

## MEMORANDUM

**TO: CITY COUNCIL**

**FROM: MICHAEL STEVENS, ADMINISTRATIVE SERVICES DIRECTOR**

**SUBJECT: CONSIDERATION OF ACCEPTANCE OF THE COMPREHENSIVE ANNUAL FINANCIAL REPORT**

**DATE: FEBRUARY 9, 2021**

### **SUMMARY OF ACTION:**

Receive and file the Comprehensive Annual Financial Report (CAFR) for the fiscal year ended June 30, 2020.

### **IMPACT ON FINANCIAL AND PERSONNEL RESOURCES:**

Preparation of the City's financial reports requires approximately 250 hours per year of personnel resources and auditing services cost approximately \$28,000 annually.

### **RECOMMENDATION:**

It is recommended the City Council receive and file the Comprehensive Annual Financial Report (CAFR) for the fiscal year ended June 30, 2020.

### **BACKGROUND:**

State law requires that every general-purpose local government publish an annual report on its financial position and activity, and that the report be audited by an independent firm of certified public accountants. The goal of the independent audit is to provide a reasonable assurance that the City's financial statements are free of material misstatements. In addition, the audit is responsible for providing an independent review of the City's internal financial controls. The City's financial statements, internal documents, and financial controls have been audited by the certified public accountant firm of Moss, Levy & Hartzheim, LLP for the fiscal year ending June 30, 2020.

### **ANALYSIS OF ISSUES:**

Generally accepted accounting principles (GAAP) provides the criteria for judging whether a financial report is presented fairly. In defining the minimum standard of acceptable basic financial reporting for state and local governments, GAAP mandates a complete set of basic financial statements, including accompanying note disclosures, as well as the presentation of certain required supplementary information. GAAP encourages government agencies to present this information within the Comprehensive Annual Financial Report (CAFR).

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

- The introductory section: provides general information on 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 external auditors conducted testing of the City's internal financial controls in August 2020 and October 2020. The testing included reviewing 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 by the auditors.

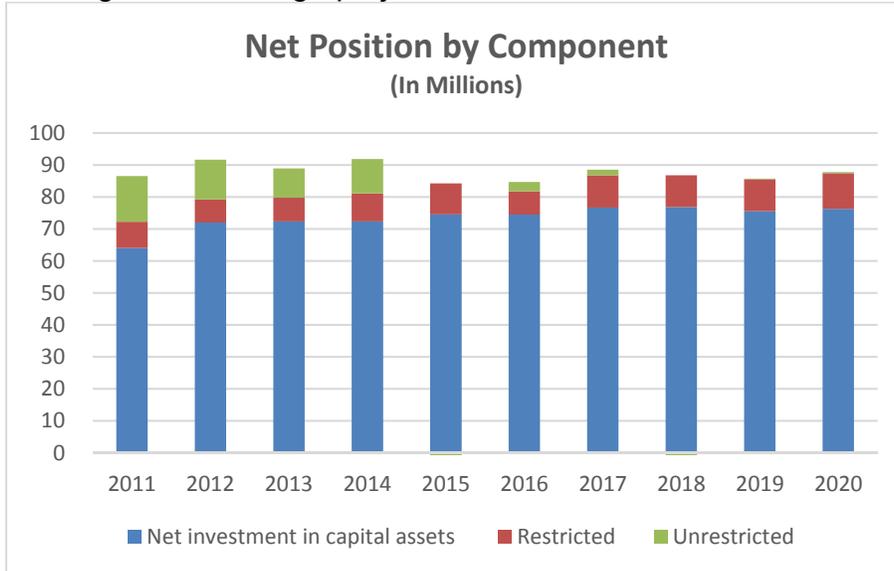
An audit was conducted on net position of the City for the financial period ending June 30, 2020. Documentation in support of the assets, liabilities, and fund balance of all the funds in the City were examined and verified. This process assures an impartial review and substantiation of the City's net position. The result of this review is documented in 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.

Auditors may issue three different types of opinions at the conclusion of an audit; an unmodified, modified, or adverse opinion. An unmodified opinion assures the reader that the information presented in the CAFR fairly represents the financial position of the City. A modified 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, 2020, the City of Arroyo Grande received an unmodified opinion, reflecting that the information presented in the CAFR fairly represents the financial position of the City.

As presented in the CAFR, the City's combined net position at June 30, 2020 increased by 2.45% from \$85.7 million to \$87.8 million. This overall increase is due to an increase in governmental activities. The increase in governmental activities is largely due to

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additional Federal Highway Bridge Replacement and Rehabilitation Program funding specific to the Bridge Street Bridge project and its associated construction in progress.



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 does not necessarily reflect the economic health of an organization. In the City’s case, about 87% of the total net position reflects capital assets. While these assets are important, they cannot 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.

For financial reporting purposes, the half percent Local Sales Tax revenue approved by voters in 2006 and Other Post-Employee Benefits funds (OPEB) are combined with the General Fund for CAFR reporting purposes. However, the City’s quarterly and year-end reporting is based on the General Fund exclusively and does not include the Local Sales Tax or OPEB funds. The combined funds, as shown in the table on the following page, reports total revenues of \$21.4 million and expenditures of \$20.8 million. As a result, there was an overall increase to the fund balance of \$612,007 during the 2019-20 fiscal year.

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	General Fund	Local Sales Tax Fund	OPEB	Total
Beginning Fund Balance 7/1/19	\$ 5,699,538	\$ 3,492,159	\$ 659,046	\$ 9,850,743
Revenues	18,870,662	2,396,608	136,667	\$ 21,403,937
Expenditures	(18,726,276)	(2,065,654)	-	\$ (20,791,930)
Net Change in Fund Balance	\$ 144,386	\$ 330,954	\$ 136,667	\$ 612,007
<b>Fund Balance:</b>				
Nonspendable	\$ 5,152	\$ -		\$ 5,152
Assigned for capital projects	-	3,737,520		3,737,520
Assigned for post employment benefits	-	-	795,715	795,715
Unassigned	5,838,770	85,593		5,924,363
Ending Fund Balance, 6/30/20	\$ 5,843,922	\$ 3,823,113	\$ 795,715	\$ 10,462,750

The CAFR reports a General Fund total fund balance of \$10.5 million. However, a small amount of the fund balance is considered non-spendable because it is held as inventory (\$5,152). Additionally, \$4.5 million is designated for completing capital projects or meeting other commitments in the future, including post-employment benefits. This leaves an unassigned balance of \$5.8 million in the General Fund and \$85,593 in the Local Sales Tax fund. Of the \$5.8 million in unassigned General Fund, \$1.0 million is classified as reserved fund balance, leaving \$4.8 million available in the General Fund for general purposes. The City's Fiscal Policy establishes the maintenance of a fund balance reserve goal of 20% of expenditures with a minimum of 15% in the General Fund. At the conclusion of Fiscal Year 2019-2020, the reserve, based on available General Funds, was 25% and exceeded the City's reserve goal.

**ALTERNATIVES:**

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

1. Receive and file the Comprehensive Annual Financial Report; or
2. Provide other 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.

**DISADVANTAGES:**

There are no disadvantages in relation to the recommended action.

**ENVIRONMENTAL REVIEW:**

No environmental review is required for this item.

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**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](http://www.arroyogrande.org))

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