



Legislation Text

File #: 19-0025, **Version:** 1

TO:

Honorable Mayor and Members of the City Council

THROUGH:

Bruce Moe, City Manager

FROM:

Steve S. Charelian, Finance Director
Henry Mitzner, Controller
Julie Bondarchuk, Senior Accountant
Libby Bretthauer, Financial Analyst

SUBJECT:

Fiscal Year 2017-2018 Comprehensive Annual Financial Report (Finance Director Charelian).

RECEIVE AND FILE

RECOMMENDATION:

Staff recommends that the City Council receive and file this report.

EXECUTIVE SUMMARY:

We are pleased to report that the City has received the best possible opinion, an unmodified (*formerly unqualified*) audit opinion, meaning that the auditor believes that the City's financial statements are fairly presented in all material respects in conformity with Generally Accepted Accounting Principles (GAAP).

FISCAL IMPLICATIONS:

There are no fiscal implications associated with the recommended action. The results of fiscal year 2017-2018 are summarized below, and are included in the attached Comprehensive Annual Financial Report (CAFR).

DISCUSSION:

Attached to this report is the City's CAFR for the year ended June 30, 2018. This independent audit report is prepared with the assistance of the City's auditor, Lance, Soll and Lunghard, the certified public accountancy firm selected by the Council. Staff would like to take this opportunity to acknowledge the auditor's professionalism and diligence in the completion of the audit.

The attached report contains detailed information about the City's financial results for FY 2017-2018. The document, which is in industry-standard format, is organized as follows:

Introductory Section

The Introductory Section includes the City's transmittal letter providing an executive summary of the

financial and economic events characterizing FY 2017-2018. A review of the transmittal letter will help the reader understand the City's organizational structure and provides performance highlights of the City's most significant funds and operations.

Financial Section

The Financial Section presents the independent auditor's report. The auditor's report contains two main sections: the Audit Opinion and the Management Discussion & Analysis (MD&A).

Audit Opinion

The Audit Opinion, worded in an industry standard format, provides a statement by the auditor attesting to the fair presentation of financial data in conformity with generally accepted accounting principles and government accounting standards.

Management Discussion & Analysis (MD&A)

The required MD&A is intended to serve as an introduction to the City's basic financial statements, which comprise three components: 1) Government Wide Financial statements, 2) Fund Financial statements, and 3) notes to the financial statements, which is an overview and analysis of the financial activities of the City of Manhattan Beach for the fiscal year ended June 30, 2018.

The Government-wide financial statements are designed to provide readers with a broad overview of the City's finances, in a manner similar to a private-sector business. These statements utilize full accrual accounting (which recognizes revenue in the period it is earned, and expenses in the period it occurs) as is done in private industry. The statements included in this section are the statement of net position and the statement of activities. Both government-wide statements are designed to show the annual increase or decrease in net assets and, in doing so, distinguish functions of the City that are principally supported by taxes and intergovernmental revenues (governmental activities) from other functions that are intended to recover all or a significant portion of their costs through user fees and charges (business-type activities). The governmental activities of the City include general government, public safety, public works, planning, building and safety, and recreation. The City's business-type activities include water, waste water, storm water, refuse and parking.

The Fund Financial Statements include governmental funds reported on a budgetary modified accrual basis (which recognizes revenues when they become available and measurable and, with a few exceptions, recognizes expenditures when liabilities are incurred), and proprietary funds reported on a full accrual basis. Major governmental funds (General Fund, Capital Improvement Fund) and major enterprise funds (Water, Waste Water, Parking) are shown individually, while non-major funds are aggregated into a single column (full details are listed later in the document). Internal service funds are considered minor proprietary funds and are aggregated following enterprise funds.

The Notes to the Financial Statements section follows, which provides financial disclosures about the City's financial statements. That section is followed by the Combining Financial Statements & Schedules and the Statistical Section. The combining statements are presented in the traditional fund manner and report on the details of all non-major funds which appear on a combined basis in the front of the document. The Statistical Section, not subject to audit review and testing, provides general trend information presenting financial and economic data over time.

The first attachment to this report is the letter of transmittal which has been extracted from the FY 2017-2018 CAFR. The Letter of Transmittal provides an overview of the financial information

contained in the statements. In addition, there is discussion of

- Profile of the Government
- Budget Process
- Economic Condition
- Financial Policies
- Major Initiatives
- Executive Financial Overview
- Current Trends & Events

Staff recommends that the reader, at a minimum, review the Letter of Transmittal, and MD&A portion of the report. The Letter of Transmittal is attached to this staff report (attachment 1). Both the Letter of Transmittal and MD&A can be referenced in the introductory sections of the CAFR.

The audit results and the FY 2017-2018 CAFR financial statements were discussed with the Finance Subcommittee at their December 17, 2018 meeting.

