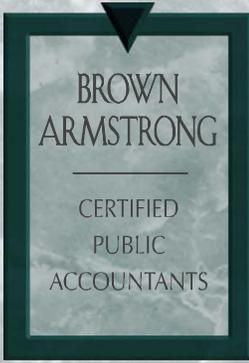


CITY OF MODESTO
SINGLE AUDIT REPORT
FOR THE YEAR ENDED JUNE 30, 2011

**CITY OF MODESTO
SINGLE AUDIT REPORT
FOR THE YEAR ENDED JUNE 30, 2011**

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BROWN ARMSTRONG

Certified Public Accountants

INDEPENDENT AUDITOR’S 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

The Honorable Mayor and City Council
of the City of Modesto, California

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We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Modesto, California (the City), as of and for the year ended June 30, 2011, which collectively comprise the City’s basic financial statements and have issued our report thereon dated February 28, 2012. 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.

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 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.

Our consideration of 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.

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*.

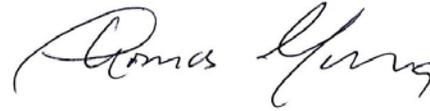


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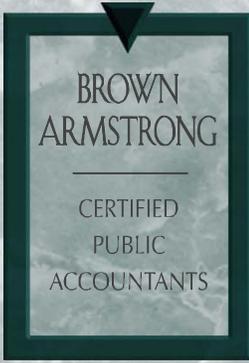
We noted certain matters that we reported to management of the City of Modesto in a separate letter dated February 28, 2012.

This report is intended solely for the information and use of management, City Council, others within the City, 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.

BROWN ARMSTRONG
ACCOUNTANCY CORPORATION

A handwritten signature in cursive script, appearing to read "Thomas Young".

Bakersfield, California
February 28, 2012



BROWN ARMSTRONG
Certified Public Accountants

**INDEPENDENT AUDITOR’S REPORT ON COMPLIANCE WITH
REQUIREMENTS THAT COULD HAVE A DIRECT AND MATERIAL EFFECT
ON EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER
COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133**

The Honorable Mayor and City Council
of the City of Modesto, California

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Compliance

We have audited the City of Modesto, California’s (the City) compliance with the types of compliance requirements described in the U.S. Office of Management and Budget (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, 2011. 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. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs 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 Agency’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 of the Agency’s compliance with those requirements.

In our opinion, the City 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, 2011.

Internal Control Over Compliance

Management of the City is responsible for establishing and maintaining effective internal control over compliance with the 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 the 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.



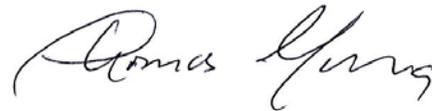
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Accounting Oversight Board and
MEMBER of the American Institute of
Certified Public Accountants

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.

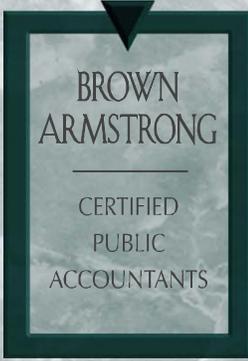
Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be *material weaknesses*, as defined above.

This report is intended solely for the information and use of management, City Council, others within the City, 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.

BROWN ARMSTRONG
ACCOUNTANCY CORPORATION

A handwritten signature in cursive script, appearing to read "Ronald Young".

Bakersfield, California
February 28, 2012



BROWN ARMSTRONG
Certified Public Accountants

**INDEPENDENT AUDITOR'S REPORT ON SUPPLEMENTARY
INFORMATION – SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**

The Honorable Mayor and City Council
of the City of Modesto, California

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Modesto, California (the City), as of and for the year ended June 30, 2011, which collectively comprise the City's basic financial statements, and have issued our report thereon dated February 28, 2012.

Our audit was performed for the purpose of forming opinions on the financial statements that collectively comprise the City's financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, 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 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 information is fairly stated in all material respects in relation to the financial statements as a whole.

