DATE:       June 21, 2016

TO:        City Council

THROUGH:    Greg Nyhoff, City Manager
            Office of the City Manager

FROM:       Dave Millican, Chief Financial Officer

SUBJECT:    Comprehensive Annual Financial Report for Fiscal Year 2014-2015 (30/75)

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RECOMMENDATION:

Receive, consider and file the Comprehensive Annual Financial Report (CAFR) for the fiscal year ending June 30, 2015.

BACKGROUND

The CAFR has been delayed for six months beyond it normal completion date for these reasons.

1. Lack of compliance with legal accounting requirements and poor accounting practices limited management’s and City’s new independent auditors ability to rely on internal controls to provide assurance that all material items were properly reported in the report.

2. A comprehensive review, reconciliation and analysis of the City’s financial records was performed to provide assurance that all material items were reported. Despite this effort records relating to capital assets were so flawed as to render them unauditable.

3. Turnover and unplanned absences in key financial management positions increased the time needed to understand and document major financial issues. Permanent files maintained in the department system did not adequately support amounts recorded in the City’s accounts, requiring extensive research.
This effort was fully supported by the City Council in its authorizations of resources to supplement staff with experts to assist in the comprehensive analysis, to increase permanent staff levels in the Finance Department and to commit hours of meeting time to receive and consider information relating to financial matters.

**DISCUSSION**

The CAFR is a complex document with hundreds of pages of information and explanation. Two elements of the CAFR provide an overview of the report, The Letter of Transmittal and Management’s Discussion and Analysis, which follows the Auditor’s Opinion. Those sections are separately copied and attached to this staff report for interested parties who want an overview of the report.

This year extensive correction of accounting records resulted in many prior period adjustments, prior period adjustments also resulted from implementation of the Governmental Accounting Standards Board’s (GASB) new standard on pension accounting and reporting. As a result comparison with the Fiscal 2014 CAFR is of limited use. However, Management’s Discussion and Analysis provides comparative information. Fiscal 2014 balances were not restated because the changes would have required another effort comparable to the analysis for the Fiscal 2015 CAFR comparative information is of limited use.

In consultation with the independent auditor, staff has moved the assets, liabilities and results of operations of the Municipal Golf Course Fund and the Performing Arts and Convention Center (PACC) into the General Fund. This was done because neither operation recovers capital costs through customer charges and each has required subsidies for many years. In addition, only a fraction of the debt service recorded in the golf course enterprise fund was actually attributable to acquisition and development of the golf course. This transfer affects comparisons between Governmental Activities amounts in both Fiscal 2014 and 2015 and between the General Fund and proprietary funds in those years.

It is important to realize that this report does not change the City’s financial condition. It provides a more accurate and realistic view of that condition. The City is complex. There are more than 8,000 active accounts and 175 funds. Tens of thousands of transactions are posted each year and its operating environment encompasses multiple service business models.

**Audit Opinion:** The auditor’s opinion is complicated by the fact that the capital asset systems are unauditable. That problem is the source of the auditor’s qualification of their opinion. Although the City has only booked assets that it can identify, weak system controls and missing records made it impossible to determine whether all capital costs associated with confirmed projects have been identified or whether some costs not booked as capital assets may in fact be associated with projects that have not been confirmed.

As a result, the opinion is qualified for CAFR accounting presentations where capital assets are significant, especially for full accrual presentations in the government-wide and business type
activities funds. In the General Fund and other governmental funds that use modified accrual accounting capital assets are not reported and the opinions are unqualified.

Next steps: The Single Audit report for state and federal grant awards will be completed in time for discussion at the July 13, 2016 Fiscal Policies Task Force Meeting. That report will identify and provide recommendations for significant and material weaknesses in internal controls. The agenda will also have a presentation on goals and objectives for the Chief Financial Officer and the Finance Department. Other reports on Measure O and the golf course will follow in July.

The teamwork required to produce the CAFR and Budget at the same time was exemplary and the effort and commitment exhibited in this effort result from the commitment of employees and consultants helping the City.

FINANCIAL IMPACT

The recommended action to receive and file the Fiscal Year 2014-15 CAFR has no financial impact.