



CITY OF LONG BEACH AIRPORT

Schedules of Passenger Facility Charges

September 30, 2007

(With Independent Auditors' Report Thereon)

CITY OF LONG BEACH AIRPORT

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KPMG LLP
Suite 2000
355 South Grand Avenue
Los Angeles, CA 90071-1568

**Report on Compliance with Requirements Applicable to the
Passenger Facility Charge Program and on Internal Control
over Compliance and Schedules of Passenger Facility
Charges Collected and Expended and Interest Credited**

The Honorable Mayor and City Council
The City of Long Beach, California:

Compliance

We have audited the compliance of the City of Long Beach Airport Enterprise Fund (the Airport) with the compliance requirements described in the *Passenger Facility Charge Audit Guide for Public Agencies*, issued by the Federal Aviation Administration (the Guide), for its passenger facility charge program for the year ended September 30, 2007. Compliance with the requirements of laws and regulations applicable to its passenger facility charge program is the responsibility of the Airport's management. Our responsibility is to express an opinion on the Airport'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 the Guide. Those standards and the Guide 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 the passenger facility charge program occurred. An audit includes examining, on a test basis, evidence about the Airport's compliance with those requirements and performing such other procedures as we consider necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the Airport's compliance with those requirements.

In our opinion, the City of Long Beach Airport Enterprise Fund complied, in all material respects, with the requirements referred to above that are applicable to its passenger facility charge program for the year ended September 30, 2007.

Internal Control over Compliance

The management of the Airport is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws and regulations applicable to the passenger facility charge program. In planning and performing our audit, we considered the Airport's internal control over compliance with requirements that could have a direct and material effect on the passenger facility charge program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, 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 Airport's internal control over compliance.

A control deficiency in an entity's internal control over compliance 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 noncompliance with compliance requirements of a passenger facility charge program on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a passenger facility charge program such that there is more than a remote likelihood that noncompliance with compliance requirements of a passenger facility charge program that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with compliance requirements of a passenger facility charge program will not be prevented or detected by the entity's internal control.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the entity's internal control that might be 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.

Schedules of Expenditures of Passenger Facility Charges Collected and Expended and Interest Credited

We have audited the financial statements of the Airport as of and for the year ended September 30, 2007 and have issued our report thereon dated May 30, 2008. Our audit was conducted for the purpose of forming an opinion on the basic financial statements of the Airport taken as a whole. The accompanying schedules of passenger facility charges collected and expended and interest credited are presented for purposes of additional analysis as specified in the Guide and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

As described in note 1 to the schedules of passenger facility changes collected and expanded and interest credited, the schedules were prepared on the cash basis of accounting, which is a comprehensive basis of accounting other than U.S. generally accepted accounting principles.

This report is intended solely for the information and use of the City Council, management, and officials of the City of Long Beach, the U.S. Department of Transportation, the Federal Aviation Administration, and other 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.

KPMG LLP

August 11, 2008, except as to the Schedules
of Passenger Facility Charges Collected
and Expended and Interest Credited
which are as of May 30, 2008.



KPMG LLP
Suite 2000
355 South Grand Avenue
Los Angeles, CA 90071-1568

**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
The City of Long Beach, California:

We have audited the financial statements of the City of Long Beach Airport Enterprise Fund (the Airport) as of and for the year ended September 30, 2007, and have issued our report thereon dated May 30, 2008. 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 Airport's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing an opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Airport's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Airport's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency 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 misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with U.S. generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control over financial reporting. We consider the deficiencies described in the accompanying schedule of findings and responses as findings FS-07-01 through FS-07-03 to be significant deficiencies in internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control. Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we believe that none of the significant deficiencies described above are a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Airport'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*.

The Airport's response to the findings identified in our audit are described in the accompanying schedule of findings and responses. We did not audit the Airport's response, and accordingly, we express no opinion on it.

This report is intended solely for the information and use of the City Council, management, and officials of the City of Long Beach, the U.S. Department of Transportation, the Federal Aviation Administration, and other 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.