This report is intended solely for the information and use of the City Council, audit committee and management of the City, as well as the City's 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.

BROWN ARMSTRONG
ACCOUNTANCY CORPORATION

Bakersfield, California
February 28, 2012



REGISTERED with the Public Company
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Certified Public Accountants

**CITY OF MODESTO
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2011**

Grantor Agency and Award Title	Identifying Pass-Through Grant Number	Federal Catalog Number	Program Expenditures
Department of Housing and Urban Development			
Community Development and Urban Development - NSP	B-08-MN-06-0004	14.218	\$ 1,741,620
Community Development and Urban Development	B-05-MC-060002	14.218	439,794
Community Development and Urban Development	B-06-MC-060002	14.218	243,470
Community Development and Urban Development	B-09-MC-060002	14.218	1,593,320
Community Development and Urban Development	B-10-MC-060002	14.218	223,179
Community Development and Urban Development	SC360080-11-04	14.218	23,826
Neighborhood Stabilization Program 3	B-11-MN-06-0004	14.253	2,103
ARRA Recovery Act - Comm Econ Development - CDBG_R	B-09-MY-060002	14.253	<u>376,510</u>
Program Subtotal			<u>4,643,822</u>
Department of Housing and Urban Development			
Emergency Shelter Grants Program	S-10-MC-060002	14.231	104,676
Emergency Shelter Grants Program	S-09-MC-060002	14.231	<u>4,556</u>
Program Subtotal			<u>109,232</u>
Department of Housing and Urban Development			
HOME Investment Partnership Grant	M-07-MC-060207	14.239	212,437
HOME Investment Partnership Grant	M-08-MC-060207	14.239	39,551
HOME Investment Partnership Grant	M-09-MC-060207	14.239	101,700
HOME Investment Partnership Grant	M-10-MC-060207	14.239	<u>145,455</u>
Program Subtotal			<u>499,143</u>
Department of Housing and Urban Development			
ARRA - Neighborhood Stabilization Program 2	B-09-LN-CA-0053	14.256 *	<u>11,188,209</u>
Department of Housing and Urban Development			
ARRA Recovery Act - Comm Econ Development - HPRP	S-09-MY-060002	14.257 *	<u>518,771</u>
United States Department of Justice			
COPS Technology Grant, 2006	2006-CK-WX-0133	16.710 *	335,241
ARRA - CHRP Grant	2009-RJ-WX-0022	16.710 *	<u>1,043,608</u>
Program Subtotal			<u>1,378,849</u>
United States Department of Justice			
County JAG DED 09/10	2009-DJ-BX-0232	16.738	7,009
ARRA Recovery Act - Byrne Memorial Justice Assistance Grant	2009-SB-B9-0405	16.804	<u>242,606</u>
Program Subtotal			<u>249,615</u>

* Denotes major program.

See accompanying notes to schedule of expenditures of federal awards and report on compliance with requirements applicable to each major program and internal control over compliance in accordance with OMB Circular A-133.

CITY OF MODESTO
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS (Continued)
FOR THE FISCAL YEAR ENDED JUNE 30, 2011

