



CITY OF ALBANY CITY COUNCIL AGENDA STAFF REPORT

Agenda Date: May 1, 2023
Reviewed by: NA

SUBJECT: Annual Comprehensive Financial Report (ACFR) and Annual Audit for FY 2021-22

REPORT BY: Heather Rowden, Finance & Admin Services Director

SUMMARY

Annually the City prepares financial statements which are audited by independent auditors. The Auditors have reviewed the City's financial statements and relayed their findings in the attached Annual Comprehensive Financial Report (ACFR) for fiscal year ending June 30, 2022.

STAFF RECOMMENDATION

That the Council:

1. Receive presentation of the results from the City's independent auditor's examination of the City's financial reports for fiscal year ending June 30, 2022;
2. Accept and file the reports; and
3. Adopt Resolution No. 2023-27, to reallocate and appropriate surplus General Fund fund balance.

BACKGROUND

The City Council has engaged the Certified Public Accounting firm of Chavan & Associates LLP, to serve as independent auditors of the City's financial reports. This is the fourth year with this firm. The scope of work performed by the auditors encompassed examinations of the City's:

- Basic Financial Statements;
- Albany Police and Fire Relief or Pension Fund;
- Alameda County Transportation Commission (ACTC) Measure B Fund, Measure BB Fund, and Vehicle Registration Fee Fund Compliance Reports;
- Transportation Development Act Reports; and
- A review of the calculation used for the annual adjustment to the City of Albany Appropriations Limit.

In addition, as part of their assignment, the auditors' report their findings and recommendations regarding the City's internal control structure.

State law dictates that a municipality may use an auditor for no more than 5 years. The fiscal year 2022-23 audit will be the fifth year with the firm. Staff will be issuing a Request for Proposal of Audit Services in late 2023, early 2024 for the fiscal year 2023-24 audit.

DISCUSSION/ANALYSIS

Annually, the City Council is presented with the City's financial reports. Previously known as the Comprehensive Annual Financial Report (CAFR), the Governmental Accounting Standards Board updated the title of this report in October, 2021 to read Annual Comprehensive Financial Report (ACFR). This was a name change, only; there are no substantive changes to the information being reported.

The complete Annual Comprehensive Financial Report (ACFR) for fiscal year ending June 30, 2022 is included as Attachment 1 to this report. This staff report is a brief overview of the City's financials. A more in-depth review can be found in the Management Discussion and Analysis found at the beginning of the ACFR.

Financial Overview

The change in net assets is a snapshot of the financial results at the highest level. For the purpose of this staff report, the information is presented separately for Governmental Activities (Table 1) and Business Type Activities (Table 2).

It is important to note that for both the Governmental Activities and Business Type Activities tables, assets overwhelmingly consist of capital assets (e.g. land, infrastructure, buildings, and equipment). These assets are not available for future spending. It should also be noted that the current asset balances include amounts that may be subject to restrictions on how they are used. Available general fund balances are discussed later in this report.

Governmental Activities Net Position (Table 1)

	2022	2021	\$ Change	% Change
Current and other assets	40,709,662	35,924,427	4,785,235	13.32%
Capital assets	53,158,307	54,393,587	(1,235,280)	-2.27%
Total assets	93,867,969	90,318,014	3,549,955	3.93%
Current liabilities	7,530,308	7,582,287	(51,979)	-0.69%
Noncurrent liabilities	50,530,442	66,214,708	(15,684,266)	-23.69%
Total liabilities	58,060,750	73,796,995	(15,736,245)	-21.32%
Net position:				
Invested in capital assets, net of related debt	36,275,403	37,380,868	(1,105,465)	-2.96%
Restricted	21,331,504	18,618,011	2,713,493	14.57%
Unrestricted	(29,312,661)	(31,777,771)	2,465,110	-7.76%
Total net position	28,294,246	24,221,108	4,073,138	16.82%

As seen in Table 1, the Net Position for Governmental Activities the City's net position has increased. This is mainly due to an increase in the City's outstanding liabilities as CalPERS most recent actuarial valuation includes a significant increase in market value. This number may change drastically year to year depending on investment returns. For example, the year presented above included an 18% return on investments, however, the next actuarial valuation will show a 6% loss, anticipated to greatly increase the noncurrent liabilities shown on the City's financial statements.

Table 2 represents the Business Type Activity which consists solely of the Sewer Enterprise Fund. The City collects user fees and provides for the maintenance and operation of the sanitary sewer collection system.

