

CITY OF VICTORVILLE
Victorville, California

Single Audit Report on Federal Awards

Year ended June 30, 2016

CITY OF VICTORVILLE

Single Audit Report on Federal Awards

Year ended June 30, 2016

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Honorable Mayor and City Council
City of Victorville
Victorville, California

**Report on Internal Control Over Financial Reporting and on Compliance and Other
Matters Based on an Audit of Financial Statements Performed in Accordance With
*Government Auditing Standards***

Independent Auditor's Report

We have audited, in accordance with the 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, the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Victorville, California (the City), as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise the City's basic financial statements, and have issued our report thereon dated December 22, 2016.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the City's internal control over financial reporting (internal control) to determine the audit 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 entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is defined to be 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 of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. 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. We did identify certain deficiencies in internal control, described in the accompanying schedule of findings and questioned costs as 2016-01, 2016-02, 2016-03, 2016-04, 2016-05, and 2016-06 that we consider to be significant deficiencies.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City's financial statements are free from 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 an instance of noncompliance or other matters that are required to be reported under Government Auditing Standards which is identified as 2016-07 in the schedule of findings and questioned costs.

City's Responses to Findings

The City's response to the findings identified in our audit are described in the accompanying schedule of findings and questioned costs. The City's response was not subjected to the auditing procedures applied in the audit of the financial statements and accordingly we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

A handwritten signature in blue ink that reads "Davis Fan" followed by a stylized flourish.

Irvine, California
December 22, 2016

Honorable Mayor and City Council
City of Victorville
Victorville, California

Report on Compliance For Each Major Federal Program; Report on Internal Control Over Compliance; and Report on the Schedule of Expenditures of Federal Awards Required by the Uniform Guidance

Independent Auditor's Report

Report on Compliance for Each Major Federal Program

We have audited the City of Victorville's compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on each of City's major federal programs for the year ended June 30, 2016. The City's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the City's major federal programs based on our audit of the types of compliance requirements referred to above. 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 the audit requirement of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Those standards and the Uniform Guidance 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 on compliance for the major federal program. However, our audit does not provide a legal determination City's compliance.

Opinion on the Major Federal Programs

In our opinion, the City of Victorville complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on the major federal program for the year ended June 30, 2016.

Report on Internal Control Over Compliance

Management of the City of Victorville is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the City's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with Uniform Guidance 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. *A significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance 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 compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

Report on Schedule of Expenditures of Federal Awards Required by Uniform Guidance

We have audited the financial statements of the City of Victorville as of and for the year ended June 30, 2016, and have issued our report thereon dated December 22, 2016, which contained an unmodified opinion on those financial statements. Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by the Uniform Guidance and is not a required part of the 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 financial statements and certain additional 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 expenditure of federal awards is fairly stated in all material respects in relation to the financial statements as a whole.

A handwritten signature in blue ink that reads "Davis Fan UP". The signature is written in a cursive, flowing style.

Irvine, California
February 7, 2017, except for the Schedule of Expenditures of Federal Awards, as to which the date is December 22, 2016

CITY OF VICTORVILLE
Schedule of Expenditures of Federal Awards
Year Ended June 30, 2016