Grantor Agency and Award Title	Identifying Pass-Through Grant Number	Federal Catalog Number	Program Expenditures
United States Department of Transportation			
Airport Runway Safety	3-06-0153-32	20.106 *	6,410
ARFF Vehicle	3-06-0153-32	20.106 *	616,070
Airport Apron Rehab	3-06-0153-32	20.106 *	120
Planning Studies	3-06-0153-33	20.106 *	3,511
Airport Runway Safety	3-06-0153-34	20.106 *	318,999
Wind Cones	3-06-0153-34	20.106 *	4,721
Airport Apron Rehab	3-06-0153-34	20.106 *	199,554
Security Fence	3-06-0153-34	20.106 *	26,030
NW Apron	3-06-0153-34	20.106 *	61,320
Program Subtotal			<u>1,236,735</u>
United States Department of Transportation (Passed through California Department of Transportation)			
State Route 219	10-STA-219-PM 1.85	20.205 *	273,259
State Route 219	CML-5059(156)	20.205 *	30,030
Carpenter Road Bridge	BRLSZA-064	20.205 *	81,395
Roundabouts (3)	CML-133	20.205 *	500
RT Carp/State and Sisk Secondary	CML-134	20.205 *	385,679
T/S New Sisk/Vintage Faire and Claus Sylvan/Floyd/Lincoln	CML-138	20.205 *	40
Claus Road A/C Overlay	STPL-142	20.205 *	843,293
SR99 Pelandale Interchange	STPL-169	20.205 *	1,424,596
2010 Pavement Condition Survey	STPL-162	20.205 *	34,441
Sylvan Ave - Coffee/Oakdale PVMT Rehab	STPL-163	20.205 *	30,536
Oakdale Rd - Scenic/Sylvan PVMT Rehab	STPL-164	20.205 *	4,637
Right Turn LNS - 4 Intersections	CML-149	20.205 *	344,489
New Traffic Signals (2008)	CML-150	20.205 *	334,130
Rideshare Program	CML-151	20.205 *	39,157
Rideshare Program	CML-180	20.205 *	2,628
Conant Ave - Curbs and Gutters	CML-152	20.205 *	277,258
RGT Turn Lane Bangs and Prescott (New)	CML-176	20.205 *	25,040
Upgrade Traffic Signals 2010 (New)	CML-179	20.205 *	15,416
New Traffic Signals 2010 (New)	CML-178	20.205 *	21,040
Retime Downtown Traffic Signals 2010 (New)	CML-177	20.205 *	8,800
Roundabouts Hillglen	CML-5059(153)	20.205 *	130,489
N/B McHenry to E/B Briggsmore	CML-5059(168)	20.205 *	50,193
E/B Briggsmore to S/B McHenry	CML-5059(167)	20.205 *	28,610
Virginia Corridor - Phase V	HPLUL-5059(157)	20.205 *	1,249,106
Landscaping Briggsmore and SR99	SHOPP TEA	20.205 *	78,189
Caltrans 2010 Community Based Transportation Planning Grant	74A0554	20.205 *	6,963
Pelandale CCTV/Fiber Optics	CML-118	20.205 *	2,429
Rideshare Program	CML-140	20.205 *	2,343
ARRA - CAPE and Slurry seal	ESPL-5059(160)	20.205 *	1,576,366
ARRA - Overlay and ADA Curb Ramp	ESPL-5059(166)	20.205 *	594,843
Program Subtotal			<u>7,895,895</u>

* Denotes major program.

See accompanying notes to schedule of expenditures of federal awards and report on compliance with requirements applicable to each major program and internal control over compliance in accordance with OMB Circular A-133.

**CITY OF MODESTO
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS (Continued)
FOR THE FISCAL YEAR ENDED JUNE 30, 2011**

