

CITY OF SAN BERNARDINO
MUNICIPAL WATER DEPARTMENT

Single Audit Report on
Federal Awards

Year ended June 30, 2017

CITY OF SAN BERNARDINO MUNICIPAL WATER DEPARTMENT

Single Audit Report on Federal Awards

Year ended June 30, 2017

TABLE OF CONTENTS

	<u>Page</u>
Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>	1
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	3
Schedule of Expenditures of Federal Awards	6
Notes to the Schedule of Expenditures of Federal Awards	7
Schedule of Findings and Questioned Costs	9
Summary Schedule of Prior Audit Findings	12

City of San Bernardino Municipal Water Department
Board of Water Commissioners

**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 Auditors' 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, each major fund of the financial statements of the San Bernardino Municipal Water Department (Department), as of and for the year ended June 30, 2017, and the related notes to the financial statements, which collectively comprise the Department's basic financial statements, and have issued our report thereon dated December 21, 2017.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Department'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 Department's internal control. Accordingly, we do not express an opinion on the effectiveness of the Department'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 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 and therefore, material weaknesses or significant deficiencies may exist that were not identified. 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 a deficiency in internal control, described in the accompanying Schedule of Findings and Questioned Costs as item 2017-001 that we consider to be a significant deficiency in internal control over financial reporting.

Response to Findings

The Department's response to the finding identified in our audit is described in the accompanying Schedule of Findings and Questioned Costs. The Department'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.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Department'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 no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

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.



Irvine, California
December 21, 2017

City of San Bernardino Municipal Water Department
Board of Water Commissioners

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 Required by the Uniform Guidance

Independent Auditors' Report

Report on Compliance for Each Major Federal Program

We have audited the San Bernardino Municipal Water Department's (Department) compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on each of the Department's major federal programs for the year ended June 30, 2017. The Department'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 federal statutes, regulations, and the terms and conditions of its federal awards applicable to its federal programs.

Auditors' Responsibility

Our responsibility is to express an opinion on compliance for each of the Department'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 Department'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 each major federal program. However, our audit does not provide a legal determination of the Department's compliance.

Opinion on Each Major Federal Program

In our opinion, the Department complied, in all material respects, with the types of 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, 2017.

Report on Internal Control Over Compliance

Management of the Department 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 Department'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 the 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 Example Entity'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 Department as of and for the year ended June 30, 2017, and have issued our report thereon dated December 21, 2017 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.



Irvine, California
December 21, 2017

CITY OF SAN BERNARDINO MUNICIPAL WATER DEPARTMENT

Schedule of Expenditures of Federal Awards

Year ended June 30, 2017

<u>Federal Grantor/ Program Title</u>	<u>Federal Domestic Assistance Number</u>	<u>Program Identification Number</u>	<u>Program Expenditures</u>
United States Department of the Interior			
<u>Bureau of Reclamation</u>			
Water Reclamation and Reuse Program	15.504	R10AC35282	\$ <u>6,350</u>
Total			<u>6,350</u>
Environmental Protection Agency			
Superfund State, Political Subdivision, and Indian Tribe Site-Specific Cooperative Agreements	66.802	V-00T73801-5	<u>166,219</u>
Subtotal			<u>166,219</u>
CONSENT DECREE	66.000	#	
Operations and maintenance:			
Newmark			846,812
Muscoy			622,379
Site wide monitoring			99,805
Project management			<u>160,713</u>
Subtotal			<u>1,729,709</u>
Total Expenditures of Federal Awards			<u>\$ 1,902,278</u>

A PIN number has not been assigned

See accompanying notes to the schedule of expenditures of federal awards.

CITY OF SAN BERNARDINO MUNICIPAL WATER DEPARTMENT

Notes to the Schedule of Expenditures of Federal Awards

Year ended June 30, 2017

(1) Summary of Significant Accounting Policies Applicable to the Schedule of Expenditures of Federal Awards

(a) Scope of Presentation

The accompanying Schedule of Expenditures of Federal Awards (the "Schedule") includes the federal grant activity of the San Bernardino Municipal Water Department (the "SBMWD") under programs of the federal government for the year ended June 30, 2017. The information in this Schedule is presented in accordance with the requirements of the Uniform Guidance. Because the Schedule presents only a selected portion of the operations of the SBMWD, it is not intended to and does not present the financial position, changes in net position or cash flows of the SBMWD.