Business Type Activities Net Position (Table 2)				
	2022	2021	\$ Change	% Change
Current and other assets	6,163,947	6,404,089	(240,142)	-3.75%
Capital assets	31,052,250	29,600,361	1,451,889	4.90%
Total assets	37,216,197	36,004,450	1,211,747	3.37%
Current liabilities	785,383	796,111	(10,728)	-1.35%
Noncurrent liabilities	2,736,100	3,345,738	(609,638)	-18.22%
Total liabilities	3,521,483	4,141,849	(620,366)	-14.98%
Net position:				
Invested in capital assets, net of related debt	27,706,512	25,656,689	2,049,823	7.99%
Restricted	-	-	-	0.00%
Unrestricted	5,988,202	6,205,912	(217,710)	-3.51%
Total net position	33,694,714	31,862,601	1,832,113	5.75%

As seen above, the City's net position in the Sewer Fund increased due to Public Works completing the installation of several major sewer lines. These increases are anticipated for the next few fiscal years before they even out as the City reaches its replacement goals.

Major Funds

In order to be designated a "Major Fund," certain minimum criteria must be met. Those criteria generally include comparison of revenues, expenditures, and assets compared to all funds. The format of the Fund Financial Statements presents individual information for each of the Major Funds and then all other Governmental Funds are reported in a single column. Table 3 provides a summary of the Governmental Fund revenue, expenditures, and changes in fund balance for the year ending June 30, 2022.

**Summary of Revenues, Expenditures,
and Changes in Fund Balances (Table 3)**

	General Fund	Street & Storm Funds	Non-Major Governmental Funds	Total Governmental Funds
Revenues	23,891,883	1,214,596	12,924,323	38,030,802
Total expenditures	26,316,388	365,779	7,590,228	34,272,395
Net transfers	3,964,750	(344,471)	(2,782,660)	837,619
Net change in fund balances	1,540,245	504,346	2,551,435	4,596,026
Fund balances, beginning of year (as adjusted)	10,048,022	4,616,576	15,702,600	30,367,198
Fund balances, end of year	11,588,267	5,120,922	18,254,035	34,963,224

Auditors' Report to City Council

Each year, the independent auditors report any material findings regarding internal accounting controls, management's compliance with generally accepted accounting principles, management's judgement in applying accounting estimates, disagreements between the auditors and management, and difficulties performing the audit. The auditors reported one finding for fiscal year ending June 30, 2022, repeated, although more refined, from the previous year. The section titled 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 and Schedule of Findings and Responses, is included within the attached ACFR. Additional detail on staff response is discussed in the Next Steps section of this report.

General Fund Balance

The City's overall general fund balance, as shown in Table 3, is \$11,588,267. The Council approved the use of \$1.48 million to cover the excess of expenses over revenue in the FY2022 budget, leaving just over \$10 million in undesignated fund balance. Based on the Fund Balance Policy passed by Council in June 2019, 25% of current year expenditures, or just under \$7 million, must be held in reserve.

The remainder, approximately \$3 million, is available surplus. In prior years, staff suggested leaving this amount in the General Fund as the effects COVID-19 would have on the City's finances were unpredictable. Coming out of the pandemic, the City has been fortunate to see stable, if not increasing, revenues, encouraging the use of these reserves for future planning purposes. Staff are not suggesting the reallocation of all surplus funds as increasing expenses, including pension costs, are still a concern and some general fund balance may be needed to cover budgeted deficits until additional general fund revenue can be realized.

Staff suggest reallocating \$2.3 million unrestricted fund balance in the following manner:

Utility Users' Taxes

In November, 2020 voters passed an increase to the Utility Users Tax on Gas and Electric, and extended the tax to Water. While the increase passed as a general tax, the measure stated in part:

... the City Council will endeavor to expend at least one-third (1/3) of the additional revenue generated from the increase in the... rate (above 7%) for the following spending priorities:

1. Those Action Items in the City's Climate and Adaptation Plan, approved by the City Council on December 2, 2019, and as it may be amended from time to time by the City Council.
2. Additional environmental sustainability programs as may be authorized by the City Council.

One third of the taxes generated from the increased rates for FY2021-22 equated to \$171,469. \$28,000 in expenses were identified as environmental sustainability expenses associated with the increased funding during the fiscal year. Since there is a surplus for FY2021-22, staff recommend that Council reallocate the remainder of the funds associated with the fiscal year 2020-21 UUT increase, \$143,469, to the Climate Action and Adaptation Reserve Fund for future sustainability project use.

Outstanding Pension Liability

Section 6 of the City's General Fund Reserve Policy lays out uses of general fund balances exceeding the 25% fund balance policy. The first of these uses is to pay down unfunded pension liabilities. While the CalPERS actuarial reports used to complete the fiscal year 2021-22 financial statements show a significant decrease in the City's outstanding pension obligations, this is misleading. The investment year used for these reports was unusually high (18% return) and the very next year the funds lost just over 6%. There will be a significant increase in outstanding pension obligations shown on the fiscal year 2022-23 financial statements once the newest CalPERS actuarial reports become available.