Grantor Agency and Award Title	Identifying Pass-Through Grant Number	Federal Catalog Number	Program Expenditures
United States Department of Transportation			
Federal Transit Agency			
Federal Transit Cluster			
Transit, Maintenance and Capital Purchases	CA-90-Y310	20.500 *	41,143
Transit, Maintenance and Capital Purchases	CA-90-Y487	20.500 *	109,557
Transit, Maintenance and Capital Purchases	CA-90-Y568	20.500 *	78,074
Transit, Maintenance and Capital Purchases	CA-90-Y680	20.500 *	624,963
Transit Capital Investment Grant	CA-03-0562	20.500 *	670,751
Transit, Maintenance and Capital Purchases	CA-04-0105	20.500 *	219,648
Transit, Maintenance and Capital Purchases	CA-04-0106	20.500 *	245,000
Transit, Maintenance and Capital Purchases	CA-95-X128	20.500 *	1,017,981
Transit, Maintenance and Capital Purchases	CA-90-Y870	20.500 *	95,242
Transit, Maintenance and Capital Purchases	CA-90-Y754	20.507 *	70,646
Transit, Maintenance and Capital Purchases	CA-90-Y393	20.507 *	71,485
ARRA - Transit, Maintenance and Capital Purchases	CA-96-X073	20.507 *	<u>2,373,594</u>
Program Subtotal			<u>5,618,084</u>
United States Department of Transportation			
(Passed through State of California Office of Traffic Safety)			
STEP Grant 2009-2010	PT1048	20.600	47,438
Sobriety Checkpoint Mini Grant 09/10	SC10262	20.600	24,782
Click or Ticket Mini Grant	CT10262	20.600	913
STEP Grant 2010-2011	PT1108	20.600	244,620
Sobriety Checkpoint Mini Grant	SC11262	20.600	13,841
Avoid the 12 - City of Turlock Fiduciary	AL0967	20.600	<u>89,566</u>
Program Subtotal			<u>421,160</u>
United States Department of Public Health			
ARRA - Wells 283 and 236 Blending	ARR09FP25	66.468 *	<u>663,013</u>
United States Department of Energy			
ARRA - PRN - HVAC Improvements (EECBG)	0628930 - SC0003034	81.128	163,821
ARRA - PRN - Install Foam Roof (EECBG)	0628930 - SC0003034	81.128	25,279
ARRA - PRN - Install Solar Panels (EECBG)	0628930 - SC0003034	81.128	21,673
ARRA - PRN - LED Street Lights Replacement (EECBG)	0628930 - SC0003034	81.128	23,767
ARRA - PRN - Modesto Centre Plaza Lighting (EECBG)	0628930 - SC0003034	81.128	<u>26,464</u>
Program Subtotal			<u>261,004</u>
FEMA			
Assistance to Firefighter Grant (2009)	EMW-2009-FR-00214	97.044	<u>324</u>
Total Expenditures of Federal Awards			<u>\$ 34,683,856</u>

* Denotes major program.

See accompanying notes to schedule of expenditures of federal awards and report on compliance with requirements applicable to each major program and internal control over compliance in accordance with OMB Circular A-133.

**CITY OF MODESTO
NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2011**

NOTE 1 – REPORTING ENTITY

The Schedule of Expenditure of Federal Awards (the Schedule) includes expenditures of federal awards for the City of Modesto, California, (the City) and its component units as disclosed in the Notes to the City's Basic Financial Statements.

NOTE 2 – BASIS OF ACCOUNTING

Basis of accounting refers to *when* revenues and expenditures or expenses are recognized in the accounts and reported in the financial statements, regardless of the measurement focus applied. All governmental funds and agency funds are accounted for using the modified accrual basis of accounting. All proprietary funds are accounted for using the accrual basis of accounting. Expenditures of Federal Awards reported on the Schedule are recognized when incurred.

NOTE 3 – DIRECT AND INDIRECT (PASS-THROUGH) FEDERAL AWARDS

Federal awards may be granted directly to the City by a federal granting agency or may be granted to other government agencies which pass-through federal awards to the City. The Schedule includes both of these types Federal award programs when they occur.

**CITY OF MODESTO
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2011**

SECTION I – SUMMARY OF AUDITOR’S RESULTS

Financial Statements

Type of auditor’s report issued: Unqualified

Internal control over financial reporting:

- Material weakness identified? Yes No
- Significant deficiencies identified that are not considered to be material weaknesses? Yes None Reported

Noncompliance material to financial statements noted? Yes No

Federal Awards

Type of auditor’s report issued on compliance for major programs: Unqualified

Internal control over major federal programs:

- Material weakness identified? Yes No
- Significant deficiencies identified that are not considered to be material weaknesses? Yes None reported

Any audit findings disclosed that are required to be reported in accordance with OMB Circular A-133, Section .510(a)? Yes No

Identification of major programs:

<u>CFDA #(s)</u>	<u>Name of Federal Program or Cluster</u>
14.256	ARRA – Neighborhood Stabilization Program 2
14.257	ARRA – Homeless Prevention and Rapid Re-Housing Program
16.710	ARRA – COPS Technology Grant
20.106	Airport Improvement Program
20.205	CalTrans Highway Planning Cluster, including ARRA Grants
20.500, 20.507	Federal Transit Cluster, including ARRA Grants
66.468	ARRA – Capitalization Grants for Drinking Water

The threshold for distinguishing type A and B programs was \$704,869.

