

City of South Daytona

Office of the City Manager / Department of Finance

Post Office Box 214960 • South Daytona, FL 32121 • 386/322-3060 • FAX 386/322-3099



MEMORANDUM

To: James L. Gillis, Jr., City Manager

From: Jason E. Oliva, Finance Director

Re: Annual Comprehensive Financial Report for the Fiscal Year Ended September 30, 2021

Date: February 2, 2022

Attached, please find the annual comprehensive financial report (ACFR) for the fiscal year ended September 30, 2021. The ACFR provides a snapshot of the City's financial position at fiscal year-end. In the spirit of full disclosure and transparency, I am submitting this summary and analysis to facilitate better understanding of the contents of the report.

Background

The ACFR communicates the City's financial condition and activity in a transparent and organized manner and follows accounting and financial reporting standards established by the Governmental Accounting Standards Board (GASB). The report presents historical and comparative information that can be useful to City staff, elected officials, and external users such as debt rating agencies, businesses, other public agencies, and the City's residents.

Financial statements are prepared by the City and audited by independent auditors. The City selects its independent auditor through a competitive procurement process that includes members of the Audit Selection Committee as proposal reviewers. The City's current independent auditor, James Moore & Co. CPAs, is in its third year auditing the City.

The quality of the City's financial reporting and the ACFR are measured in two ways: (1) an unmodified audit report by the independent auditors; and (2) the Certificate of Achievement for Excellence in Financial Reporting, awarded by Government Finance Officer Association (GFOA). The attainment of the latter is the highest form of recognition in governmental accounting and financial reporting.

Auditors follow audit industry standards established by the American Institute of Certified Public Accountants (AICPA). These standards require auditors to provide an opinion on specific areas of the City's financial statements based on observations, inquiries, testing of transactions, and analysis.

The City's ACFR includes the following major sections and information:

Introductory Section

Letter of Transmittal – prepared by management and used to communicate information on areas that may have an impact on the City’s finances now and in the future. This includes economic factors as well as budget and management factors.

Financial Section (the main body of the ACFR for current year information)

- Independent Auditors’ Report – the City’s report card on the content of the ACFR
- Management’s Discussion and Analysis (MD&A) – provides an analytical overview of the City’s financial status and results for the year
- Basic Financial Statements – reports finances at a point in time (assets - liabilities) and throughout the year (revenues - expenditures), and cash flows
 - City-Wide Statements – overview of financial information including all the City’s operations by financial activity
 - Fund Financial Statements – a detailed look at funds, reporting the Balance Sheet and Statement of Revenues, Expenditures and Changes in Fund Balance
 - Notes to the Financial Statements (Notes) – a narrative explanation that accompanies the Basic Financial Statements

Required Supplementary and Supplementary Information Sections

- Budget to Actual Comparisons – for all governmental funds with a legally adopted budget
- Notes to Required Supplementary Information
- Pension Information – schedule of changes in the proportionate share of net pension liability and related ratios; schedule of contributions by plan
- OPEB Information – schedule of changes in the net Other Post-Employment Benefits (OPEB) liability and related ratios; schedule of contributions
- A breakout of individual non-major funds – for funds that were presented in a cumulative manner in the Financial Section

Statistical Section (current and historical information – up to 10 years)

- Financial Trends
- Revenue Capacity Information
- Debt Capacity Information
- Demographic and Economic Information
- Operating Information

Discussion

The attached ACFR for FY 2020-21 has received an unmodified opinion by James Moore & Co. An unmodified opinion communicates that the financial statements are fairly presented, and that the information used in the report is reliable. In their written communications to Council, the auditors note that they encountered no significant difficulties with management in performing or completing the audit.

Statement on Auditing Standards (SAS) 114 establishes standards for the auditors’ communication with those charged with governance. These statements require the auditors to consider and report on internal controls, significant audit findings, and other matters as prescribed in the standards as they relate to the audit of the financial statements. The letters that satisfy the SAS requirements are attached to this report.