KPMG LLP

May 30, 2008

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Schedule of Passenger Facility Charges Collected and
Expended and Interest Credited

Amended Application 03-02-C-02-LGB

Year ended September 30, 2007

Passenger facility charges collected	\$ 3,654,541
Interest credited (note 2)	<u>178,632</u>
	3,833,173
Expenditures for passenger facility charge approved projects	<u>1,570,127</u>
Change in unexpended passenger facility charges	2,263,046
Unexpended passenger facility charges as of September 30, 2006	<u>2,955,284</u>
Unexpended passenger facility charges as of September 30, 2007	<u><u>\$ 5,218,330</u></u>

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Schedule of Passenger Facility Charges Collected and
Expended and Interest Credited

Application 06-03-C-00-LGB

Year ended September 30, 2007

Passenger facility charges collected	\$ —
Interest credited (note 2)	<u>—</u>
Expenditures for passenger facility charge approved projects	<u>1,661,911</u>
Change in passenger facility charges	(1,661,911)
Unexpended passenger facility charges as of September 30, 2006	<u>—</u>
Excess of passenger facility charges expended over charges collected as of September 30, 2007 (note 3)	<u><u>\$ (1,661,911)</u></u>

See accompanying notes to schedules of passenger facility charges collected and expended and interest credited and report on compliance with requirements applicable to the passenger facility charge program and on internal control over compliance and schedules of passenger facility charges collected and expended and interest credited.

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Schedule of Passenger Facility Charges Collected and Expended and Interest Credited

Amended Application 03-02-C-02-LGB

Quarters ended December 31, 2006, March 31, 2007, June 30, 2007, and September 30, 2007

	<u>December 31, 2006</u>	<u>March 31, 2007</u>	<u>June 30, 2007</u>	<u>September 30, 2007</u>	<u>Total</u>
Passenger facility charges collected	\$ 840,061	958,508	1,079,749	776,223	3,654,541
Interest credited	33,692	39,588	51,017	54,335	178,632
	<u>873,753</u>	<u>998,096</u>	<u>1,130,766</u>	<u>830,558</u>	<u>3,833,173</u>
Expenditures for passenger facility charge approved projects	332,575	500,593	389,868	347,091	1,570,127
Change in unexpended passenger facility charges	541,178	497,503	740,898	483,467	\$ <u>2,263,046</u>
Unexpended passenger facility charges at beginning of quarter	2,955,284	3,496,462	3,993,965	4,734,863	
Unexpended passenger facility charges at end of quarter	\$ <u>3,496,462</u>	<u>3,993,965</u>	<u>4,734,863</u>	<u>5,218,330</u>	

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Schedule of Passenger Facility Charges Collected and Expended and Interest Credited

Application 06-03-C-00-LGB

Quarters ended December 31, 2006, March 31, 2007, June 30, 2007, and September 30, 2007

	<u>December 31, 2006</u>	<u>March 31, 2007</u>	<u>June 30, 2007</u>	<u>September 30, 2007</u>	<u>Total</u>
Passenger facility charges collected	\$ —	—	—	—	—
Interest credited	—	—	—	—	—
Expenditures for passenger facility charge approved projects	143,722	456,287	204,865	857,037	1,661,911
Change in passenger facility charges	(143,722)	(456,287)	(204,865)	(857,037)	\$ <u>(1,661,911)</u>
Excess of passenger facility charges expended over charges collected at beginning of quarter (note 3)	—	(143,722)	(600,009)	(804,874)	
Excess of passenger facility charges expended over charges collected at end of quarter (note 3)	\$ <u>(143,722)</u>	<u>(600,009)</u>	<u>(804,874)</u>	<u>(1,661,911)</u>	

See accompanying notes to schedules of passenger facility charges collected and expended and interest credited and report on compliance with requirements applicable to the passenger facility charge program and on internal control over compliance and schedules of passenger facility charges collected and expended and interest credited.

