

**CITY OF COSTA MESA  
Costa Mesa, California**

**SINGLE AUDIT REPORT ON EXPENDITURES  
OF FEDERAL AWARDS**

**Year ended June 30, 2020**

**CITY OF COSTA MESA**  
**SINGLE AUDIT REPORT ON EXPENDITURES OF FEDERAL AWARDS**  
**Year ended June 30, 2020**

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**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**

The Honorable Mayor and City Council  
City of Costa Mesa, California

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, each major fund, and the aggregate remaining fund information of the City of Costa Mesa (the City), as of and for the year ended June 30, 2020, and the related notes to the financial statements, which collectively comprise the City of Costa Mesa's basic financial statements, and have issued our report thereon dated December 21, 2020.

**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 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 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 one deficiency in internal control, described in the accompanying schedule of findings and questioned costs as item 2020-001 that we consider to be a significant deficiency.

**Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the City of Costa Mesa'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*.

### **City's Response to Findings**

The City's response to the finding identified in our audit is noted in the accompanying schedule of findings and questioned costs. The 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 City of Costa Mesa'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 City'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 UP". The signature is written in a cursive, flowing style.

Irvine, California  
February 17, 2021

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

**Independent Auditor's Report**

The Honorable Mayor and City Council  
City of Costa Mesa, California

**Report on Compliance for Each Major Federal Program**

We have audited the City of Costa Mesa'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 the City of Costa Mesa's major federal programs for the year ended June 30, 2020. The City of Costa Mesa'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.

***Auditor's Responsibility***

Our responsibility is to express an opinion on compliance for each of the City of Costa Mesa'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 requirements 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 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 City of Costa Mesa'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 City of Costa Mesa's compliance.

***Opinion on Each Major Federal Program***

In our opinion, the City of Costa Mesa 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, 2020.

## **Report on Internal Control Over Compliance**

Management of the City of Costa Mesa 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 of Costa Mesa'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 of Costa Mesa'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 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 Costa Mesa as of and for the year ended June 30, 2020 and have issued our report thereon dated December 21, 2020 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 17, 2021 except for our report on the Schedule of Expenditures of Federal Awards, for which the date is December 21, 2020

**CITY OF COSTA MESA**  
**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**  
**Year Ended June 30, 2020**

Federal Grantor / Pass - Through Grantor / Program / Cluster Title	Catalog of Federal Domestic Assistance Number	Program Identification Number	Federal Expenditures	Amount Provided to Subrecipients
<b><u>United States Department of Housing and Urban Development</u></b>				
Direct Assistance:				
Community Development Block Grants (CDBG) Total CDBG Cluster	14.218	B-19-MC-06-0503	\$ 448,742	112,844
			<u>448,742</u>	<u>112,844</u>
HOME Investment Partnerships Program	14.239	M-12-MC-06-0507	8,150	-
	14.239	M-13-MC-06-0507	50,675	-
	14.239	M-14-MC-06-0507	53,013	-
	14.239	M-16-MC-06-0507	1,030	-
	14.239	M-18-MC-06-0507	18,830	-
		Program income	109,732	-
Total HOME Investment Partnerships Program			<u>241,430</u>	<u>-</u>
Total United States Department of Housing and Urban Development			<u>690,172</u>	<u>112,844</u>
<b><u>United States Department of Justice</u></b>				
Direct Assistance:				
Bulletproof Vest Partnership Total United States Department of Justice	16.607	n/a	9,828	-
			<u>9,828</u>	<u>-</u>
<b><u>United States Department of Treasury</u></b>				
Direct Assistance:				
Equitable Sharing	21.016	n/a	45,527	-
Passed through the County of Orange:				
COVID-19 Coronavirus Relief Fund	21.019	COVID-19-CARES Act Funding	995,615	-
COVID-19 Coronavirus Relief Fund (motels for homeless individuals)	21.019	COVID-19-CARES Act Funding	8,876	-
Total COVID-19 Coronavirus Relief Fund			<u>1,004,491</u>	<u>-</u>
Total United States Department of Treasury			<u>1,050,018</u>	<u>-</u>
<b><u>United States Department of Health and Human Services</u></b>				
Direct Assistance:				
Provider Relief Fund Total United States Department of Health and Human Services	93.498	n/a	45,616	-
			<u>45,616</u>	<u>-</u>
<b><u>United States Department of Homeland Security</u></b>				
Passed through the City of Los Angeles to the City of Anaheim:				
Prepare Communities for Complex Coordinated Terrorist Attacks	97.133	FAIN#DHS-16-NPD-133-00-01	13,300	-
Passed through the Governor's Office of Emergency Services:				
Fire Management Assistance Grant Total United States Department of Homeland Security	97.046	Cal OES-CAL FIRE-USFS -BLM-NPS-FWS-BIA	30,438	-
			<u>43,738</u>	<u>-</u>
<b><u>United States Department of Transportation</u></b>				
Passed through California Department of Transportation:				
Bicycle Racks at Public Locations	20.205	CML-5312(098)	23,262	-
Harbor Boulevard from 19th Street to Wilson Improvements	20.205	RPSTPLE-5312(099)	161,485	-
Fairview Road from Baker to Adams	20.205	HSIPL-5312(102)	1,499	-
Total Highway Planning and Construction Cluster			<u>186,246</u>	<u>-</u>
Passed through California Office of Traffic Safety:				
Minimum Penalties for Repeat Offenders for Driving While Intoxicated	20.608	PT1728	34,381	-
	20.608	PT18032	61,911	-
Total Minimum Penalties for Repeat Offenders for Driving While Intoxicated			<u>96,292</u>	<u>-</u>
Passed through California Office of Traffic Safety:				
State and Community Highway Safety	20.600	PT1728	1,729	-
State and Community Highway Safety	20.600	PT18032	68,530	-
Total Highway Safety Cluster			<u>70,259</u>	<u>-</u>
Total United States Department of Transportation			<u>352,797</u>	<u>-</u>
TOTAL EXPENDITURES OF FEDERAL AWARDS			<u>\$ 2,192,169</u>	<u>112,844</u>