The following is an explanation of some key indicators reported in the ACFR.

General Fund Balance

The most notable measure of a City's financial health is the General Fund balance. As presented in the Basic Financial Statements, the City's General Fund assets exceeded liabilities to the good by \$5,475,859 as of September 30, 2021 (page 43, total fund balance). This balance is comprised of several categories, as follows, and are listed from money not available to spend at all to unassigned balances to be used as desired:

\$16,278 nonspendable fund balance includes amounts that are not in a spendable form and cannot be used to meet current obligations, such as prepaid items and advances to other funds;

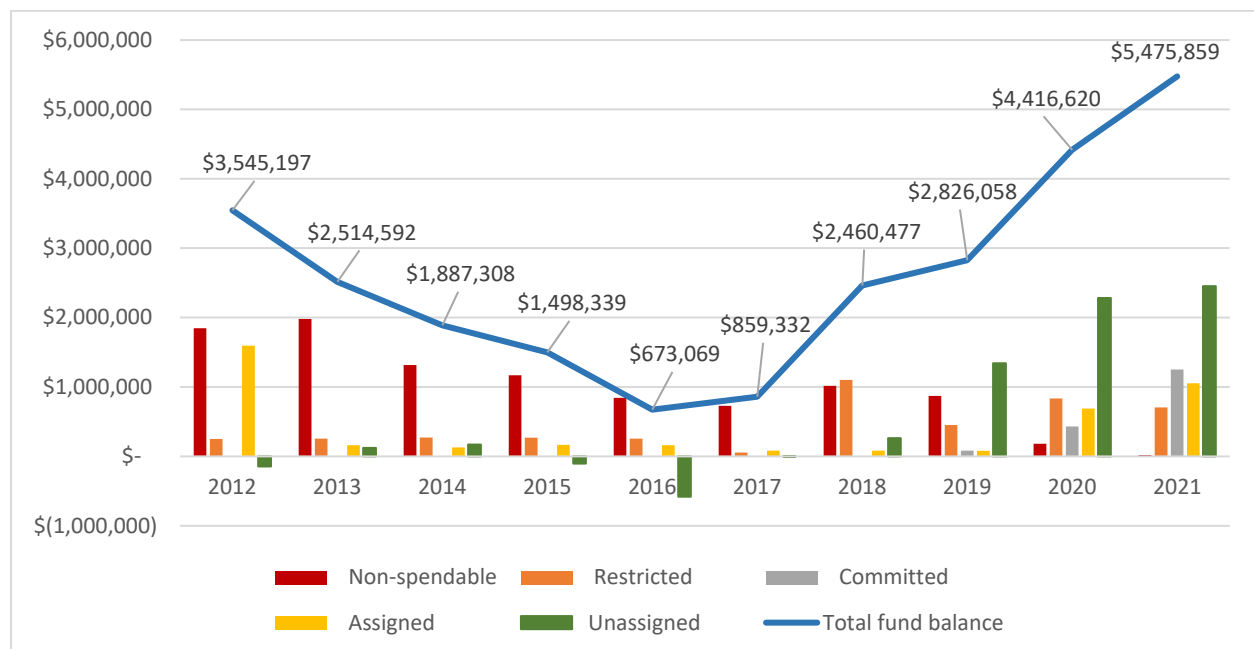
\$703,596 restricted fund balance are restricted for a specific purpose as stipulated by either external resource providers or enabling legislation such as debt service payments and impact fees;

\$1,250,000 committed resources represent amounts designated for a specific purpose by formal action from City Council, this balance is the disaster recovery reserve. City policy requires that funds committed to disaster recovery have a balance of \$1,250,000 by 2026;

\$1,052,499 assigned funds set aside for specific purposes based on budget priorities (i.e., cell tower maintenance; prior year reappropriations; and capital); and

\$2,453,126 in unassigned funds. City policy requires the unassigned fund balance for the General Fund to be between 15-20 percent of the following years operating budget expenditures. At fiscal year-end, unassigned fund balance represents 20% of the 2022 budget. City policy allowed unassigned fund balance over 20% to be committed for the disaster recovery reserve or for future capital outlay.