Auditee qualified as low-risk auditee? Yes No

SECTION II – FINANCIAL STATEMENT FINDINGS

Our audit disclosed no current year findings required to be reported in accordance with *Government Auditing Standards*.

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

Our audit disclosed no current year findings and questioned costs required to be reported in accordance with Section .510(a) of OMB Circular A-133.

SECTION IV – STATUS OF PRIOR YEAR FINDINGS AND QUESTIONED COSTS

2010-01 – Water Use Tax

Condition

In accordance with Modesto Municipal Code Section 8-2.907 Water Use Tax, a tax is imposed upon every person in the City of Modesto (City), other than a water corporation, for usage of water which is delivered through mains or pipes at a rate of 6% of all water charges. During our testing of Utility Billings, it was discovered that not all residences selected for testing were being charged the 6% City tax on the water services. This tax should be assessed to all residences located within the City of Modesto city limits.

Recommendation

It appears that this problem is most apparent to those residences that existed and had water service prior to being annexed into the City. The Utility Billing staff relies on the Planning Department to relay the listing of those residences that are annexed into the City and need to have the Modesto tax charged. The effect of the condition is that the City of Modesto is losing additional tax revenue from all residences within city limits from not being charged the 6% tax for water services. We recommend that the City implement a policy or procedures that would ensure that all residences located in an annexed area are clearly communicated to the Utility Billing department. This would allow the department to verify that those residences are being charged the appropriate charges, including the City of Modesto tax for water services.

Management Response

Customer Services and IT performed an audit and found that 82 out of approximately 78,000 customer accounts were not being billed water tax since the system was set up in 2000. Out of these accounts, 6 were attributed to parcel annexations into the city limits. 76 accounts were primarily due to error when the accounts were originally set up. For the fiscal year 09/10, the revenue loss was approximately \$3,600. It is difficult to capture the exact fiscal impact for the prior years due to variances in rate increases, flat to metered rate changes, new homes, property vacancies, etc. Since inception, the estimated fiscal impact is less than \$30,000. Utility Billing has corrected this discrepancy and has implemented a procedure to assure this will not reoccur.

Current Year Status

Implemented.

2010-02 – Depreciation Expense

Condition

We noted during our testing over capital assets and the related depreciation expense that current year depreciation was being overstated, causing an overstatement of accumulated depreciation and understating capital assets, thus decreasing net assets. In the current and previous year, when Construction in Progress (CIP) projects were completed and transferred to a depreciable asset base such as improvements, the depreciation expense for the year was being calculated based on the original start date of the project, and not on the date when the project was completed and transferred out of the CIP asset base into a depreciable asset base. The capital asset system was then calculating incorrectly the depreciation to bring accumulated depreciation for that particular asset based on the straight-line method to where it should be had it been depreciated since the start date of the project rather than the transfer date. This led to multiple years of depreciation being calculated and expensed in the current year, rather than just for the first year of depreciation.

Recommendation

We recommend that management communicate and train staff on the importance of properly setting up fixed assets in the asset management software, so that depreciation is calculated properly and started based on the transfer date for CIP projects rather than on start date of the project.

Management Response

City staff is working with the current staff to ensure written procedures are documented to ensure capitalizing a completed project to an improvement has step by step instructions to ensure any new staff transitioning into this process has clear instructions on how to properly capitalize an asset and ensure depreciation is calculated correctly.

Current Year Status

Implemented.