

# Agenda Report

March 13, 2017

**TO:** Honorable Mayor and City Council/Successor to Pasadena  
Community Development Commission

**THROUGH:** Finance/Audit Committee

**FROM:** Director of Finance

**SUBJECT: FISCAL YEAR JUNE 30, 2016 ANNUAL FINANCIAL REPORTS**

**RECOMMENDATION:**

It is recommended that the following reports for the year ended June 30, 2016 be reviewed, discussed, and filed by the City Council and/or the Successor Agency to Pasadena Community Development Commission.

- A. Comprehensive Annual Financial Report\*
- B. Single Audit Report
- C. Independent Auditor's 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\* (This replaces what was called the "Management Letter.")
- D. Pasadena Center Operating Company Basic Financial Statements\*
- E. Rose Bowl Operating Company Basic Financial Statements\*
- F. Pasadena Community Access Corporation Basic Financial Statements
- G. Pasadena Fire and Police Retirement System Independent Auditor's Report and Basic Financial Statements with Required Supplemental Information\*
- H. Air Quality Improvement Fund Financial and Compliance Report \*
- I. Independent Accountant's Report on Agreed-Upon Procedures Applied to Appropriation Limit Worksheets\*
- J. Independent Accountant's Report on Agreed-Upon Procedures Applied to Employee Deductions for the Internal Revenue Code Section 457 Deferred Compensation Program\*
- K. The Auditor's Communications with the City's Audit and Finance Committee\*
- L. Pasadena Housing Successor Basic Financial Statements\*

\*Reports previously delivered.

## **EXECUTIVE SUMMARY:**

This action is to receive and file the City's seven annual financial statements and five compliance-related reports for the fiscal year ended June 30, 2016. All financial statements received an unqualified (or clean) opinion. One material weakness in internal controls and two significant deficiencies were identified in the Independent Auditor's 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. Management responses are provided for the material weakness and the significant deficiencies. The Single Audit report repeats the above three financial statement findings and reports an additional material weakness and six additional significant deficiencies related to federal awards. In all cases corrective action has already occurred or an action plan to address the finding has been established. A presentation will be made by the City's external auditors, Lance, Soll & Lunghard, LLP at the March 13, 2017 Finance/Audit Committee and City Council meetings.

## **BACKGROUND:**

This year's audit was the second annual audit performed by Lance, Soll & Lunghard, LLP, who was awarded a three year contract to perform the City's audits on May 18, 2016. The contract calls for an expanded scope audit with samples from every City fund and a reduced level of materiality so that sample sizes are increased. All seven financial statements received unqualified opinions from the outside auditors. This is the highest or cleanest attestation report given by independent auditors and includes the phrase "the financial statements referred to above present fairly, in all material respects, the financial position..." The five remaining reports presented deal with compliance information, specifically requested test work, and provide comment on internal controls, errors, lack of errors, or suggestions for future improvements.

### **Comprehensive Annual Financial Report (CAFR) (Attachment A)**

Section 912 of the City Charter requires that an independent audit of the City's records, books, and inventories be conducted annually and a report issued thereon. In the attached audited CAFR for the year ending June 30, 2016, the City received an unqualified opinion, which means that the statements are free of material misstatement and are presented in conformity with generally accepted accounting principles.

### **Single Audit Reports on Federal Awards (Attachment B)**

The Single Audit Act of 1984, Single Audit Act Amendments of 1996, and more recent Office of Management and Budget's (OMB) "Uniform Guidance" establish uniform audit requirements for local governments expending federal awards greater than \$750,000 a year. The audit is on an "entity-wide" basis and imposes additional requirements in

relation to testing of, and reporting on, internal control and compliance with laws and regulations. The Single Audit Reports for Fiscal Year ended June 30, 2016 contains

two reports. The first one reports on internal control over financial reporting and reports one material weaknesses in internal control over financial reporting, two instances of significant deficiency, and no instances of noncompliance or other matters requiring disclosure. The second reports on compliance with major federal programs and found that the City complied in all material respects with the requirements that have a direct and material effect on each of the City's major federal programs. However, there was one finding identified as a material weakness and six findings of significant deficiency in internal controls related to federal programs. A management response and corrective action plan is provided, and staff either have or will fully address all findings.

The auditors also express an opinion that the schedule of expenditures of federal awards (SEFA) is "fairly stated" in all material respects. Lastly, the Single Audit Report provides a status update on all prior year findings (from FY 2015). Of the 32 findings, 30 are identified as "This finding is considered to be resolved." Two findings are reported as "not resolved" and repeated as a finding in FY 2016.

**Independent Auditor's 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 (This replaces what was called the "Management Letter") (Attachment C)**

This report explains the auditors' audit of the City's financial reports in relation to their review of internal controls. The City's audit was performed in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in the *Government Auditing Standards*, issued by the Comptroller General of the United States. Such audits utilize sampling of data, inquiries of staff and management, testing of procedures, confirmation with outside parties, spot checking of internal files and documents, review of meeting minutes, specialized audit checklists, and numerous other techniques. The auditors considered the City's internal controls in determining what procedures to use and the size of samples to be selected. While audit procedures do not include review of 100 percent of transactions, the City contracted to have every fund examined and for sample sizes to be greater than required under generally accepted audit procedures.

