

FINANCIAL AUDIT ADVISORY COMMITTEE

REPORT

Thursday, January 11, 2018

Present: Councilor Gentile (Chair), Councilor Grossman, Councilor Markiewicz, School Committee Member Bridget Ray Canada, Citizen Representative Tony Logalbo, and Citizen Representative Howard Merkwitz

Also present: Sue Dzikowski (Comptroller), Julie Kirrane (Long Range Planning Manager; School Department), Councilor Danberg, and Matt Hunt, CPA (Clifton, Larson, Allen, LLP)

06/30/2017 Audit

The Committee met with Matt Hunt of Clifton, Larson, Allen, LLP (CLA), the City's external auditing firm, to discuss CLA's review of the City's Comprehensive Annual Financial Report (CAFR) and to review the auditor's draft of the Reports on Internal Control and Federal Awards related to the Fiscal Year 2017 Audit. The draft Management Letter is not complete and its review will take place at a later meeting. The Committee members received copies of all completed draft documents related to the audit. Once finalized, the CAFR, Reports on Internal Control and Federal Awards, and the Management Letter will be available on the City's website on the Comptroller's page.

Comprehensive Annual Financial Report

Mr. Hunt reviewed the audit of the City's Comprehensive Annual Financial Report (CAFR), including the Management's Discussion and Analysis (MD & A) and the Budget to Actual Statement portions of the CAFR. Comptroller Sue Dzikowski prepares the MD & A. Mr. Hunt added that the audit process went well overall. The budget to actual statements provides a useful window into how the City's general fund performed. The CAFR also includes the Pension Trust Fund and the Other Post-Employment Trust Fund Statements.

The primary fieldwork by the auditor began in September 2017 and the City provided all information that the auditors requested in a well-organized manner. The City management and staff involved in the audit were responsive to all inquiries. There were no disagreements with management during the audit process and everything went smoothly. Clifton, Larson, Allen also included a quality control review by an independent partner outside of the auditor's Massachusetts office.

The CAFR has an introductory section that includes a letter of transmittal, a financial section that includes the auditors' opinion and the management's discussion and analysis, and a statistical section. The only GASB Statement of any impact this year is GASB 74 that requires the City to report its Other Post-Employment Benefits (OPEB) liability in a manner that aligns

with reporting requirements for pension liability in the CAFR. The OPEB liability is not on the balance sheet this year but is part of the CAFR footnotes.

There are no new audit standards that result in real changes to the FY 2017 audit. The auditor's opinion on Fiscal Year 2017 Comprehensive Annual Financial Report is unmodified (i.e., the financial statements present fairly, in all material respects, the City's financial situation), which is in keeping with prior years. Part of the opinion includes reliance on the auditors that provide the audit of one of the City's small component units, the Newton Commonwealth Foundation.

Mr. Hunt reviewed the financial highlights of the audit of the CAFR. The Government Wide Financial Statements are reported on Pages 18-21 of the CAFR, which shows the City's assets, liabilities, and net position. The key information is the fund balance information, particularly for the General Fund. The City's assets are currently valued at approximately \$748 million of which \$195.5 million is from cash and investments and \$554 million is from capital assets. The City's current liabilities are approximately \$958 million of which \$283 million are bond payable obligations, \$283 million are net OPEB obligations, and \$317 million are net pension liabilities.

The City's has a negative net position of \$180 million, which is an increase of \$19.6 million from last year, which is largely attributed to a \$36 million increase in OPEB and pension liabilities. In addition, there is an unrestricted *deficit* of \$485 million in governmental activities, which is attributable to the recognition of the pension and Other Post-Employment Benefit obligations. The City's negative net position is similar to that of other municipalities. The City does have a plan for funding both the pension liabilities and the OPEB liabilities.

The City's general fund debt service compares favorably with other communities at 4.8%. It is a .4% decrease over the past fiscal year. Debt service is not absorbing a large piece of the City's operating budget. The general fund balance at the end of FY 2017 was \$67 million, which includes 3.6 million in restricted funds, \$14.9 million set aside for FY 2018 and 2.4 million of assigned funds and the unassigned balance. The City continues to build its unassigned fund balance primarily through increasing the City's Rainy Day Stabilization Fund. The FY 2017 unassigned balance is \$46.2 million, which includes \$19.7 million in the Rainy Day Stabilization Fund. The MDMA on Page 12 of the CAFR show trends on how balances in the unassigned funds have grown over the past five years. In addition, Pages 24-26 provides a reconciliation of the governmental fund balance totals to the statement of net position that pinpoints how the General Fund compares to the budget.