GENERAL FUND BALANCES



Citywide Net Position

The Statement of Net Position, like a balance sheet, reports total assets and liabilities of the City as of September 30, 2021. The total net position of the City for all activities was \$27,290,405 (page 41, total net position). The City's total net position increased \$3,399,009 primarily due to debt reduction, a continued focus to increase fund balance in the General and Utility Service Funds, and a decrease in post-employment benefit liabilities. To increase fund balance, the City originally budgeted a \$50,000 transfer to reserve that was increased to \$78,000 during the mid-year budget adjustment. The general fund had many revenue sources come in higher than budgeted and had \$551,183 in expenditures that have been assigned for the subsequent year budget. The Utility Service Fund also had \$237,516 in expenditures that are being rolled into the subsequent year budget. These delays in major purchases allowed the funds to be under budget for the current fiscal year but will be spent in the subsequent year.

Net position is broken out into three categories: capital, restricted, and unrestricted.

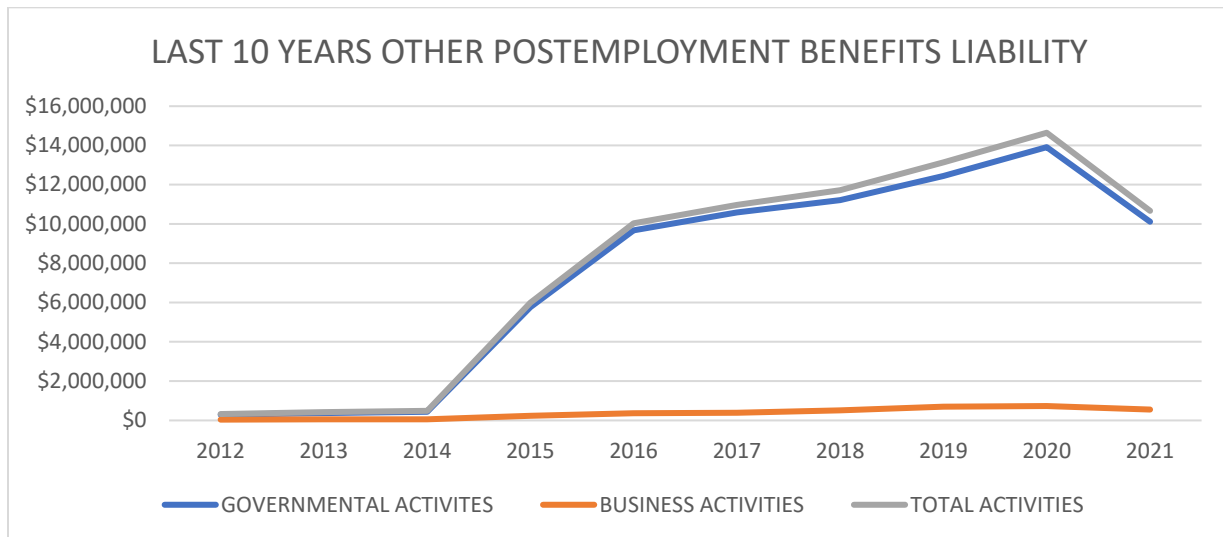
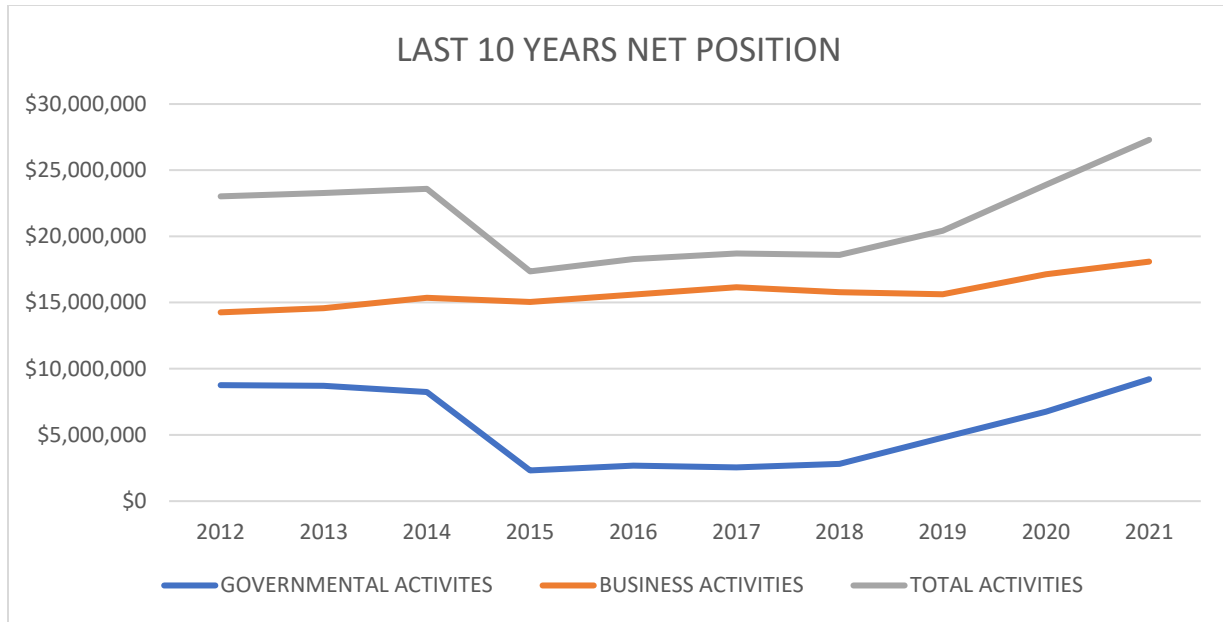
Net Investment in Capital Assets (\$31,802,889) includes land, buildings, improvements, infrastructure and utility systems, and construction in progress net of depreciation/amortization and related debt.

