

City Council of the
City of Palos Verdes Estates
Palos Verdes Estates, California

In planning and performing our audit of the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the City of Palos Verdes Estates, California (the City), as of and for the year ended June 30, 2017, in accordance with auditing standards generally accepted in the United States of America and *Government Auditing Standards*, 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.

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 material weaknesses. Given these 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. As discussed below, internal control and other operational matters are presented for your consideration. This letter does not affect our report dated January 17, 2018, on the financial statements of the City. Our comments and recommendations are intended to improve internal control or result in other operating efficiencies. Our comments along with our recommendations for improvement are summarized as follows:

Compliance with Investment Policy

Auditors' Comment and Recommendation

During our review of the City's Investment Policy (the Policy), we noted the following:

- Section 8 of the Policy requires that quarterly investment reports are prepared and rendered to the City Council and the City Manager within 30 days of the end of the quarter. We noted that the report for quarter ending December 31, 2017, was not submitted until February 14, 2018.

Compliance with Investment Policy (Continued)

Auditors' Comment and Recommendation Continued)

- Section 8 of the Policy requires that an annual report on the performance of the investment program and an update to the Policy be presented to the City Council. We noted that this reporting requirement was not adhered to for the 2015-2016 fiscal year nor was it adhered to for the 2016-2017 fiscal year.
- Section 9 of the Policy requires that the Policy shall be reviewed and adopted by resolution annually by the City Council. For the fiscal year 2016-2017, the Policy was not reviewed and adopted by resolution.

We recommend that the City establishes procedures to ensure compliance with the Policy.

Management's Response

For 2015-2016, due to the transition to a new Finance Director at the beginning of March 2016, the City Treasurer in coordination with the Finance Director combined the second quarter report and third quarter reports to allow the new Director time to review both reports.

Effective in March 2017, the City Council established an Investment Policy Advisory Committee comprised of two residents and the City Treasurer. The terms of the resident members began in July 2017. Also, in March 2017, voters of Palos Verdes Estates elected a new City Treasurer. Their first order of business at their first meeting on July 13, 2017 was to review and update the City Council's Investment Policy. The Committee's proposed revisions to the Investment Policy was approved by Resolution by the City Council on September 12, 2017. The Policy is calendared by the Investment Policy Advisory Committee and the City Council to be reviewed annually and approved concurrent with adoption of the City's annual operating budget.

Staff agrees with the comment noting that Quarterly Investment Report for December 2017 was submitted 14 beyond the standard established by the City's policy. The delay was due to staff vacancies and the use of temporary personnel in the Finance Department. With filling the vacant positions and long-term continuity, the Quarterly Investment Report will be completed in a timely manner. However, the Quarterly Investment Report contains interest earnings and changes in market value of investments that was continually provided throughout the year for public scrutiny.

Outstanding Checks

Auditors' Comment and Recommendation

During our testing of a bank reconciliation, we noted several checks that had been outstanding for more than one year, some dating as far back as 2012. We recommend that an outstanding checks listing be reviewed periodically to help determine why some checks remain outstanding for so long. Based on this investigation, the City can take the appropriate action with regard to these outstanding checks (i.e., void the check, void and reissue the check, or keep the check listed as outstanding). In addition, we recommend that the City considers adopting a policy for stale checks and implementing controls to ensure the policy is adhered to.

Outstanding Checks (Continued)

Management's Response

The amount of each check is immaterial. However, staff follows the recommendation of the auditor for keeping a list of outstanding checks. Due to staff vacancies and the use of temporary personnel in the Finance Department, and the immaterial amount of these checks, the Department's primary focus has been basic accounting and operations. With filling the position vacancies and the subsequent long-term continuity of personnel, staff will be incorporating a stale check policy within the broader framework of creating new accounting policies.

The table listed below includes the checks in question.

ACCOUNT	CHECK NUMBER	Year	CHK DATE	VENDOR NUMBER	VENDOR NAME	CLEARED	OUTSTANDING
10105	521690	2012	6/12/2012	CHA7	HEATHER CHAPMAN		45.00
							45.00
10105	523346	2013	4/9/2013	RIO01	RIO HONDO COLLEGE		9.20
							9.20
10105	118764	2014	11/15/2013		John Eberhard		0.87
10105	525713	2014	6/24/2014	PER10	PAULA PEREZ		50.00
							50.87
10105	525946	2015	8/12/2014	ROS01	ROSCO PRODUCTIONS		514.12
10105	526364	2015	10/28/2014	FRO01	MARK FRONTEROTTA		3.62
10105	526422	2015	10/28/2014	THO12	SANDRA THOMPSON		3.62
10105	526425	2015	10/28/2014	VAN12	STEVEN VAN SICKLEN		3.62
10105	526435	2015	10/28/2014	WRI01	WILLIAM WRIGHT		3.62
10105	526568	2015	11/25/2014	SOU20	SOUTH BAY ORTHOPAEDIC SPE		280.00
							808.60
					Total Dollars		\$ 913.67

Capitalization Policy

Auditors' Comment and Recommendation

Currently, the City does not have a formal capitalization policy that provides guidelines as to the formal treatment of certain assets and appropriate lives for depreciation purposes. However, there is a reference to the capitalization threshold in the City's procurement policy. To ensure uniform treatment of capital expenditures, we recommend that the City adopts a policy for capitalization of assets.

Management's Response

The Capitalization Policy is listed within the notes to the Comprehensive Annual Financial Report (CAFR) under Note 1; Summary of Significant Accounting Policies. With new staff that will be filling existing vacancies and their longevity in their positions, an Accounting Policy Manual will be developed to address this finding.

Capital Asset Inventory

Auditors' Comment and Recommendation

During our audit, we noted that the City has not performed a physical inventory of its capital asset in several years. To ensure capital assets on hand are correctly accounted for, we recommend that the City performs a physical inventory of its capital assets and uses the results to modify the subsidiary schedule, as necessary.

Management's Response

Staff agrees with this recommendation and will incorporate the recommendation into future work plans.

Interfund Balances

Auditors' Comment and Recommendation

During our testing of interfund transactions, we noted that balances due from the Special Projects Fund to the General Fund in the amount of \$28,331 have been carried over for several years and have not been reconciled. The amounts are immaterial; however, in order to provide accurate interfund balances, we recommend that the City reconciles all general ledger accounts, including interfund amounts, each year and adjusts the general ledger, as necessary.

Management's Response

Staff agrees with this recommendation and will incorporate the recommendation into future work plans.

Payroll Reports

Auditors' Comment and Recommendation

During our testing of payroll expenditures, we noted that the City does not currently reconcile the Quarterly Payroll Information Returns (Form 941) to the general ledger. A reconciliation of these returns is a critical process to ensure the completeness of the records and provide an understanding of the expenditures reported. We recommend that the City reconciles these returns to the general ledger before they are filed.

Management's Response

Staff agrees with this recommendation and will be incorporating a general ledger reconciliation to the Quarterly Payroll Information Returns (Form 941) with the filling of vacant positions to manage day-to-day work responsibilities.

City's Responses to Auditors' Comments and Recommendations

The City's responses to the comments and recommendations identified in our audit are described above. The City's responses were not subjected to the auditing procedures applied in the audit of the financial statements, and accordingly, we express no opinion on them.

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

White Nelson Dick Evans LLP

Irvine, California
January 17, 2018