



MEMORANDUM

TO: CITY COUNCIL

FROM: DEBORAH MALICOAT, DIRECTOR OF ADMINISTRATIVE SERVICES

SUBJECT: CONSIDERATION OF ACCEPTANCE OF THE COMPREHENSIVE ANNUAL FINANCIAL REPORT

DATE: MAY 22, 2018

SUMMARY OF ACTION:

Receive and file the Comprehensive Annual Financial Report (CAFR) for the fiscal year ended June 30, 2017.

IMPACT ON FINANCIAL AND PERSONNEL RESOURCES:

Preparation of the City's financial reports requires approximately 200 hours per year of personnel resources and auditing services cost approximately \$20,000 annually.

RECOMMENDATION:

It is recommended the City Council receive and file the Comprehensive Annual Financial Report (CAFR) for the fiscal year ended June 30, 2017.

BACKGROUND:

On April 22, 2014, the City Council awarded an agreement for consultant services to Moss, Levy & Hartzheim, LLP to audit the City's financial records for the fiscal years ended June 30, 2014 through June 30, 2018. Audit services are retained for two reasons: first, to have an independent review of internal control; and secondly, to ensure that the resulting financial reports fairly represent the financial position of the City. Typically, the audited financial statements would be presented to the City Council by December 31, however due to other workload priorities the preparation of the CAFR was delayed this year.

ANALYSIS OF ISSUES:

Generally accepted accounting principles (GAAP) provide the criteria for judging whether a financial report is fairly presented. In defining the minimum standard of acceptable basic financial reporting for state and local governments, GAAP mandate a complete set of basic financial statements, including accompanying note disclosures, as well as the presentation of certain required supplementary information. GAAP

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encourages government agencies to present this information within the Comprehensive Annual Financial Report (CAFR).

The CAFR is a more detailed financial report beyond just the basic financial statements. It is made up of three basic sections:

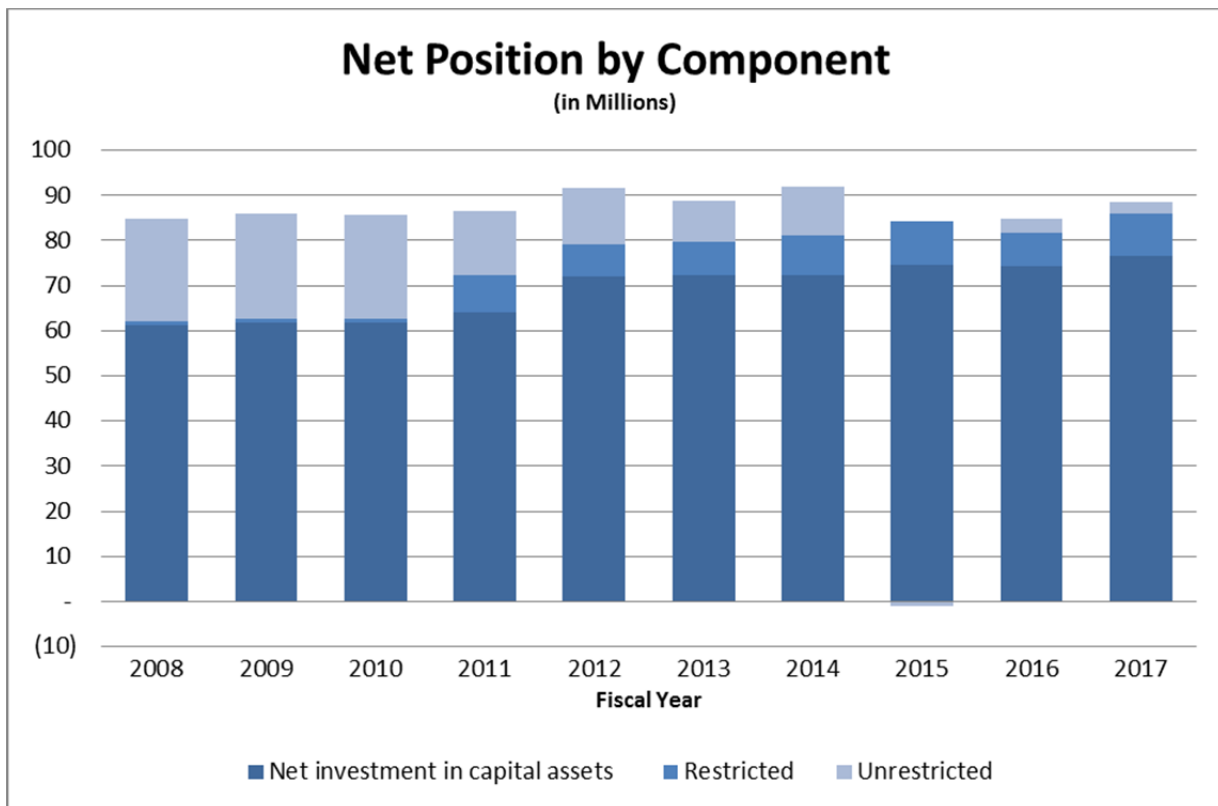
- The introductory section: provides general information of the City which includes the letter of transmittal, list of principal officials, and organizational chart.
- The financial section: provides the overall financial information of the City which includes the report of the independent auditor, management's discussion and analysis (a narrative of the City finances), the basic financial statements, required supplementary information and other supplementary schedules and statements.
- The statistical section: provides a broad range of operational, economic, and historical data that provides a context for assessing the City's economic condition. This section provides information about the City's general financial trends, revenue capacity, debt capacity, economic and demographic trends, and operating information.