Federal Grantor/Pass-through Grantor/Program Title	Program Identification Number	Federal Domestic Assistance Number	Federal Financial Assistance Expenditures
<u>U.S. Department of Commerce</u>			
Direct assistance:			
Economic Development - Support for Planning Organizations	07-49-05916	11.302	\$ 767,158
Development Administration - Economic Adjustment Assistance	07-49-06560	11.307	932,008
Total - U.S. Department of Commerce			<u>1,699,166</u>
<u>U.S. Department of Housing and Urban Development</u>			
Direct assistance:			
Community Development Block Grant	*	14.218	1,106,609
Neighborhood Stabilization Program (NSP1 Loan Expenditures)	B08-MN-06-0523	14.218	209,569
Home Investment Partnerships Program	*	14.239	400,656
Neighborhood Stabilization Program (NSP3)	B11-MN-06-0523	14.218	96,223
Total - U.S. Department of Housing and Urban Development			<u>1,813,057</u>
<u>U.S. Department of Justice</u>			
Passed through the County of San Bernardino:			
Edward Byrne Memorial Justice Assistance Grant Program	2013-DJBX-0874	16.738	40,632
Edward Byrne Memorial Justice Assistance Grant Program	2012-DJBX-1013	16.738	23,688
Total - U.S. Department of Justice			<u>64,320</u>
<u>U.S. Department of Transportation</u>			
Direct Assistance:			
Federal Aviation Association:			
Airport Improvement Program	3-06-0359-21	20.106	3,813,051
Airport Improvement Program	3-06-0359-22	20.106	47,324
Airport Improvement Program	3-06-0359-23	20.106	764,408
Subtotal			<u>4,624,783</u>
Passed through the County of San Bernardino:			
Highway Planning and Construction:			
Bear Valley Road OH over BNSF Railroad	BHLS-5380(026)	20.205	171,676
Federal Transportation Improvement Program	HSIPL-5380(029)	20.205	333,860
Federal Demonstration/ Highway Planning	DEMO4L-5380(10)/(028)	20.205	858,096
Subtotal			<u>1,363,632</u>
Total - U.S. Department of Transportation			<u>5,988,415</u>
Total Expenditures of Federal Awards			<u>\$ 9,564,958</u>

* - Multiple projects

CITY OF VICTORVILLE

Notes to the Schedule of Expenditures of Federal Awards

Year ended June 30, 2015

(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 (and related awards received) by the City of Victorville, California ("City") that are reimbursable under federal programs of federal agencies providing financial assistance. For purposes of this schedule, financial assistance includes federal financial assistance received directly from a federal agency and federal funds received indirectly by the City from non-federal entities. Only the portion of program expenditures reimbursable with such federal funds is reported in the accompanying schedule. Program expenditures in excess of the maximum federal reimbursement authorized and the portion of program expenditures that were funded with other 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 or selected state program, as required by these agencies.

(c) Subrecipients

During the fiscal year ended June 30, 2016, the City of Victorville disbursed \$362,299 of federal awards to subrecipients under the Department of Housing and Urban Development - Community Development Block Grants/Entitlement Grants Program - CFDA No. 14.218.

CITY OF VICTORVILLE

Schedule of Findings and Questioned Costs

Year Ended June 30, 2016

Section I Summary of Auditor's Results

Financial Statements

- | | |
|---|------------|
| 1. Type of auditors' report issued on whether the financial statements audited were prepared in accordance with GAAP: | Unmodified |
| 2. Internal control over financial reporting: | |
| a. Material weakness(es) identified? | No |
| b. Significant deficiency(ies) identified? | Yes |
| 3. Noncompliance material to the financial statements noted? | Yes |

Federal Awards

- | | |
|--|---------------|
| 1. Internal control over major programs: | |
| a. Material weakness(es) identified? | No |
| b. Significant deficiency(ies) identified? | None Reported |
| 2. Type of auditors' report issued on compliance for major programs: | Unmodified |
| 3. Any audit findings disclosed that are required to be reported in accordance with 2 CFR 200.516 (a)? | No |
| 4. Identification of major programs: | |

CFDA Number

Name of Federal Program or Cluster

11.307
20.106

Economic Adjustment Assistance
Airport Improvement Program

- | | |
|---|-----------|
| 5. Dollar threshold used to distinguish between Type A and Type B programs: | \$750,000 |
| 6. Auditee qualified as a low-risk auditee? | No |

CITY OF VICTORVILLE

Schedule of Findings and Questioned Costs

Year ended June 30, 2016

Section II - Financial Statement Findings

2016-01 Water Assessment District Surplus Funds

During the year the City transferred \$311,522 of surplus assessment funds from the Water Assessment District 2R Agency Fund to the Water District in order to fund ongoing maintenance of the underlying assets of the particular Assessment District for which the related bonds were issued. The official statement of the bonds do not specify that the funds could be used for maintenance of the project and the City did not obtain a legal determination as to the allowability of the transfer and use for maintenance costs.

Recommendation

Per subsequent follow up with bond legal counsel, the surplus assessment funds can be used for other purposes "in amounts determined by the legislative body". Bond legal counsel recommended City Council approval prior to moving surplus funds. We recommend the City obtain consult with legal counsel prior to transferring excess Assessment District funds.