Mr. Hunt reviewed the financial highlights related to the enterprise funds and internal service funds. The sewer enterprise fund ended the fiscal year with assets totaling \$90 million and liabilities of \$22 million, which includes both pension and OPEB liabilities. There is an increase of \$5.9 million in net position over last fiscal year. The water enterprise fund ended the fiscal year with assets of \$78 million and liabilities of \$30 million, which represents an

increase of \$4 million in net position. The Storm Water Enterprise assets total \$5 million and its liabilities total \$1.2 million. The internal service assets were \$35.3 million at the end of the fiscal year and liabilities totaled \$13.5 million, consisting mainly of incurred but not reported health claims liabilities and workers compensation liabilities. The net position of the internal service funds is \$22 million. Overall, the internal service funds increased by about \$6 million. Further information on the City's enterprise funds, insurance funds can be found on Pages 28-30.

Mr. Hunt continued with a review of the fiduciary funds financial statements found on Pages 31-32 of the CAFR. The City's Pension Trust Fund total is \$306 million increasing by \$16 million over last year and the OPEB Trust Fund total is \$6 million, which is an increase of \$2.4 million over last fiscal year, which is partially due to a \$555,000 return on investment.

In addition, Mr. Hunt provided a quick review of the footnotes included in the CAFR, which can be found on the City's website on the Comptroller's webpage. Note 10 of the CAFR footnotes relate to long-term dept. Total outstanding long-term debt is \$297.1 million (Note 10). The city has issued \$66 million of general obligation bonds and retired \$64 million in debt from general fund bonds. The OPEB unfunded actuarial accrued liability is \$645 million, a decrease of \$77 million from the prior year's \$722 million (Note 12). The decrease is a result of increasing the discount rate to 3.58% from 2.06%. The OPEB liability is 0.93% funded with assets of \$6 million. The City's annual OPEB costs are \$48.9 million and City contributions to the cost are \$20.8 million. The net OPEB obligation as of June 30, 2017 is \$289.8 million. The total pension liability is \$636 million. This year the liability is 48.6% funded, which is an increase of .6% from the prior year funding. For further information on the pension liabilities, refer to Pages 74 – 76 of the CAFR.

Government Accountability Office (GAO) and Office of Management and Budget (OMB) A-133 Reports

The independent auditor provides reports on the internal control over federal and state financial reporting and on compliance. The report does not provide an opinion on internal controls but includes any significant deficiencies and/or material weaknesses in internal controls and material noncompliance to laws and regulations.

There was a reduction in the number of major grants reviewed as the threshold for the dollar value of grant review was increased from \$300,000 to \$750,000. The two major programs reviewed were the Child Nutrition and the SPED Programs, which receive grant funding. There were no financial reporting findings and no current year grant findings. The City received an unmodified opinion on federal grant award programs; however, significant deficiencies were identified that are not considered material weaknesses.

As part of the audit of the Child Nutrition Program, the auditor identified insufficient information to support eligibility for free or reduced lunch benefits in four of 40 applicants

tested. The auditor recommends implementation of procedures to ensure that all applications and supporting records are preserved for all participants in the program. In addition, the verification for qualification for free and reduced price was not done in accordance with the federal guidelines. The recommendation is to implement a process to ensure the verifications are done in accordance with the uniform guidelines.

The second finding is related to the SPED Program's special reporting requirements. One of the student files tested did not contain evidence of a signature review and approval. The auditor recommends putting procedures in place to make sure that all student files have the appropriate review and signatures.

Next Meeting

The next meeting of the Financial Audit Advisory Committee is scheduled for February 8, 2018 at 8:15 PM. The Committee will discuss the draft Management Letter.

The Committee adjourned at 9:30 a.m.

Respectfully submitted,

Leonard J. Gentile, Chair