This report provides definitions of "deficiency in internal control," "material weakness," and "significant deficiency" involving the internal control structure. This year's audit identified one material weakness and two significant deficiencies. The auditors did not identify any "other matters" which are a third and less critical category of findings. These comments and recommendations have been reviewed with the appropriate members of City staff and City responses are provided. In all cases staff fully understands the issues and has already or will fully address the issues.

## **Component Unit Financial Statements**

Financial statements for Pasadena Center Operating Company (Attachment D), Rose Bowl Operating Company (Attachment E), Pasadena Community Access Corporation (Attachment F), and Pasadena Fire and Police Retirement System (Attachment G) are included as they are component units of the City. Component units are legally separate entities in substance but are part of the government's operations. Each of the City's component units received an unqualified opinion.

## **Pasadena Housing Successor Basic Financial Statements (Attachment L)**

In previous years the Pasadena Housing Successor fund has been presented with the other non-major special revenue funds. This year and going forward the City has elected to present it as a major fund presenting it with the major governmental funds in the CAFR. This facilitates meeting the state's required reporting and auditing requirements for this fund.

## **Air Quality Improvement Fund Financial and Compliance Report (Attachment H)**

Assembly Bill 2766 (AB2766) authorized the South Coast Air Quality Management District (SCAQMD) to impose an annual vehicle registration fee and to distribute a portion of those collected revenues to all local jurisdictions within the South Coast Air Basin. These revenues are to be used solely to reduce air pollution from motor vehicles by implementing new programs and studies necessary for the implementation of the California Clean Air Act. The City's Air Quality Improvement Fund accounts for the use of these funds received from SCAQMD. The Air Quality Improvement Fund Financial and Compliance Report received an unqualified opinion.

## **Independent Accountant's Report on Agreed-Upon Procedures Applied to Appropriation Limit Worksheets (Attachment I)**

Section 1.5 of Article XIII B of the California Constitution requires that the City follow the procedures agreed upon by the State of California and the League of California Cities (as presented in the League publication entitled Article XIII B Appropriations Limitation Uniform Guidelines) to determine the annual appropriations limit. The auditors perform an "Agreed-Upon Procedure" where they recalculate the Gann Limit. They determined that the City has incorrectly calculated the Gann Limit. The Fiscal Year 2016 appropriation limit should have been \$255,661,600, resulting in an immaterial understatement of the limit of \$42,344 from the original City adopted limit of \$255,619,256. This has not resulted in any budget or actual impact on the City and the calculation will be corrected to reflect the correct amount upon the next budget adoption.

### **Independent Accountant's Report on Agreed-Upon Procedures Applied to Employee Deductions for the Internal Revenue Code Section 457 Deferred Compensation Program (Attachment J)**

At the request of the City, the auditors performed certain procedures as enumerated in the report to verify the accuracy and timely posting of contributions to the deferred compensation program provided by Great West Retirement Services. The auditors noted that the amounts deposited did not match to the amounts withheld. The City has determined that this is solely a timing difference resulting from retirement and separation checks which, due to the payroll cycle, are reported with the next or subsequent regular payroll.

### **The Auditor's Communications with the City's Audit and Finance Committees (Attachment K)**

One auditing pronouncement, Statement of Auditing Standards (SAS) No. 114 requires defined and documented communications between the auditors and the City Audit Committee/Finance Committee. This letter provides an opportunity for the auditors to report on any difficulties or major concerns discovered during the audit and to further define their role. They provide commentary on management's responsibilities for accounting policies and states that no significant difficulties were encountered in performing the audit, and no disagreements occurred with management. They point out that management has corrected all known misstatements, even those that could be passed adjustments that would be not material either individually or in the aggregate.

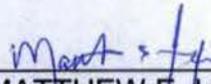
### **COUNCIL POLICY CONSIDERATION:**

The City Council's strategic planning goal of maintaining fiscal responsibility and stability will be advanced through the receipt and review of these reports.

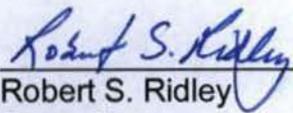
**FISCAL IMPACT:**

There is no fiscal impact as a result of this action nor will it have any indirect or support cost requirements. There is no anticipated impact to other operational programs or capital projects as a result of this action.

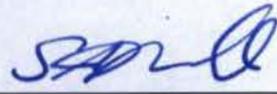
Respectfully submitted,

  
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MATTHEW E. HAWKESWORTH  
Director of Finance

Prepared by:

  
\_\_\_\_\_  
Robert S. Ridley  
Controller

Approved by:

  
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STEVE MERMELL  
City Manager

Attachments: (2)

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