See accompanying notes to schedule of expenditures of federal awards



**CITY OF COSTA MESA**

**NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**

**Year ended June 30, 2020**

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

(a) Basis of Presentation

The accompanying Schedule of Expenditures of Federal Awards (the "Schedule") includes the federal grant activity of the City of Costa Mesa (the City) under programs of the federal government for the year ended June 30, 2020. The information in this Schedule is presented in accordance with the requirements of Title 2 U.S. Code of Federal Regulations Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards. Because the Schedule presents only a selected portion of the operations of the City, it is not intended to and does not present the financial position, changes in net assets or cash flows of the City. The City did not use the 10% de minimis indirect cost rate as covered in section 200.414 of the Uniform Guidance.

(b) Summary of Significant Accounting Policies

Expenditures reported on the Schedule are reported on the modified-accrual basis of accounting for those grants that were recorded in governmental funds, and on the accrual basis of accounting for those grants that were recorded in proprietary funds. Such expenditures for part of the year are recognized following the cost principles contained in OMB Circular 87, Cost Principles for State, Local, and Indian Tribal Governments, and for part of the year contained in Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards wherein certain types of expenditures are not allowable or are limited as to reimbursement. Pass-through entity identifying numbers are presented where available.

(c) Subrecipients

For the fiscal year ended June 30, 2020, payments to subrecipients consisted of the following:

**Community Development Block Grant**

B-19-MC-06-0503	\$ 112,844
Total	\$ <u>112,844</u>

**CITY OF COSTA MESA**  
**SUMMARY OF FINDINGS AND QUESTIONED COSTS**  
**Year ended June 30, 2020**

**Section I – Summary of Auditor’s Results**

***Financial Statements:***

Type of auditor’s report issued:	Unmodified
Internal control over financial reporting:	
• Material weakness(es) identified?	No
• Significant deficiency(ies) identified not Considered to be material weaknesses?	Yes (2020-001)
Noncompliance material to financial statements noted?	No

***Federal Awards:***

Internal control over major programs:	
• Material weakness(es) identified?	No
• Significant deficiency(ies) identified not Considered to be material weaknesses?	None Reported
Type of auditor’s report issued on compliance for major programs:	Unmodified
Any audit findings disclosed that are required to be reported in accordance with Uniform Guidance?	No

Identification of major programs:

<b><u>CFDA Number(s)</u></b>	<b><u>Name of Federal Program or Cluster</u></b>
21.019	COVID – 19 Coronavirus Relief Fund

Dollar threshold used to distinguish between Type A and Type B programs:	\$750,000
Auditee qualified as a low-risk auditee?	Yes

**CITY OF COSTA MESA**  
**SUMMARY OF FINDINGS AND QUESTIONED COSTS**

**Year ended June 30, 2020**

**(Continued)**

**Section II – Findings Relating to the Basic Financial Statements Reported in Accordance with Government Auditing Standards**

**Reference Number: 2020-001**

***Financial Health and Deficit Fund Equity***

We noted certain deficit balances in the financial statements that warrant management’s attention. For the fiscal year ended June 30, 2020, the City reported a positive net position of \$21,765,850. However, after removing amounts that are restricted for specific purposes or invested in capital assets, the City reported a deficit unrestricted net position of (\$251,417,100). The unrestricted net position deficit is largely the result of the recent accounting standards that required the City to report net pension liabilities and total Other Post Employment Benefit (“OPEB”) liabilities. As of June 30, 2020, the City’s net pension liability and total OPEB liability were \$304,665,311 and \$58,917,480, respectively.