Highlights and Trends

As of June 30, 2018, the City's net position totaled \$191.6 million government wide, an increase of \$6.45 million from the prior year. This increase was due to a positive net position change of \$3.0 million due to operations and a prior period restatement in net position of \$3.45 million. The change in the Governmental activities was \$874,292 and the change in the business type activities was \$5.58 million.

Governmental Funds (*General, Capital Improvement, and Special Revenue*)

Revenue totaled \$79.4 million, an increase of \$4.5 million (6.1%) from the prior year due to higher revenues from property taxes and charges for services. Expenditures totaled \$75.0 million, up \$1.5 million (2.1%) compared to the prior year due to an increase in operational expenditures in the General Fund, mainly in public safety. Total fund balances increased \$3.0 million to \$47.3 million.

General Fund balance was at \$26.9 million, up \$1.8 million compared to prior year. Revenues exceeded expenditures by \$3.4 million and transfers out totaled \$1.8 million.

Transfers out included:

- \$982,355 to the Stormwater Fund to relieve a deficit fund balance due to operations.

\$667,000 to the Insurance Reserve Fund to support long-term liabilities. Insurance Fund balance decreased \$1.8 million to negative \$2.98 million due to claim payments of \$8.1 million, worker's compensation expense of \$1.3 million and liability expense of \$421,422. The unpredictable nature of the claims, compounded by rising medical costs and claim judgements, caused the internal service fund charge outs to fall behind funding needs. In the future, charge outs to departments should match the expense incurred or further transfers will be required.
- \$198,935 to the Street Lighting Fund to relieve a deficit fund balance.

General Fund support will continue to increase for the Stormwater Fund and Street Lighting Fund

unless a Proposition 218 assessment vote can be passed to fund operations. Storm water runoff is under increased regulatory and environmental pressures, which has resulted in increased costs. Both assessments have been fixed since 1996.

Enterprise Funds

The net position of all enterprise funds totaled \$92.1 million, up \$5.5 million from the prior year. Revenue totaled \$27.8 million, up \$1.3 million compared to the prior year due to an increase of sales and service charges. Operating expenses totaled \$22.8 million, an increase of \$2.2 million from the prior year driven by an increase in contract services and materials. Operating income totaled \$5 million, down \$887,038 from the prior year.

Restatements

This year, the City implemented Governmental Accounting Standards Board (GASB) Statements 74 and 75, Accounting and Financial Reporting for Postemployment Benefits (OPEB) other than Pensions. The purpose of these statements is to establish new accounting and financial reporting standards for OPEB that is provided to state and local governments. OPEB benefits relate to medical benefits provided to retirees. Due to the implementation, the City made prior period restatements totaling \$3.75 million. Refer to page 11 of the MD&A for more information.

At the start of the audit, City staff informed the auditors of a fund balance restatement required in the Stormwater Fund in the amount of negative \$282,464 due to a reclassification of prior year capital outlay expenditures originally recorded as construction in progress that was later considered major repair and maintenance. This restatement resulted in what the auditors classify as a *material weakness* due to the size of the restatement compared to the balance in the fund. This item was presented to the Finance Subcommittee on November 5, 2018.

Pension Contributions

The City paid \$6.65 million for pension contributions in FY 2017-2018, compared to \$6.17 million in the prior year. Future City of normal service contributions and amortization of unfunded liability are projected to increase by approximately \$900,000 per year for the next five years. For additional details, see attachment 5 of this report which outlines a summary of pension amortization and projected employer normal service contributions through FY 2026-2027.

Managing the growing Net Position Liability (NPL) and meeting retirement obligations remain some of the City's biggest challenges. Nearly 98% of retirement costs are attributable to the City's Governmental Funds, and growing pension costs certainly have the potential to crowd out other funding needs.

The issue of rising pension contributions is shared by all members of local agency of PERS and not just Manhattan Beach. Finance staff is preparing a plan to address the issue of pension cost to the Finance Subcommittee and City Council in Spring 2019.

In closing, staff is pleased to report that the fiscal year 2017-2018 financial audit resulted in the City once again receiving an unmodified opinion. The General Fund performed better than expected, with an increase in fund balance of \$1.8 million. City Council policy reserves remain fully funded at the end of FY 2017-2018.

The City Manager and Finance Director wish to recognize the dedication, hard work and attention to

detail of all departments during the year that enables the City to achieve the unmodified opinion. Special recognition is in order for Finance staff, particularly Henry Mitzner, Julie Bondarchuk and Libby Bretthauer.

PUBLIC OUTREACH/INTEREST:

After analysis, staff determined that public outreach was not required for this issue.

LEGAL REVIEW

The City Attorney has reviewed this report and determined that no additional legal analysis is necessary.

Attachments:

1. FY 2017-2018 Letter of Transmittal
2. FY 2017-2018 Comprehensive Annual Financial Report (CAFR)
3. Report on Internal Control (Management Letter)
4. Audit Committee Letter
5. Projection of Pension Liability and Employer Contribution
6. PowerPoint Presentation