Restricted Net Position (\$1,633,135) is subject to agreements with creditors, laws or regulations of other governments such as debt service payments and impact fees.

Unrestricted Net Position (deficit balance of \$6,145,619) represents the balance of net position that is neither part of capital assets nor restricted. The main reason for the deficit balance in unrestricted net position is the \$10,476,409 in liabilities recorded for postemployment benefits. Postemployment liabilities reported are for the City's portion of the unfunded liability of the FRS pension plan (\$3,830,091), the net effect of deferred inflows and outflows (\$4,977,206) and the other postemployment benefits (OPEB, \$1,669,112) for retiree healthcare. The unfunded liability in the pension plan represents the amount the City would have to contribute for its employees in the plan in the hypothetical situation that FRS stopped existing, and payments were made to all retirees. OPEB recognizes the liability incurred by the City for providing health care coverage to employees after they retire. Even though the retirees pay the full amount of their own premium, the liability is recorded because the higher rate to cover retirees is blended with the rate to cover active employees. These liabilities are recorded per Governmental Accounting Standard Board reporting requirements even though the City does not have an obligation to fund or budget for these liabilities for general government activities. If the City was not required by GASB to record these liabilities, the City's Unrestricted Net Position would be a surplus balance of \$4,330,790.

GASB 68, accounting for pensions, was implemented in 2015 and the pronouncements impact on unrestricted net position can be seen in the following graphs.

