

Lompoc City Council Agenda Item



City Council Meeting Date: March 25, 2014

TO: Patrick Wiemiller, City Administrator

FROM: Brad Wilkie, Management Services Director
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SUBJECT: Acceptance of Annual Financial Statements for the Year Ending June 30, 2013

Recommendation:

Staff recommends the City Council accept the Financial Statements, together with the Independent Auditor's Report, for the fiscal year ending June 30, 2013.

Background:

The City's Finance Division has prepared the Annual Financial Statements as of June 30, 2013, and for the fiscal year ending June 30, 2013 (Annual Financial Statement). The City's independent external auditor, Glenn Burdette Attest Corporation (Glenn Burdette), has audited the Annual Financial Statements and has provided the City with an unqualified opinion regarding the fair presentation of the City's financial position. An unqualified (commonly referred to as a "clean audit") opinion is the preferred outcome for any financial audit. The Annual Financial Statements include Basic Financial Statements, Required Supplementary Information, Supplementary Information, as well as other regulatory required reports.

Generally, an Annual Financial Statement issued within six months after the end of the fiscal year is considered timely. Many governmental organizations subject to audit requirements also have a deadline nine months after the end of their fiscal year for reporting on federally awarded funds, if they are subject to the Office of Management and Budget Circular 133 (OMB-133). The City was subject to OMB-133 (commonly referred to as the "Single Audit") for grant and other federal assistance received during the fiscal year that ended June 30, 2013. The filing obligation required by OMB-133 includes the submission of a data collection form, as well as the filing of the Annual Financial Statement with the Federal Audit Clearinghouse (FAC). The required forms were accepted by the FAC on January 14, 2014.

While the City has been in compliance with the nine-month filing requirements since 2011, the Annual Financial Statements as of June 30, 2013 are the first in a number of years to be completed within six months of the end of the fiscal year.

The City has issued Annual Financial Statements for the past seven years. Prior to the report issued as of June 30, 2007, the City had issued a higher level report called the Comprehensive Annual Financial Report (CAFR). In fact, the City had received awards for 16 straight years, up to the report issued as of June 30, 2006. With the level of resources available to the Finance Division and the advantages of issuing a CAFR, staff has a goal of issuing a CAFR either as of June 30, 2014 or June 30, 2015.

Glenn Burdette has offered to assist with the transition from a simple Annual Financial Statement to a CAFR, as they have assisted with a comprehensive review of the Annual Financial Statements, starting with the report issued as of June 30, 2011. The report issued June 30, 2011 was the first audit by Glenn Burdette after the award, on February 1, 2011, of a contract for audit services following a competitive RFP process.

Discussion:

The first audit by Glenn Burdette was a challenging transition for the City and Finance Division staff. The change in auditors was also an opportunity to review past practices and conditions and to identify those requiring changes to conform to current accounting guidelines. The auditor conveyed their findings in three ways. The first was verbally, to Finance Division staff that included constructive suggestions to correct any financial presentations and to implement changes to procedures to improve the structural processes involved. The second, if warranted, was a report included in the Annual Financial Statement report package identifying Audit Findings and Recommendations. The third was a separate Management Report, for findings that do not rise to the level to be included in the Annual Financial Statement report package.

I am pleased to report the Audit Findings and the Management Report items have been reduced each year since the report issued as of June 30, 2011. With the reports issued as of June 30, 2013, there were just three Audit Findings and three Management Report items. Glenn Burdette staff met with City Administration staff on January 23, 2014, to review the overall audit, as well as the reported issues. The Audit Findings, published in the body of the Annual Financial Statement report package, includes detailed City responses for the Audit Findings and can be found in the Financial Statements beginning on page 127.