Recommendation

We recommend the City continue to evaluate solutions for improving the overall Unrestricted Net Position deficit caused by the pension and OPEB liabilities.

Management’s Comments Regarding Corrective Actions Planned

The City concurs with the auditor’s recommendation and continues to work on a funding plan to address the city-wide long-term obligations such as pensions and OPEB. The funding plan includes setting aside funds for a Section 115 pension trust; prepaying pension obligations annually, which saves the City approximately \$760,000; and depositing an additional \$500,000 annually towards the unfunded pension liability in the Fire Side Fund.

The City also strives to manage its pension liability through workforce recruitment. The City implemented tier 2 pension formulas for classic employees in addition to the Public Employees’ Pension Reform Act (PEPRA) formulas established statewide. These new formulas aim to reduce long-term pension liability as the City recruits new talents.

Fiscal year 2019-20 was a year filled with challenges, primarily brought on by the unprecedented COVID-19 pandemic. At the onset of the pandemic, the City Council and management quickly implemented a comprehensive cost containment plan to reduce significant operating expenses. The strong budgetary flexibility and leadership enabled the City to end fiscal year 2019-20 in balance without using reserve funds.

**CITY OF COSTA MESA**  
**SUMMARY OF FINDINGS AND QUESTIONED COSTS**

**Year ended June 30, 2020**

**(Continued)**

Furthermore, Standard and & Poor's (S&P) reaffirmed the City's lease revenue bonds AA+ rating in December 2020 based on a very strong and diverse economy, very strong management and financial practices, and strong liquidity and debt position. The City remains committed to address its long-term pension and OPEB obligations through its proven ability to manage the City's finance.

**Section III – Federal Award Findings and Questioned Costs**

None noted.

**CITY OF COSTA MESA**  
**STATUS OF PRIOR AUDIT FINDINGS**  
**Year ended June 30, 2020**

There were two findings reported in the Single Audit Report for fiscal year 2018-2019. The status of those findings is as follows:

**Reference Number: 2019-001**

***Financial Health and Deficit Fund Equity***

We noted certain deficit balances in the financial statements that warrant management's attention. For the fiscal year ended June 30, 2019, the City reported a positive net position of \$28,658,066. However, after removing amounts that are restricted for specific purposes or invested in capital assets, the City reported a deficit unrestricted net position of (\$241,478,263). The unrestricted net position deficit is largely the result of the recent accounting standards that required the City to report net pension liabilities and total Other Post Employment Benefit ("OPEB") liabilities. As of June 30, 2019, the City's net pension liability and total OPEB liability were \$295,591,759 and \$53,202,676, respectively.

We also noted that two of the City's Internal Service Funds did not have sufficient revenues to cover expenses during the year. The Self Insurance Worker's Compensation and General Liability Internal Service Fund expenses exceeded revenues by \$1,181,914 during the year which increased the fund deficit to (\$4,670,953) at June 30, 2019. The Equipment Replacement Fund expenses exceeded revenue by \$796,404 during the year which resulted in deficit cash and subsequent borrowing from other City funds.

Status

Unrestricted net position deficit as of the end of the year is (\$251,417,100), an increase in the deficit from the prior year. All of the internal service funds in the fiscal year ended June 30, 2020 had revenues that exceeded expenses. The finding has been repeated with modification as finding 2020-001.

**CITY OF COSTA MESA**  
**STATUS OF PRIOR AUDIT FINDINGS**

**Year ended June 30, 2020**

**(Continued)**

**Reference Number: 2019-002**

***Financial Accounting System***

The City's financial accounting system has not been substantially upgraded in a number of years and the current version of the system is no longer supported by the vendor. The current system properly records accounting information; however, it can be time intensive and costly to retrieve certain information from the system in a format that is useful for management.

Additionally, during our prior year audit, we performed a review of the City's information systems (IT) internal controls. Of the four specific recommendations we communicated in the prior year, two were fully addressed by the City and one was partially addressed. The City should continue making improvements in IT controls in the following areas:

- a) The City does not have documented policies and procedures over IT general controls, including access management, change management, and data backup.
- b) The City does perform periodic reviews of user accounts; however, we noted that a recent review had not been performed for financial system access, which would include remote access.

Status

This finding has been substantially resolved.