

To: James L. App, City Manager
From: Mike Compton, Director of Administrative Services
Subject: Comprehensive Annual Financial Report
DATE: February 18, 2003

Need:

Present the Comprehensive Annual Financial Report for the fiscal year ending June 30, 2002 for City Council consideration.

Facts:

1. The Comprehensive Annual Financial Report (CAFR) is prepared in accordance with generally accepted accounting procedures, including compliance with pronouncements issued by the Governmental Accounting Standards Board (GASB).
2. The CAFR and all supporting accounting and financial records are audited by the outside certified public accounting firm, Moss, Levy & Hartzheim in accordance with generally accepted auditing standards and the *Government Auditing Standards* as issued by the Comptroller General of the United States.
3. The opinion letter issued by Moss, Levy & Hartzheim is unqualified (clean) and indicates that the financial statements and other information reported in the CAFR fairly represent, in all material respects, the financial position of the City as of June 30, 2002.
4. Moss, Levy & Hartzheim has also issued a management letter citing two recommended improvements to the City's financial operations as well as their "communication to council" letter (copies attached).
5. A CAFR is designed and prepared in order to provide the interested reader with much detailed information and data regarding the financial results of operations. It represents a much higher degree of financial reporting than a simple audit report.
6. Attached as part of the CAFR presentation is the annual Management Letter prepared and submitted by Moss, Levy & Hartzheim. Staff is prepared to present point-by-point response to each finding.

Analysis and

Conclusions:

For purposes of understanding the distinction between fund balance or retained earnings and cash balance, the following explanation is provided:

Fund balance and retained earnings represent the net difference between total assets and total liabilities. Thus, if there are not assets other than cash and there are no liabilities, fund balance and cash will be one and the same. However, if the balance sheet contains an accounts receivable item in the amount of \$10,000 and there are no other assets except cash or there are no liabilities, fund balance will exceed the cash balance by \$10,000 representing the net difference between total assets and total liabilities.

The distinction between fund balance and retained earnings is that retained earnings includes the balance sheet items for the net investment in fixed assets and long-term debt. Fund balance does not include the investment in fixed assets nor long-term debt because they are recorded elsewhere (the General Fixed Asset and General Long Term Debt Account Groups). Retained earnings only applies to enterprise funds, while fund balance applies to all other fund types.

General Fund

The General Fund experienced an increase in fund balance (reserves) due to the fact that revenues and operating transfers in exceeded operating expenditures and operating transfers out by \$1,366,351. Total fund balance at 6/30/02 was \$8,234,466, up from the prior year's fund balance of \$5,465,082. The unreserved/undesignated portion was \$6,274,004 as compared to last year's unreserved balance of \$5,100,499. The \$6,274,004 represents a reserve of 47%; unreserved fund balance to operating expenditures including operating capital.

It needs to be noted that the positive increase to fund balance, \$1,366,351 will be offset in the following fiscal year by carry-overs totaling slightly over \$2.7 million for appropriations that were not spent in fiscal year 2002.

Special Revenue Funds

Special Revenue Funds are a category of non-enterprise funds whose use is restricted for some special purpose either by state or federal regulation or by local ordinance and/or policy and is not identified as a capital projects fund. In the aggregate, Special Revenue Funds experienced an increase in total fund balance. Total fund balance for all special revenue funds was \$4,535,424 as compared to last year's total of \$3,992,827. \$673,700 of this fund balance is restricted as it represents the balance in the Redevelopment Agency's Low/Moderate Income Housing Fund. The total aggregate cash balance at 6/30/01 was \$4,747,823 as compared to last year's balance of 3,637,134\$.

Description of each special fund is provided on page of 61 of the CAFR.

Debt Service Funds

Debt Service Funds include three funds, the 1993 Public Facility Certificate of Participation, the Redevelopment Agency Debt Service Fund and the Measure D General Obligation Bond Fund. In October 2000, the Agency sold \$4,090,000 in tax allocation bonds. The general obligation bonds will not have reportable transactions until fiscal year 2003 when tax collections and debt service payments are activated.