Following is a summary of the reported items and a summary of the plans to address each:

The City has three funds with negative Net Positions as of June 30, 2013. The financial trend for all three funds is positive. One fund is expected to return to a positive net position by June 30, 2014, and the Solid Waste Utility fund has an amortizing loan for operation losses incurred up to June 30, 2010, scheduled to be repaid on June 30, 2017. The Broadband fund is scheduled to pay off all external debt on November 7, 2014. Operational changes, identified in the City's FY 2013-15 Budget, and additional

services to City operations due to the loss of Comcast franchise benefits beginning January 1, 2015, will provide that fund with resources to eliminate its net position deficit, similar to the process approved for the Solid Waste Utility in 2010 to eliminate its net position deficit.

The City's agreement with Vandenberg Village Community Services District (VVCSD) includes a requirement for VVCSD to hold cash reserves with the City, based on a formula. While the requirement was calculated correctly, the incremental increase required as of June 30, 2013 was not invoiced by the City until December 18, 2013. VVCSD's payment was received by the City on December 27, 2013.

Three of the six findings are related to fixed assets or capital assets. Fixed asset reporting for financial statement presentation purposes is similar to non-governmental reporting, in that the assets are valued at cost on the balance sheet of the City, with annual depreciation charged over the life of the asset. For budgetary purposes, the City accounts for capital outlay items in the year of acquisition, so that economic resources can be matched with budgetary obligations. In other words, the budget accounts for the cash cost of a fixed asset in the year of purchase, but does not address the long-range use of the asset, or the cost of the eventual replacement of the asset.

The dual reporting requirements have been addressed by many governmental entities by implementing a separate tracking system for fixed assets, which provides for the calculation of depreciation necessary for reporting purposes in the Annual Financial Statements. Depreciation has always been reported in proprietary funds, but only since 2004 have depreciation calculations been required for government-wide reporting. The City's fixed-asset system was created in the 1980s with internal resources and has worked adequately for the purposes intended. However, the system requires substantial manual attention, in order to assure the information generated from the system is materially correct. It would be advantageous to the City to consider a more current fixed-asset tracking system, concurrently with the ongoing evaluation of the primary finance systems of the City, which have also been in place since the 1980s.

Finally, during the physical inventory count process conducted during the final week of June, observed by Glenn Burdette staff, the inventory amounts were calculated and confirmed by both City staff and audit staff. Concurrently, the annual closing process provides for the payment of invoices dated on or before June 30, for the first 45-60 days of the next period. That is commonly called the accounts payable accrual period. During audit testing of the accounts payable process, invoices related to inventory items were tested. By processing invoices related to inventory in the accounts payable process after June 30, the inventory balances as of June 30 are modified from the balances determined through the physical inventory process. Finance staff has addressed that timing issue and have changed the accounts payable accrual process to exclude payment of inventory invoices after June 30, since the values have already accounted for the inventory received as of June 30 in any particular year.

Fiscal Impact:

While there are no immediate financial impacts to the General Fund or other funds for accepting the financial statements, the longer-term impact to the City from having financial statements without substantial findings will be beneficial. Stronger financial statements will provide flexibility to the City in the near and long-term, as additional financial challenges are in the future. One example of a longer-term benefit would be possible lower interest rates on future debt, based on a higher credit rating due to a strong financial reporting history.

Conclusion:

While no explicit action is required of the Council to approve the Annual Financial Statements, it is good practice to accept the Annual Financial Statements. Finance staff will continue towards the goal of returning the City's reporting to the CAFR level.

Mr. Eschenbach of Glenn Burdette will be at the Council meeting regarding this report and available to make a brief presentation regarding the audit process and the City's Annual Financial Statements.

Respectfully submitted,

Brad Wilkie, Management Services Director

APPROVED FOR SUBMITTAL TO THE CITY COUNCIL:

Patrick Wiemiller, City Administrator

- Attachments: 1) [Financial Statements for the Year Ended June 30, 2013](#)
2) [Recommendations to Management Report dated June 30, 2013](#)

Attachment 1 is available for review at the City Clerk's Office, Lompoc Public Library or on the City's website.