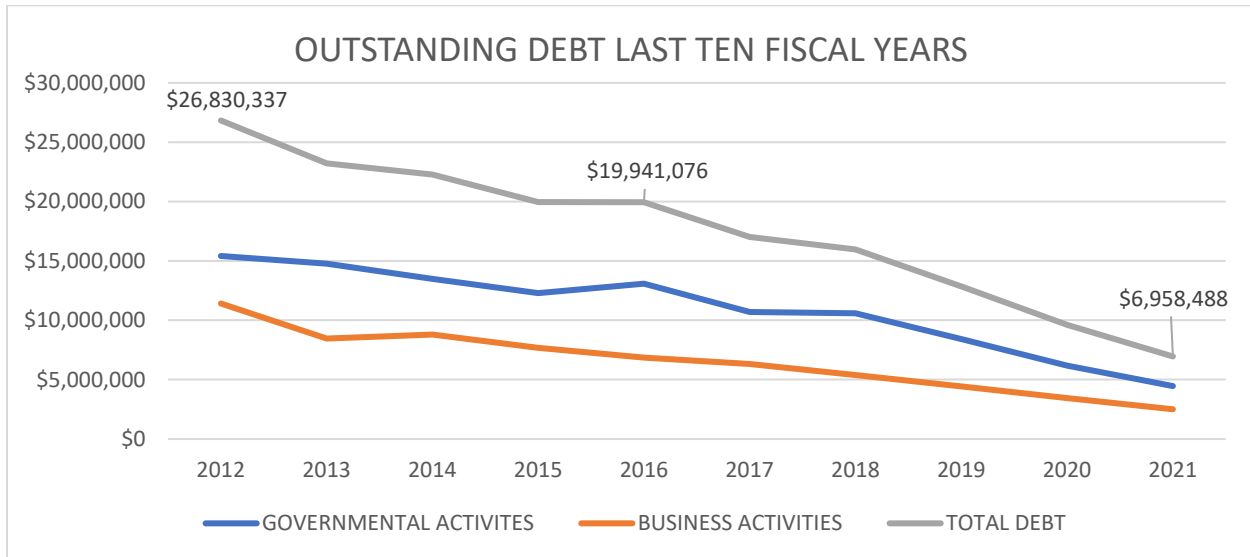
The City did receive \$3,275,583 from the American Rescue Plan Act during the fiscal year. These funds **did not** make an impact to the net position of the city for fiscal year-end 2021. Since the City has not yet spent any of the money for approved projects under the program, the revenue is considered to be unearned and is accounted for as a liability on the balance sheet (page 43, Capital Projects Fund Balance Sheet). The unearned revenue liability offsets the increase to the cash asset resulting in no impact to fund balance.



Debt

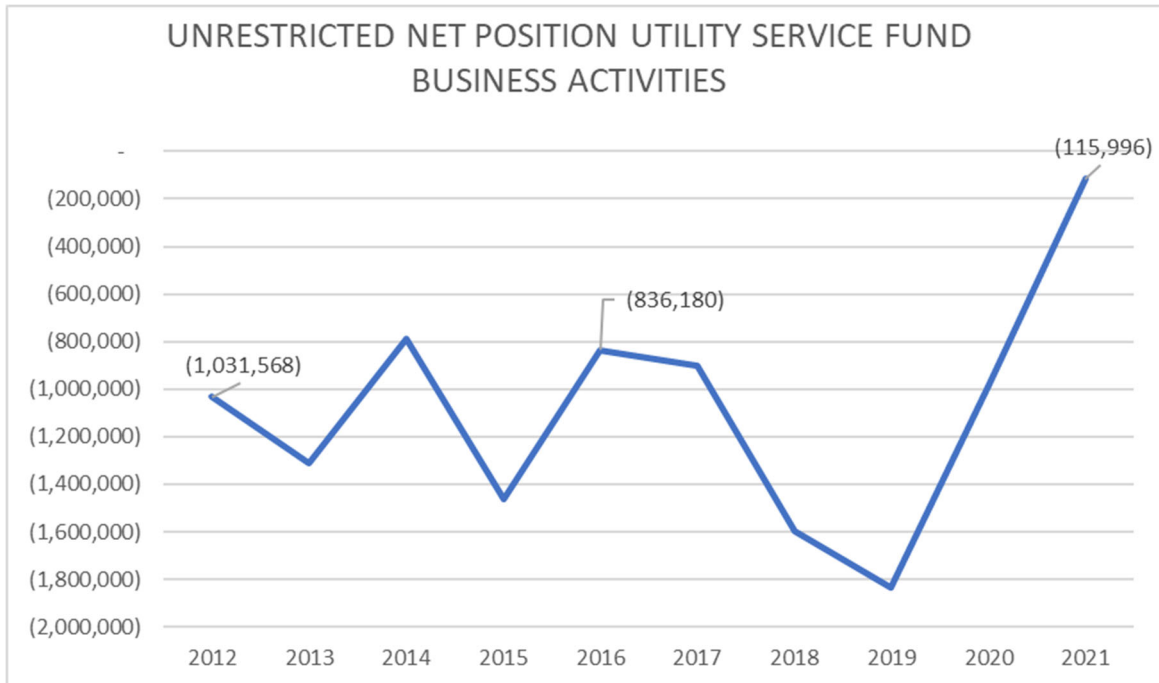
One of the main reasons for the upward trend in Net Position is the continued commitment by the City to eliminate debt. During the current fiscal year, the City reduced outstanding debt by \$2,654,546 as the City has made a commitment to reduce debt via a combination of making additional principal payments and not taking out any additional debt. A narrative summary of the City's debt can be found on pages 36 & 37 in the MD&A section of the ACFR. More detailed information such as amortization schedules about the City's long-term debt can be found in notes to the financial statements section Notes 10 and 11 on pages 69-75 of the ACFR. Specifically, on page 71, you can see the reduction to the balloon payment due on Wells Fargo Capital Improvement Revenue Note # 117. The balloon payment due on June 30, 2023 has been reduced an additional \$330,000 this fiscal year and the original amount due of \$1,314,559 has now been reduced to \$166,559. The City will continue to use proceeds from the additional .4 mills dedicated for debt to make additional principal payments in future years. This will not only retire the debt early but generate savings because reducing the outstanding balances decreases the amount the City will have to