Capital Project Funds

Capital Project Funds, in the aggregate, had a fund balance of \$25,506,175 as compared to \$21,530,124 last year. Cash resources experienced an increase from \$22,600,910 in the prior fiscal year as compared to \$26,299,158 this year. Description of each special fund is provided on page of 87 of the CAFR.

Enterprise Funds

Water Operations - Water Operations saw an increase in retained earnings but only due to interest earnings on impact fees, capital replacement monies and the change in reporting requirements that dictated the inclusion of developer contributed fixed assets as revenues. The amount included in for developer contributed fixed assets was \$1,469,985. Retained earnings rose from \$15,098,347 to \$17,156,564 in spite of an operating loss of \$(356,403).

It is noted that the Water Operations Fund has no outstanding debt.

With regard to cash resources, the balance at 6/30/01 was \$11,986,912 as compared to last year's balance of \$9,957,116.

Note that cash resources include development impact fee revenues that have been collected for projects currently underway and projects identified in the CIP budget that have not yet been started. While the City expects to collect a few million dollars in impact fees over the next three years, the CIP budget contains \$20 million + in projects over the same time frame.

The main concern is operating revenues. As noted above, operating revenues were \$356,403 short of covering operating expenses and represents the ninth straight year that water operations has experienced an operating loss. The Council adopted increased user fees that became effective 3/1/02. It is expected to eliminate the operating deficit when the impact of a full year's increased revenues is realized.

Sewer Operations - As with Water Operations, Sewer Operations saw a significant increase in retained earnings; increasing from \$5,208,828 to \$8,056,390. As with Water Operations, the increase is attributable to interest income on impact fees and capital replacement monies as well as the change in

reporting requirements that dictated the inclusion of developer contributed fixed assets as revenues. The developer contributed fixed assets totaled \$2,234,190.

Cash resources at 6/30/02 totaled \$7,764,965, up from last year's total of \$6,090,815. The increase is mainly due to sewer connection fee revenue collections generated from development activity.

Note that cash resources include development impact fee revenues that have been collected for projects currently underway and projects identified in the CIP budget that have not yet been started. While the City expects to collect a few million dollars in impact fees over the next three years, the CIP budget contains nearly \$19 million in projects over the same time frame.

As has been the case since fiscal year 1994, the Sewer Operations Fund has experienced an operating loss. The operating loss, \$(4,252), was significantly reduced from last year's loss. The Council adopted increased user fees that became effective 3/1/02. It is expected to eliminate the operating deficit when the impact of a full year's increased revenues is realized.

Airport Operations - Retained earnings in this Fund increased due to the inclusion of capital contributions in the amount of \$1,753,019. Retained earnings were \$10,220,866 this year versus \$8,446,651 last year.

Cash resources decreased significantly from \$394,623 to \$239,967 this year. The net loss for the year was \$(185,534) as compared to last year's net loss of \$(119,308).

Solid Waste Operations - Due to the long-term "turn-key" operations contract, this Fund was decommissioned as an enterprise fund. Its net equity and cash (after repayment of accrued liabilities) was transferred to the General Fund. The equity transfer was \$1,326,909.

Transit Operations - Transit operations saw a slight decrease in retained earnings from \$373,702 last year to \$363,757 this year.

The Fund's cash balance ended the year at \$84,695 as compared to \$357,633 last year. The decline is due to the purchase of two new transit buses and the one-time allocation of TDA funds from transit uses to street and road uses.

Fiscal

Impact:

None

Options:

- a. That the City Council receive and file the Comprehensive Annual Financial Report for the fiscal year ending June 30, 2002 or
- b. Amend, modify or reject any of the options above.

COMPREHENSIVE ANNUAL FINANCIAL REPORT

A Copy is available in the library for public review.

**Additional copies are available in the City Clerk's Office
and Administrative Services**