The auditors conducted testing of internal controls in June and July 2017. The procedures for receiving and disbursing cash, the accounting methodology used to record transactions, the separation of duties to avert collusion, and asset securities were reviewed. As a result of this testing, there were no internal control issues/events noted.

In November 2017, an audit was conducted on net position of the City at June 30, 2017. Documentation in support of the assets, liabilities, and fund balance of all the funds in the City were examined and verified. This process assures an impartial review and substantiation of the City's net position. The result of this review is the City's CAFR.

The City's CAFR is in compliance with newly effective Government Accounting Standards Board (GASB) pronouncements, as detailed in the Notes to the Financial Statements.

As presented in the CAFR, the City's combined net position at June 30, 2017 increased by 4.5% from \$84.7 million to \$88.5 million. This increase is largely due to an increase in governmental activities, which includes activities in the General Fund, and a decrease in business-type activities, which represents water and wastewater activities.



Net position of all funds reflects all the assets and liabilities of the City. It includes the City’s investment in capital assets such as parks, bridges and roads as well as the liabilities or obligations to pay vendors, employees and debt service payments. The net position is the mathematical difference between assets and liabilities, but it doesn’t necessarily reflect the economic health of an organization. In the City’s case, about 90% of the total net position reflects capital assets. While these assets are important, they can’t be used to fund the day-to-day operations of the City and, therefore, may not be the most useful measure of the City’s liquidity. It may be more useful to compare unassigned fund balance to get a sense of the City’s ability to pay for ongoing operations. In the General Fund, this amount represents 39.3% of total expenditures, which exceeds the City’s reserve goal of 20%.

For financial reporting purposes, the additional ½ percent local sales tax revenue approved by voters in 2006 is combined with the General Fund. The combined funds, as shown in the table on the following page, reports revenues and other financing sources of \$17.9 million and expenditures and other financing uses of \$16.1 million. As a result, there was an increase to the fund balance of \$1.8 million during the 2016-17 fiscal year.

The General Fund’s total fund balance is \$7.8 million or approximately 48% of expenditures (including transfers out). However, some fund balances are considered nonspendable because it is held as inventory (\$7,497) or reflects prepaid items

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(\$1,063,503). Additionally, \$1,986,271 is designated for completing capital projects or meeting other commitments in the future, including post employment benefits. This leaves an unassigned General Fund balance of \$6.3 million that is available for appropriation for City programs and projects, which equates to approximately 39% of expenditures.

	Local Sales		
	General Fund	Tax Fund	Total
Beginning Fund Balance 7/1/16	\$ 7,352,010	\$ 238,187	\$ 7,590,197
Revenues	14,118,017	2,174,019	16,292,036
Expenditures	(15,272,330)	(829,699)	(16,102,029)
Other Financing Sources/(Uses)	1,604,692	-	1,604,692
Net Change in Fund Balance	<u>\$ 450,379</u>	<u>\$ 1,344,320</u>	<u>\$ 1,794,699</u>
Fund Balance:			
Nonspendable	\$ 1,071,000	\$ -	\$ 1,071,000
Assigned for capital projects	-	1,582,507	1,582,507
Assigned for post employment benefits	403,764	-	403,764
Unassigned	6,327,625	-	6,327,625
Ending Fund Balance, 6/30/17	<u>\$ 7,802,389</u>	<u>\$ 1,582,507</u>	<u>\$ 9,384,896</u>

Auditors may issue three different types of opinions at the conclusion of an audit; an unqualified, qualified, or adverse opinion. An unqualified opinion assures the reader that the information presented in the CAFR fairly represents the financial position of the City. A qualified opinion states that the information is fairly presented except for a particular issue. An adverse opinion indicates that the agency has major accounting and/or internal control issues and no reliance may be placed on the financial statements. The Administrative Services Department staff is proud to report that for the fiscal year ended June 30, 2017, the City of Arroyo Grande received an unqualified opinion.

ALTERNATIVES:

The following alternatives are provided for the Council's consideration:

- Approve staff recommendations and receive and file the Comprehensive Annual Financial Report;
- Do not approve staff recommendations;
- Modify staff recommendations and approve;
- Provide direction to staff.

ADVANTAGES:

By receiving and filing the Comprehensive Annual Financial Report, the City will be accepting the auditors' unqualified opinion. As mentioned above, an unqualified opinion assures the reader that the information presented in the CAFR fairly represents the financial position of the City.

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DISADVANTAGES:

There are no disadvantages in relation to the recommended action.

ENVIRONMENTAL REVIEW:

No environmental review is required for this item.

PUBLIC NOTIFICATION AND COMMENTS:

The Agenda was posted at City Hall and on the City's website in accordance with Government Code Section 54954.2.

Attachments:

- 1) Comprehensive Annual Financial Report and Independent Auditors' 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* (on file in the Administrative Services and Legislative and Information Services Departments for public review, as well as on the City's website at www.arroyogrande.org)

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