

Agenda Report

February 11, 2019

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, 2018 ANNUAL FINANCIAL REPORTS

RECOMMENDATION:

It is recommended that the following reports for the year ended June 30, 2018 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 Reports
- 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 Statements 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, Independent Auditors' Report on Internal Control over Financial Reporting and on Compliance and other Matters Based on an audit of Financial Statements, Independent Auditors' Report on Compliance with Applicable Requirement and on Internal Control Over Compliance, and Housing Successor Annual Report Regarding the Low and Moderate Income Housing Asset Fund *

*Report 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, 2018. All financial statements received an unmodified (or clean) opinion. The financial statement audit resulted in three findings. Two are material weaknesses in internal controls, one a significant deficiency, and no instances of noncompliance. These are explained in more detail below. The Single Audit Report reiterates these three findings and reports on six additional findings all related to grants. In all cases corrective action has already occurred or an action plan to address the findings have been established. A presentation will be made by the City's external auditors, Lance, Soll & Lunghard, LLP at the February 11, 2019 Finance/Audit Committee and City Council meetings.

BACKGROUND:

This year's audit was the fourth annual audit performed by Lance, Soll & Lunghard, LLP, who was awarded a one year contract extension to perform the City's audits on May 14, 2018. On May 14, 2018, City Council also asked that the fifth year optional contract extension be brought back for consideration. Staff will bring this back to the Audit Committee in March. The current 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 unmodified 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 present 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, 2018, the City received an unmodified 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 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 related to grants and contracts applicable to the City's federally funded programs. Our Single Audit Report repeats the three financial statement related findings and contains six additional findings. Five of these additional findings relate to either reporting or subrecipient monitoring deficiencies and are considered significant deficiencies and instances of non-compliance involving the Home Investment Partnerships Program. The sixth finding is a carryover from two prior years where the auditors' selected the same contract in all three years that did not have a SAM check performed before execution in the initial year. Audit standards require that they continue to report the finding in subsequent years when there are expenses paid.

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 and has three findings. 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 two material weaknesses and one significant deficiency. The first material weakness deals with capital project reporting and when a project should be considered completed. The second material weakness involved a timing difference that put an expense into a different fiscal year and was not caught by City staff. The third finding was a significant deficiency that a City lacks a formal policy requiring timely resolution of bank reconciling items. The auditors did not identify any "other matters", which are a third and less critical category of findings, and no instances of noncompliance. 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 addressed 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 unmodified opinion.

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 unmodified 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 current year calculation is correct but that the City had to correct the beginning balance of the Gann Limit to reflect a prior year correction. This has not resulted in any budget or actual impact on the City.

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. This is not considered a finding.

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 explain 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 whether management has corrected or passed on correcting all known misstatements. This year there were no uncorrected items.

Pasadena Housing Successor Basic Financial Statements, Independent Auditors' Report on Internal Control over Financial Reporting and on Compliance and other Matters Based on an audit of Financial Statements, Independent Auditors' Report on Compliance with Applicable Requirement and on Internal Control Over Compliance, and Housing Successor Annual Report Regarding the Low and Moderate Income Housing Asset Fund (Attachment L)

Since Fiscal Year 2016 the Pasadena Housing Successor fund has been presented as a major fund with the major governmental funds in the CAFR. This facilitates meeting the state's required reporting and auditing requirements for this fund. To meet the reporting requirements; the Housing Successor Financial Statements, the Independent Auditors' Report on Internal Control, Report on Compliance With Applicable Requirement and on Internal Control Over Compliance, and the Housing Successor Annual Report Regarding the Low and Moderate Income Housing Asset Fund were delivered to the Mayor and City Council Members on December 28, 2018 and posted on the City's website. The Auditors' opined that the Housing Successor has complied in all material respects with the compliance requirements they must report on and they did not identify any noncompliance with the California Health and Safety Code requirements.

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,



MATTHEW E. HAWKESWORTH
Director of Finance

Prepared by:



Robert S. Ridley
Controller

Approved by:



STEVE MERMELL
City Manager

Attachments: (12)

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