Management's Response

The Official Statement of the bonds approved by the Board of Directors of the Baldy Mesa Water District on January 19, 2006, states that the bonds were issued pursuant to the Refunding Act of 1984 for 1915 Improvement Act Bonds, being Division 11.5 of the California Streets and Highways Code. Section 9518 of Division 11.5 states "any surplus remaining in the improvement fund for the assessment district, after completion of the improvements and the payment of all claims, may be used as a credit upon the reassessment in the manner provided in Section 10427.1 or as otherwise provided in Section 10427." The City originally consulted with Willdan Financial Services for the proper way to handle the surplus assessment funds and Willdan referenced Section 10427. The transfer of the surplus funds was originally prepared based on the above references.

Bond legal counsel was consulted and it was determined that the surplus assessment funds could be used for maintenance for improvements funded by the district, as stated in the California Streets and Highways Code Section 10427(c). However, since this code states "in amounts determined by the legislative body", legal counsel suggested "it would be prudent for the City Council to approve the transfer." The entry to record the transfer of the surplus assessment funds was reversed and the transfer request is now on the agenda for City Council approval.

CITY OF VICTORVILLE

Schedule of Findings and Questioned Costs

Year ended June 30, 2016

2016-02 Golf Course Management Fee Payment

During the year ended June 30, 2016, the City made a payment of \$107,857 to the Green Tree Golf Course's management company for management fees from the period of July 1, 2014 to June 30, 2015. However, per review of the agreement between the management company and the City, the current agreement does not allow for the payment of a management fee for that period.

Recommendation

We recommend that the City review and make payments in accordance with the terms and conditions of the related contractual agreements with its vendors. Changes to contractual agreements should be approved and formalized prior to committing City funds for payment.

Management's Response

City staff is currently working with the City's attorney and Sierra Golf Management on the amended agreement.

2016-03 Developer Deposit Prior Year Adjustment

Prior to June 30, 2016, the City received a deposit of \$592,640 from a developer which was erroneously recorded as revenue. During the year ended June 30, 2016, the City identified the error and recorded it as developer deposit payable.

Recommendation

We recommend the City develop and implement procedures necessary ensure that all deposits received from developers are properly recorded as a deposit payable and not revenue.

Management's Response

This was a correction to fiscal year 2014 deposit payable. The City has been proactive in reviewing all deposits and revenue since then.

2016-04 Cost Allocation Plan Update

The City's annual cost allocation plan is based upon a study of expenditures from the fiscal year ended June 30, 2011. Given the changes in the size and structure of the City since that time, it is likely that the current allocable expenses are not consistent with the allocable expenses in 2011.

CITY OF VICTORVILLE

Schedule of Findings and Questioned Costs

Year ended June 30, 2016

Recommendation

We recommend that the City consider necessary efforts to ensure that the cost allocation plan properly reflects of the City's allocable expenses. The City should update the cost allocation plan to determine the proper allocations of administrative and other costs between City funds and departments.

Management's Response

The City has recently hired a consultant to perform the cost allocation plan. The new plan will be available by June 30, 2017.

2016-05 Auditor Detected Adjustments

Auditing standards require auditors to include as an internal control weakness material audit adjustments detected during the audit. For the year ended June 30, 2016, material adjustments detected by the audit process were as follows:

- An entry to correct the accrual of wages payable
- An entry to record a pollution remediation liability
- An entry to record additional claims payable
- An entry to transfer notes receivable from the Successor Agency to the City Housing Asset Successor Agency

Recommendation

An important element of controls over financial reporting is for management to identify adjustments necessary for financial statements to be fairly stated. Whenever possible, adjustments should be reflected in the accounting records prior to the start of the audit. When this is not possible, management should identify and communicate to the auditors the potential areas of adjustment that may need to be addressed during the audit process. This will help to reduce the risk of material misstatement.

Management's Comments Regarding Corrective Actions Planned or Taken

Finance staff has been trained and is aware of the adjustment to the year-end accrual wage payable. The entry to transfer notes receivable from the Successor Agency to the City Housing Asset Successor Agency was a correction entry to the reconciliation transfer as requested by the Department of Finance.

Both the pollution remediation liability and the claim payable were unresolved matters that required an attorney's letter. At the time of the audit, the claim payable was still in litigation and the information was only available from the City's attorney.

