilities.

In planning and performing our audit, we considered City of Peoria's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and not to provide assurance on the internal control over financial reporting. We also considered internal control over compliance with requirements that could have a direct and material effect on major federal programs in order to determine our 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.

As part of obtaining reasonable assurance about whether City of Peoria's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, 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. Also in accordance with OMB Circular A-133, we examined, on a test basis, evidence about City of Peoria's compliance with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* applicable to each of its major federal programs for the purpose of expressing an opinion on City of Peoria's compliance with those requirements. While our audit provides a reasonable basis for our opinion, it does not provide a legal determination of City of Peoria's compliance with those requirements.

Planned Scope and Timing of the Audit

We performed the audit according to the planned scope and timing previously communicated to you in our engagement letter and communicated to management throughout the planning and performance of the audit.

Qualitative Aspects of Accounting Practices

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by City of Peoria are described in Note 1 to the financial statements. Management has informed us there were no new accounting policies adopted during the year, nor were there any changes in the application of existing policies. We noted no transactions entered into by the City of Peoria during the year for which there is a lack of authoritative guidance or consensus. There are no significant transactions that have been recognized in the financial statements in a different period than when the transaction occurred.

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 disclosures in the financial statements are neutral, consistent, and clear.

Difficulties Encountered in Performing the Audit

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

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. During the course of the audit we did not identify any uncorrected misstatements and/or audit adjustments that we deemed to be material.

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 October 15, 2010.

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 of Peoria'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.

Responsibility for Fraud

It is important for both management and the Honorable Mayor and Members of the City Council to recognize their role in preventing, deterring, and detecting fraud. One common misconception is that the auditors are responsible for detecting fraud. Auditors are required to plan and perform an audit to obtain reasonable assurance that the financial statements do not include material misstatements caused by fraud. Unfortunately most frauds which occur in an organization do not meet this threshold.

The attached document is provided as a courtesy and provides some basic steps that should be taken to help prevent fraud from occurring in your organization. Some of these steps may already be in place, others may not. Not even the most well-designed internal controls or procedures can prevent and detect all forms of fraud. However, an awareness of fraud related factors, as well as the active involvement by management and the Honorable Mayor and Members of the City Council in setting the proper “tone at the top”, increases the likelihood that fraud will be prevented, deterred and detected.

The information in this letter is intended solely for the use of the Honorable Mayor and Members of the City Council and management of City of Peoria and is not intended to be and should not be used by anyone other than these specified parties.

Very truly yours,



HEINFELD, MEECH & CO., P.C.
Certified Public Accountants

Steps Management Should Take in Preventing the Occurrence of Fraud

First and foremost, acknowledge that fraud can and does occur – Fraud occurs in organizations often because management provides the perpetrator with a substantial amount of authority and a high degree of trust. Consequently, management performs limited or no review of the individual's work. Recognizing that fraud can occur in any organization, including your own, is the first step in prevention.

Clearly communicate to employees the behavior that is expected of them – Believe it or not, ignorance has been cited as a common cause of fraud. Some employees have been trained to commit fraudulent acts without knowing what they were doing, just assuming that "that's the way it's done".

Take strong action against employees who commit fraud – Call the police or other law enforcement agency and press charges. Failing to do so sends a message to other employees that management doesn't take fraud seriously.

Provide employees an opportunity to report the occurrence of fraud or other abuse anonymously – In a recent national survey, one in five employees said they were personally aware of the occurrence of fraud in the workplace. Eighty percent said they would be willing to report fraud if they did not have to identify themselves. Management can establish a fraud hotline, "suggestion boxes," or other means to enable employees to bring the occurrence of fraud to its attention without requiring employees to give their names.

Conduct your own activities on a high ethical level – Employees will follow the lead of the governing body and management, whether that lead is ethical or not. More than what is said or included in a policy manual, the actions of the governing body and management establish behavioral norms.

Be alert to changes in employee attitudes, behavior and lifestyles – Because of day-to-day contact, management is in the best position to observe the unusual – attitudes that are hostile or defensive toward management or the organization in general, changes in behavior that are inconsistent with employees' normal disposition or lifestyles that are not reasonable based on the employees' level of compensation. Matters that may be of particular concern include:

- Indications of dissatisfaction with compensation, or a lack of promotion
- Indications of gambling
- Indications of drug use or excessive use of alcohol
- Indications of financial distress
- Indications of severe stress

Steps Management Should Take in Preventing the Occurrence of Fraud

Perform thorough background checks on all new employees – Call former employers and educational institutions for verification of previous employment and education. Beware of "gaps" in employment or educational history. Consider obtaining a credit report (if authorized by the candidate) before employment.

Require uninterrupted vacations for all employees and establish a schedule of rotation of employee responsibilities – More than just good management, rotation of duties provides a strong disincentive to commit fraud. In addition, it provides an opportunity to discover fraud that has already occurred.

Establish a budget – The governing body/management should establish an operating budget and monitor actual results on a regular basis. Any significant variances should be investigated.

Monitor exception reports – Unprocessed transactions should be carefully examined for propriety. This includes revenues, expenses, purchasing and payroll transactions.

Control the mail –The mail should be picked up by an employee who has no responsibilities related to the handling or recording of deposits, accounts receivable records or revenues. All remittances should be directed to a post office box. Limiting access to the organization's mail is essential in preventing the unauthorized negotiation of cash receipts.

Control the bank statements – Similarly, the bank statements should be picked up by an employee who has no related responsibilities and delivered to the management or other person independent of the reconciliation process. This person should review the contents of the statements before they are reconciled. Specific items to be alert to include:

- Missing checks
- Checks issued out of sequence
- Unknown payees
- Checks that appear to have been altered
- Checks not signed by authorized signatories
- Other unusual items

Account for sequences – Whether it is checks, invoices, credit memoranda, receiving reports, shipping documents, or other pre-numbered items, all sequences should be accounted for. Voided documents should be defaced to prevent unauthorized use and retained to complete sequences.

Steps Management Should Take in Preventing the Occurrence of Fraud

Control general journal entries – Management should either make or personally review and approve all general journal entries. Supporting documentation should be reviewed before approving general journal entries. In particular, the following items should be investigated:

- Entries made to unrelated accounts
- Entries made to receivables or revenues at or near the close of a period
- Entries made by persons whose responsibilities are not consistent with the accounts being adjusted

Obtain reasonable fidelity bond coverage – If the unthinkable occurs, insurance coverage is the most likely means of recovery of amounts misappropriated. The amount of coverage should be reviewed periodically for adequacy.

Evaluate the internal control framework – Lastly, evaluate the internal control framework of your organization. One particular useful evaluation tool is available in the Committee of Sponsoring Organization's (COSO) guidance on internal control over financial reporting for smaller organizations. This guidance may be obtained through the AICPA's website at www.cpa2biz.com (product #990017).

© Audit Litigation, Training and Efficiency Consulting, Inc. 2008