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Notes to Schedules of Passenger Facility Charges Collected and Expended and Interest Credited

September 30, 2007

(1) Basis of Accounting

The schedules of passenger facility charges (PFC) collected and expended and interest credited are prepared on the basis of cash receipts and disbursements, as prescribed by Sections 9110 and 9111 of the Aviation Safety and Capacity Expansion Act of 1990, issued by the Federal Aviation Administration of the United States Department of Transportation, which is a comprehensive basis of accounting other than U.S. generally accepted accounting principles.

Passenger facility charges collected include amounts collected by the airlines and transferred to the City of Long Beach Airport. Expenditures for passenger facility charge approved projects are presented on a cash basis and include only the expenditures for approved PFC projects.

(2) Interest Credited

Interest credited represents interest income allocated to the PFC Program (Program) based on the ratio of the Program's unexpended passenger facility charges cash balance to the Airport's total cash and investments balance included in the pooled cash funds of the City of Long Beach.

(3) Amendment and New Application

On July 7, 2006, the Airport was given approval for additional collection authority, which amended the total PFC amount collected ending May 2017.

On September 14, 2006, the Airport was given approval for a new application with a charge-effective date of May 1, 2017 and a charge expiration date of December 1, 2018. The collection of passenger facility charges under Application 06-03-C-00-LGB will begin once amended Application 03-02-C-02-LGB expires.

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Schedule of Findings and Responses

September 30, 2007

I. Summary of Auditors' Results

- a. The type of report issued on the financial statements: **Unqualified opinion**
- b. Significant deficiencies in internal control were disclosed by the audit of the financial statements: **Yes**
- c. Material weakness: **None**
- d. Noncompliance which is material to the financial statements: **None**
- e. Significant deficiencies in internal control over the passenger facility charge program: **None Reported**
- f. Material weaknesses: **None**
- g. The type of report issued on compliance for the passenger facility charge program: **Unqualified opinion**
- h. Any audit findings: **None**

II. Findings Related to the Financial Statements Reported in Accordance with *Government Auditing Standards*

FS 07-01: Financial Reporting

Criteria

A significant deficiency in internal controls is the result of a deficiency in internal controls, or combination of deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with U.S. generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected. We believe the control deficiencies described below represent significant deficiencies in internal controls.

Condition and Context

The City of Long Beach (City) Airport does not have an effective process or controls in place to compile their financial statements and related disclosures in accordance with U.S. generally accepted accounting principle (GAAP). During our audit and review of the financial statements of the Airport, we noted errors in the presentation and disclosure of the financial statements. These include improper initial reporting and/or disclosure of the following:

- The Airport does not perform a formal evaluation to ensure that all non-GAAP policies are identified and quantified to ensure any related adjustments do not materially misstate the financial statements. During our audit we identified certain non-GAAP policies resulting in \$60,000 in adjustments.
- The Airport recorded capital assets acquired in the prior year during the current period. This resulted in an understated in depreciation expense in the prior year in the amount of \$47,000.

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- Omission of criteria according to GAAP in the capital assets rollforward for FY 2006 and FY 2007.
- Lack of disclosure related to the fair market value requirements of Government Accounting Standards Board No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Tools*, related to the Airport's cash and cash equivalents balances.

Cause

The Airport financial statements were not prepared by the Airport in previous years; however beginning fiscal year 2007, the responsibility for the compilation of these statements was transferred to the Airport.

Effect or Potential Effect

The current design of controls related to the recording of financial transactions may lead to certain instances of financial information that do not conform to GAAP.

Recommendation

We recommend that management refines its internal controls to ensure the preparation of financial statements in accordance with GAAP.

Views of Responsible Officials

The Airport has controls in place over the accounting and reporting process to ensure that the financial statements are presented in accordance with GAAP. With the Airport's review paralleling the external auditor's review, not all corrections are reconciled prior to the audit review due strictly to time constraints. The Airport is continually working to improving their accounting procedures.

For Fiscal year 2008, the Airport's accounting team will seek additional GASB and FASB training to ensure the integrity of the financial statements.

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Schedule of Findings and Responses

September 30, 2007

Findings FS-07-02 – Lack of Information Technology Policies and Procedures

Criteria

A significant deficiency in internal controls is the result of a deficiency in internal controls, or combination of deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with GAAP such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected. We believe the control deficiency described above represents a significant deficiency in internal controls.