Even though the statements appear positive, it is still important that the City address future pension obligations. Staff suggest moving \$775,000 into a Pension Reserve Fund to offset pension increases to the general fund anticipated over the next several years. While this will not reduce the City's obligations as listed on the financial statements, it will help offset the general fund increases that will be needed for pension obligations over the next decade.

The Financial Advisory Committee has been focused on the City's pension obligations and their work will be presented along with the biennial budget next month.

Asset Reserve Funding

The second two uses of excess general fund balance laid out in Section 6 of the General Fund Reserve Policy are capital improvements and equipment purchases. Council passed the City's Capital Reserve Fund Policy in May, 2020 for the purpose of saving for these purchases. The Council will receive an update on anticipated needs over the next five years when the biennial

budget is presented next month, but the needs far exceed the amount currently in Reserve Funds and no other funding mechanisms have been identified for these purchases.

Staff recommend allocating the remaining \$1.4 million from the excess General Fund balance to fund capital reserves as follows;

Reserve Fund	Minimum Funding Level	Current Balance (04/20/2023)	Suggested Contribution	Proposed Ending Balance
Community Development Reserve Funds (0004/2208/2401)	\$100,000	\$613,683	\$100,000	\$713,683
Emergency Medical Services (EMS) Reserve Fund (2204)	\$100,000	\$112,250	\$100,000	\$212,250
Fire Department Reserve Fund (2205)	\$100,000	\$96,869	\$250,000	\$346,869
General City Building Reserve Fund (2007)	\$250,000	\$367,686	\$200,000	\$567,686
IT Equipment Reserve Fund (2207)	\$50,000	\$272,957	\$350,000	\$622,957
KALB Equipment Reserve Fund (2209)	\$50,000	\$50,000	\$0	\$50,000
Police Department Reserve Fund (2202)	\$100,000	\$58,974	\$200,000	\$258,974
Public Works Reserve Fund (2210)	\$100,000	\$250,000	\$100,000	\$350,000
Recreation Reserve Fund (2211)	\$100,000	\$170,056	\$100,000	\$270,056

These recommendations are being made in consideration of departmental operational needs as expressed in Section 7.2 of the biennial operating budget, to be updated next month, and ongoing Council priorities.

SUSTAINABILITY CONSIDERATIONS

Not applicable.

SOCIAL EQUITY AND INCLUSIVITY CONSIDERATIONS

Not applicable.

CITY COUNCIL STRATEGIC PLAN INITIATIVES

GOAL 5: Increase Revenue to Sustain City Services; OBJECTIVE: Identify funding and strategies to manage unfunded pension liabilities

FINANCIAL CONSIDERATION

Allocation of excess General Fund balances assists the City with long-term planning and paying down outstanding liabilities. These items put the City in a better position moving forward. While these recommendations were presented to the Financial Advisory Committee, due to delays presenting the audited financial statement, the Committee did not have the

information necessary to make a formal recommendation to Council on staff's suggested allocations. That said, staff are requesting that these allocations be made in advance of the biennial budget presentations so that the amounts indicated above can be relied upon for planning purposes.

NEXT STEPS

Finance staff have made significant effort to correct prior year reporting and systems issues and continue work towards refining policies and procedures. The single finding reported for fiscal year 2021-22 is a repeat finding, however the finding becomes more refined over time as staff address pieces of the year end closing process each year. Staff have balanced correcting issues uncovered during prior audits while ensuring ongoing financial stability for the City. Below is a listing of items resolved from prior audits, as well as discussion of the current year finding:

Items Resolved from FY 2018-19

Grant Tracking (2019-005)

Disbursements (2019-006)

Cash Receipt (2019-007)

Internal Service Funds and Related Liabilities (2019-008)

Items Resolved from FY2019-20

Capital Assets and Related Debt (2020-001)

Cash and Investments (2020-003)

Long-term Debt (2020-004)

Finding for FY2021-22

Financial Reporting and Closing (2022-001) Repeat Finding

While this is a repeat finding, the severity was decreased from a Material Weakness to a Significant Deficiency. Staff continue to implement processes and procedures that refine day to day tasks and allow for more detailed reporting at year end. Rollover balances from the 2016 software conversion continue to be addressed as time allows, however staff turnover has pushed off some of these reviews. These items are balance sheet amounts that may slightly inflate amounts the City is due or owes, however, staff are confident that current revenues and expenditures are being accounted for properly and therefore any changes shown on the statements are accurate. Staff will continue to refine month and year end close processes, as well as address rollover balances, as time allows.

Attachments

1. Annual Comprehensive Financial Report for the year ended June 30, 2022
2. Resolution No. 2023-27, to reallocate and appropriate surplus General Fund fund balance