(b) Basis of Accounting

Expenditures reported on the Schedule are reported on the accrual basis of accounting. Such expenditures are recognized following the cost principles contained in the Uniform Guidance. Under the accrual basis of accounting, expenditures are recognized when incurred. Expenditures reported include any property or equipment acquisitions incurred under the federal program. SBMWD did not use the 10% de minimis indirect cost rate as covered in section 200.414 of the Uniform Guidance.

(c) Subrecipients

During the fiscal year ended June 30, 2017, there were no disbursements made to subrecipients.

(2) Background of Consent Decree

In 1996, the City of San Bernardino (City) filed a complaint against the United States of America, Department of the Army (Army) to recover damages, response costs and other available remedies relating to contamination alleged to have originated at a World War II Army installation known as Camp Ono. In March 2005, the United States Department Court, Central Department, entered judgment, in the form of a consent decree (Consent Decree), in the matter of City of San Bernardino v. United States of America. The consent decree settles the City's and the State's claims arising from the groundwater contamination allegedly caused by the Army. The Consent Decree contains a number of provisions obligating the City (through the Municipal Water Department) to operate and maintain the Newmark Groundwater Superfund site (Site). The Site consists of two operable units, the Newmark Operable Unit and the Muscoy Operable Unit. The Newmark Operable Unit was declared operational and functional in 1998.

CITY OF SAN BERNARDINO MUNICIPAL WATER DEPARTMENT

Notes to the Schedule of Expenditures of Federal Awards

Year ended June 30, 2017

(2) Background of Consent Decree, (Continued)

The Consent Decree provided for a payment of \$69 million from the Army to the City for performance of the work outlined in the consent decree. Upon entry of the Consent Decree, the City, through the Department, received title to all facilities constructed by the United States Environmental Protection Agency (EPA) for the Site and agreed to operate and maintain the groundwater extraction and treatment system for a period of 50 years. The \$69 million payment consisted of \$59 million for operation and maintenance and \$10 million for the construction of certain capital facilities that would be required in the future. The funds are subject to strict limitations, contained in the Consent Decree, as to how they may be spent.

Pursuant to the Consent Decree, \$10 million, including interest earned, has been set aside to be used only for (i) funding construction of treatment and directly related transmission systems that expanded the Department's capacity to deliver potable water, and (ii) funding work performed by the Department to complete construction of the Muscoy Operable Unit extraction system. These "capital facility" funds may not be used for costs incurred to operate, maintain, repair or retrofit components of the Site extraction or treatment systems constructed by EPA. In September 2007, the Muscoy Operable Unit was declared operational and functional.

CITY OF SAN BERNARDINO MUNICIPAL WATER DEPARTMENT

Schedule of Findings and Questioned Costs

Year ended June 30, 2017

Section I - Summary of Auditors' 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? | No |

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: | |
| <u>CFDA Number</u> | <u>Name of Federal Program or Cluster</u> |
| 66.000 | Environmental Protection Agency - Consent Decree |
| 5. Dollar threshold used to distinguish between Type A and Type B programs: | \$750,000 |
| 6. Auditee qualified as a low-risk auditee? | Yes |

CITY OF SAN BERNARDINO MUNICIPAL WATER DEPARTMENT

Schedule of Findings and Questioned Costs

Year ended June 30, 2017

Section II - Financial Statement Findings

(2017-001) Adjustments Detected During the Audit

Criteria

Auditing standards require that the auditor include in the report material adjustments detected by the audit process. A similar condition was noted in the prior year as Finding 2016-001.

Condition

Audit procedures detected account balances requiring adjustment.

Cause

During the year there was retirement and transition of key staff members within the Finance Department.

Effect

As a result of the audit process, we detected a number of adjusting journal entries. An entity's internal control plan should include adequate mitigating controls to prevent potential financial statement errors from becoming material.

Recommendation

To mitigate the risk of a material adjustment, we recommend the Department develop controls to prevent the likelihood of a misstatement occurring. Such controls may include a month end and year end closing checklist to ensure all adjustments are captured.

Views of Responsible Officials and Planned Corrective Actions

Management agrees and is working to establish procedures to ensure proper controls are in place in the future.

CITY OF SAN BERNARDINO MUNICIPAL WATER DEPARTMENT

Schedule of Findings and Questioned Costs

Year ended June 30, 2017

Section III - Federal Award Findings and Questioned Costs

There are no federal award findings and questioned costs.

CITY OF SAN BERNARDINO MUNICIPAL WATER DEPARTMENT

Summary Schedule of Prior Audit Findings

Year ended June 30, 2017

The following is the status of prior audit findings for the year ended June 30, 2016:

(2016-001) Adjustments Detected During the Audit

This finding has been repeated as finding 2017-001.