Condition and Context

The Airport does not have formal Information Technology (IT) security and safeguarding policies and procedures. During our audit, we noted that the Airport has implemented procedures to address the issues surrounding information security, such as signing a confidentiality agreement upon commencing of employment. However, policies and procedures, while in existence and in practice for many years, are not formally documented.

Additionally, the Airport does not have formally documented policies and procedures related to systems and application change control. Based on our audit of the Human Resources System (Tesseract), we note that the system changes do follow an informal process and programming changes are documented into the program itself; however, formal documentation of appropriate approval, testing, and user acceptance is not always obtained. Based on our audit of FAMIS, the Fixed Asset Accounting System (FAACS), and the Advanced Purchasing and Inventory Control System (ADPICS), we note that system patches and bug fixes performed by the Financial Systems Officer in the Department of Financial Management do follow a formal process and programming changes are documented. However, changes made by the technology services programmers for other changes, such as modifying custom reports, follow an informal documentation process and appropriate approval, testing, and user acceptance are not always obtained.

Cause

The City centrally has policies and procedures over its information technology security, systems, and application change management. These policies and procedures were in full practice, however, were not consolidated into formal written manual until fiscal year 2008.

Effect or Potential Effect

Lack of documented information security policies and procedures weaken the IT general control environment. With regards to change management, once a system is operational, further changes to the system are usually required to meet the business developing needs. Such changes should be subjected to controls as stringent as those used in the development or implementation of a new system. If there is little or no control over system changes, the benefits originally gained by controlling the system's implementation may be lost as subsequent changes are made.

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Recommendation

We recommend that management formalize the current procedures into policies and develop standard IT security and safeguarding policies, such as:

- Information security infrastructure requirements
- Password-based access control
- Password protection
- Virus protection
- Internet website controls
- Standard network system configuration
- Network system administration
- Application security administration
- Firewall and router security
- Transmission of data/encryption
- Physical/perimeter security and data center protection

Additionally, we recommend that management develop and implement formal IT change management policies, standards, and related procedures associated with system (e.g., infrastructure and configuration change) and application change control. Management should ensure that the new developments are understood and communicated to all IT and supporting Airport personnel. Adequate formal change management procedures should be designed and implemented to ensure that changes to the key financial systems are made in a controlled manner. Specifically, we recommend that the following controls be implemented and enforced:

- All change requests should be formally authorized and documented by appropriate management and business owner;
- Appropriate change management software should be utilized for the Tesseract application to support the migration of programming changes to the live environment;
- Changes that are made to the IT systems are tested, validated, and approved prior to implementation into the production environment. Test criteria should be documented and applied for all testing. This is to ensure that the changes will meet the user requirements and that the changes will not have a negative impact on any of the existing;
- User acceptance sign-off should be obtained and maintained before changes are migrated to the production environment;
- Changes made to IT systems should be validated after promotion to production to confirm that the change did not impact the system functionality or data integrity and that unauthorized changes were not inadvertently or intentionally promoted;

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Schedule of Findings and Responses

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- Access to migrate changes into production should be segregated from the responsibilities of program development. Only a limited number of personnel should have access to migrate changes to the production environment to ensure that this process is well controlled and only tested, authorized, and properly approved changes are migrated into production;
- Change procedures also be applied to both system and application configuration settings (e.g., tolerance setting such as check authorization limits; three-way match; work flow flags to escalate for approval; and system configuration on hardware). Configuration settings are a key component of many information systems. Configuration settings frequently can impact the design and/or operating effectiveness of internal control over financial reporting;
- Emergency change provisions and controls are outlined to ensure that changes requiring immediate implementation are properly handled, allowing for timely change and no impact to systems and applications related to the financial reporting process; and
- Finally, we recommend that documentation of the activities above be maintained to strengthen the overall IT general control environment.

We recommend that these policies be formally communicated throughout the organization to users supporting and maintaining information systems and technology and are accessible and understandable to all persons. This ensures that management sets a clear direction and demonstrates support and commitment to information security through the issuance and maintenance of an information security policy. We recommend an annual review and update of the IT policies and procedures occur to integrate any new system, technology, and process improvements.