CITY OF VICTORVILLE

Schedule of Findings and Questioned Costs

Year ended June 30, 2016

2016-06 Interfund Advances

The City had a loan from the Southern California Logistics Airport Authority (SCLAA) to the Successor Agency to the Victorville Redevelopment Agency (Successor Agency) totaling \$10,278,395 which per the terms of the note were to be repaid on June 30, 2014. Due to revenue shortfalls the loans were not repaid as scheduled, and there were no amendments to the underlying promissory notes, extending the period of repayment.

Recommendation

We recommend that the City make scheduled interfund advance repayments in accordance with the terms of their related promissory notes or modify the agreements to reflect new terms.

Management's Comments Regarding Corrective Actions Planned or Taken

The above-referenced loans are subordinate to SCLAA debt service payments and tax increment revenue has been insufficient to make debt service payments. Therefore, such loan repayments cannot be made until sufficient revenue exists. Because the Successor Agency to the Victorville Redevelopment Agency is party to the loan agreements, a modification of the repayment terms is unlikely to be approved given the need for Oversight Board and State Department of Finance approval of such new terms. Ultimately, SCLAA will not be able to repay the loans until sufficient tax increment revenue exists.

2016-07 Pledge Revenues Shortfalls, Underfunded Reserves, and Bond Defaults

Because of recurring declines in assessed valuation in recent years, the Southern California Logistics Airport Authority (SCLAA) has received less tax increment revenue than was necessary to properly meet its debt obligations. As in prior years, during the fiscal year ended June 30, 2016, SCLAA-pledged revenues for bonded debt fell below the amounts required by bond covenants. Additionally, bond reserve accounts fell below the amounts required by bond covenants for Subordinate Tax Allocation Revenue Bonds (Series 2007, and Series 2008A).

In addition, on December 1, 2015, the SCLAA defaulted on the principal and interest payment, of \$1,715,961 for SCLAA Subordinate Tax Allocation Revenue Bonds, Series 2007 and the principal and interest payment of \$250,063 for SCLAA Subordinate Tax Allocation Revenue Bonds, Series 2008A. Also, on June 1, 2016, the SCLAA defaulted on the interest payment of \$1,155,961 for SCLAA Subordinate Tax Allocation Revenue Bonds, Series 2007 and the interest payment of 165,063 for SCLAA Subordinate Tax Allocation Revenue Bonds, Series 2008A. Finally, on December 1, 2016, the SCLAA defaulted on the principal and interest payment of \$1,745,961 for SCLAA Subordinate Tax Allocation Revenue Bonds, Series 2007 and the principal and interest payment of \$255,063 for SCLAA Subordinate Tax Allocation Revenue Bonds, Series 2008A.

CITY OF VICTORVILLE

Schedule of Findings and Questioned Costs

Year ended June 30, 2016

Recommendation

We recommend that the City continue its efforts to closely monitor and properly report insufficiencies of pledged revenues with the related impacts on the ability of the SCLAA to meet reserve requirements and annual debt service requirements with respect to airport authority bonds.

Management's Comments Regarding Corrective Actions Planned or Taken

There has been a significant decrease in the assessed value for the Victor Valley Redevelopment Project Area since Fiscal Year 2008-09, which has resulted in decreased tax increment revenue pledged for SCLAA debt service. SCLAA will continue to closely monitor and report insufficiencies of pledged revenues and reserve requirements; however, defaults will continue on current debt service payments for the two subordinate bond issues until sufficient tax increment revenue is received and all past due amounts are paid and reserves are replenished.

Section III - Findings and Questioned Costs for Federal Awards

There are no auditors' findings to be reported in accordance with section 200.516 of the Uniform Guidance.

CITY OF VICTORVILLE

Summary Schedule of Prior Audit Findings

Year ended June 30, 2016

Section IV – Summary of Prior Audit Findings and Current Status

2015-01 Adjusting Journal Entries

This item has been repeated as 2016-05 in the current year.

2015-02 Pledge Revenue Shortfalls, Underfunded Reserves, and Bond Defaults

This item has been repeated as 2016-07 in the current year.

2015-03 Housing Successor Agency Disclosure Requirements

This item has been resolved.