pay in interest each year. The City paid a total of \$314,417 in interest in the current fiscal year. Governmental funds paid \$207,286 (page 45, total governmental funds interest) and the Utility Service paid \$107,131 (page 53, interest expense).



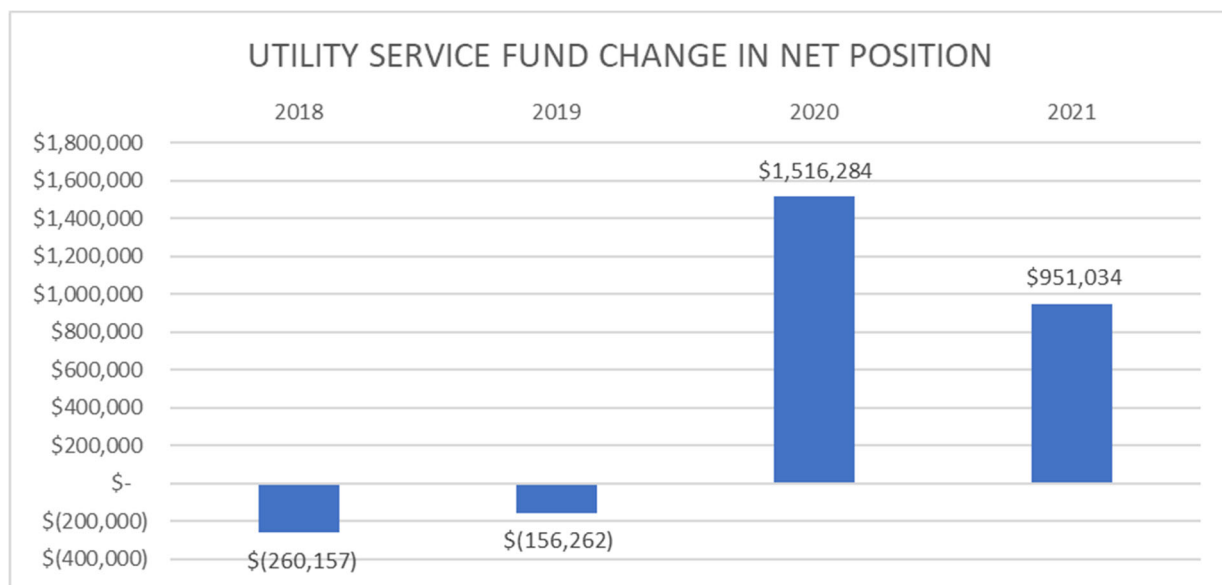
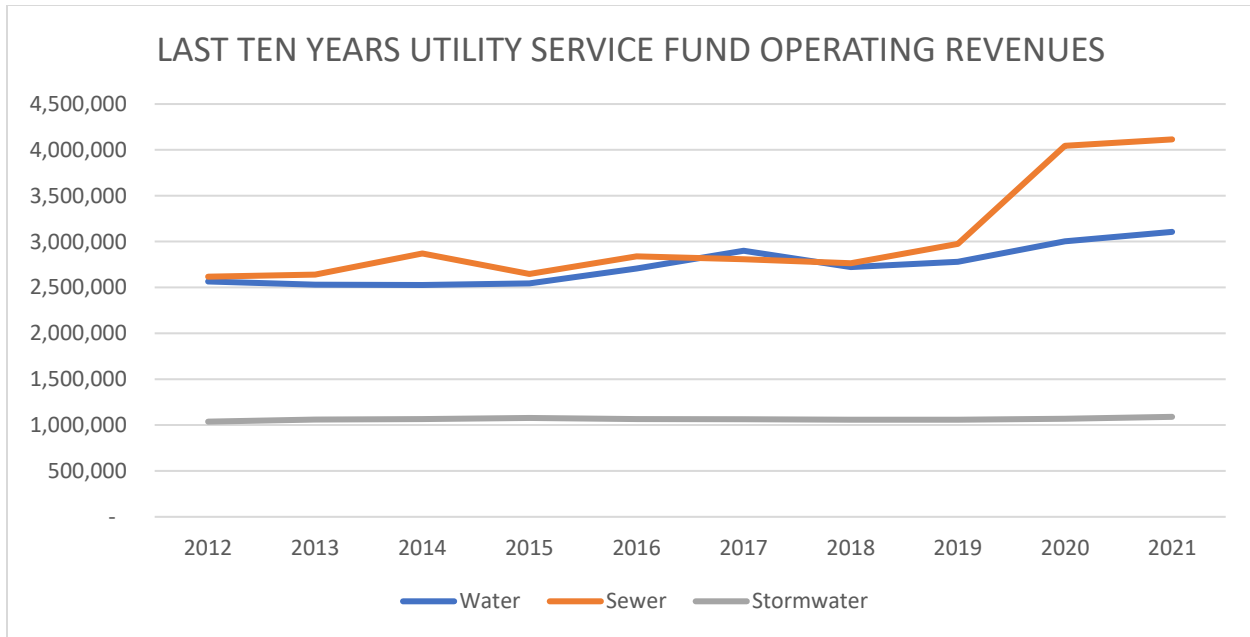
Utility Service Fund

The Utility Service Fund is reported with both a long-term and short-term focus. The City will need to increase revenues and decrease debt to improve the deficit unrestricted net position of \$115,996 (page 50, unrestricted deficit). The rate changes implemented by the City in 2019 are helping the unrestricted amount to trend in a positive direction. In fiscal year-end 2021 net position increased by \$951,034. Keep in mind that \$237,516 of that increase is from capital expenses not incurred in the fiscal year 2020-2021 that will be expensed in fiscal year 21-22. City policy requires that net position in the utility service fund be between 12-20 percent of the following years operating expenses. This amount is \$1,760,550 short of the 12% minimum required. Since this number is below the 12% goal per Resolution No. 2020-34, a plan must be developed and adopted to return the unrestricted net position to 12% or greater threshold within two years.



While the unrestricted portion of net position in the utility service fund increased by \$870,807 in the current fiscal year, the City must remain diligent in reducing expenditures and defer capital, when possible, to restore net position in the Utility Service Fund.