Views of Responsible Officials

In fiscal year 2008, the City's Technology Services Department formalized its various security procedures in a comprehensive information technology security policy to guide those supporting and maintaining information systems, as well as those using the systems. This security policy was approved by the City Manager on April 22, 2008. Also, in fiscal year 2008, the City's Technology Services Department formalized its various change management policies in a comprehensive information technology change management policy to guide those supporting and maintaining the City's software applications.

The City's formal policies and procedures ensure the proper safeguarding of:

- Information security infrastructure requirements
- Password-based access control
- Password protection
- Virus protection
- Internet website controls
- Standard network system configuration
- Network system administration
- Application security administration

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- Firewall and router security
- Transmission of data/encryption
- Physical/perimeter security and data center protection

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Findings FS-07-03 – Administrative Access – Inappropriate Administrative Access and Lack of Review over Appropriateness of User Access and Segregation of Duties within Certain Applications

Criteria

A significant deficiency in internal controls is the result of a deficiency in internal controls, or combination of deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with GAAP such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected. We believe the control deficiency described above represents a significant deficiency in internal controls.

Condition and Context

We noted two users with excessive administration access: a technical support officer and a system support specialist. In addition, management does not have a control in place to ensure proper segregation of duties within Software Configuration and Library Manager (SCLM). We noted several programmers have SCLM access to promote changes to production causing a segregation of duties conflict. Access to SCLM should be limited to two – three individuals independent of any programming responsibilities. Furthermore, management does not currently have controls in place to periodically review and document the appropriateness of user access to the related applications, administrative access to Active Directory, Resource Access Control Facility (RACF), and SCLM.

Cause

Technology Services' current level of application support staff has precluded segregation of duties between the test and production environments within the SCLM application. Since SCLM is a tool that is not utilized for the Airport's primary financial systems (FAMIS, ADPICS, BPREP, and FAACS), the lack of segregation of duties within the SCLM does not pose a significant internal control risk.

Effect or Potential Effect

Weaknesses in user access control may lead to situations where an employee has the ability to perpetrate an error or irregularity and to conceal the error or irregularity. Additionally, a lack of adequate security over user access in the business systems and improper segregation of duties can potentially expose the City to a variety of risks resulting from unauthorized manipulation of data as well as an unauthorized exercise of system functions.

Recommendation

We recommend that administrative access be restricted to users within the IT Department with a specific job need. Users with administrative access, making programming changes, and promoting those changes into production should be segregated. Periodic review of users with access to certain applications helps prevent unauthorized access. We recommend that the City implement a formal review, similar to the established procedures performed on the FAMIS system of administrative access to supporting applications, including Active Directory, SCLM, and RACF. Additionally, management should include the data center as part of the annual review or review data center access more frequently based on the rate of turnover. This review should be performed at least annually to ensure that inappropriate system access is detected and remediated. Similar to the FAMIS procedures, this review should be performed in

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Schedule of Findings and Responses

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conjunction with the IT Department and business owners. Evidence of review by business owners and the IT department should be documented, signed and dated, and maintained for audit purposes.

Views of Responsible Officials

The Technology Services Department applications support programming staff that have administrative access to systems use the access so they can move programming changes into the production environment. A policy change has been made to this process to require the technology services operation's staff to make all moves into production. New procedures for the operations organization have been developed. This is part of a larger change management control process that is being developed that at a high level, will include the following:

- Procedures that define the type of documentation needed for system changes;
- Approval required to process system changes;
- Appropriate testing (QA and user), and proof of testing;
- Appropriate signoff for each change prior to putting into production;
- Requirements for an internal TSD system that will track all change requests;
- Communication plan to business partners within the City notifying them of the internal change management system; and
- Deployment of the process to all systems maintained by TSD.

In addition, access to Active Directory, SCLM, and RACF will be reviewed, verified and documented annually.

III. Findings and Questioned Costs Related to the Passenger Facility Charge Program

- a. None