The Utility Service Fund was able to avoid the repeat audit comment findings and recommendations. The Utility Service Fund repaid the remaining \$178,011 owed to the General Fund during the current fiscal year. The fund also did have cash on hand equal to the \$987,940 customer deposits liability. Those repeat findings had resulted in a letter to the Mayor from the Florida Legislature Joint Legislative Auditing Committee requesting a response for repeat audit findings. The Utility Service Fund also was able to restrict \$278,617 for renewal and replacement. The \$500 unrestricted cash in the Utility Service Fund at fiscal year-end represents cash on hand in the Utility Billing Department (page 50).



The total increase in net position for business-type activities (water and sewer) was \$951,034. The growth, in large part, is attributable to rate increases for water and sewer enacted in September 2019. While the Utility Service Fund still is \$1,760,550 short of the 12% minimum net position required by City policy, the fund is trending in a positive direction. *It is imperative that any rate increases in the new contract with the City of Daytona Beach for wholesale water and sewer services be carefully analyzed to make sure that the City of South Daytona rates for services will still generate an increase to net position.*

General Fund Budget Highlights

Evaluating the City's financial performance relative to the adopted budget is an essential input in demonstrating accountability. The Statement of Revenues, Expenditures, and Changes in Fund Balance-Budget and Actual for the General Fund can be found on page 47.

Original budget compared to final budget. During the year, a mid-year budget amendment was made to adjust the original estimated revenues or budget appropriations. Overall, the general fund budget was increased by \$759,550. The significant variances between the original budget and final amended budget are as follows:

- Budgeted intergovernmental revenue increased by \$147,717 mostly attributed to the Florida Department of Revenue revising their revenue estimates in December 2020 in response to a better performing economy during this pandemic.
- Federal grants were increased by \$66,031 due to the Police Department receiving a 2020 Coronavirus Emergency Supplemental Funding reimbursement grant for Covid-19 related expenditures.
- Budgeted revenues in Charges for Services increased by \$24,117. Most of this change is due to an increase in environmental service (roll-off services) of \$101,177 and a decrease in culture and recreation activity revenues of \$77,060 (due to the cancellation of sports programs and events during the pandemic). Environmental services changes in revenues are offset by changes in expenses incurred by providing these services.
- Budgeted transfer from reserves increased by \$521,685 primarily due to the \$455,154 of Coronavirus Aid, Relief and Economic Security (CARES) money recognized in FY 19/20 and \$66,531 in budgeted expenditures for FY 19/20 that did not incur until the current fiscal year due to delays in projects caused by the pandemic.

Generally, other movement of the appropriations between departments were not significant.

Final budget compared to actual results. Revenues reported an overall negative variance in the General Fund with actual revenues lower than the final FY 2021 Budget by \$114,943. Most of this variance is primarily due to the following:

- Transfer from reserves was budgeted for CARES. revenue of \$455,154 that had been assigned in the previous fiscal year.
- Communication service tax, state revenue sharing, sales tax, fines and forfeitures all **were trending high during the fiscal year, but staff did not adjust the budget at midyear to allow the additional funds to increase reserves.**

Expenditures reported an overall positive variance in the General Fund with actual expenditures lower than the final FY 2021 Budget by \$1,200,645. This variance is attributed to a continued focus on cost containment efforts, salary attrition due to vacancies across the community development, police, and parks departments, and not needing to spend budgeted contingency money.

The Covid-19 pandemic has resulted in project and capital outlay delays. Capital outlay was 34% of budget which represent \$565,334 under the budgeted amount. Most of these expenditures were delayed due to COVID-19 and are being rolled into the subsequent budget. The amount is reported as part of the general fund balances assigned for the subsequent year budget.

Other Fund Highlights

The fund balance of the City's Redevelopment Trust Fund increased by \$197,272 during the current fiscal year. This increase is a result delays in the completion of the Riverfront Park Playground Replacement and other capital purchases. Due to those delays, \$188,363 is being moved to the subsequent budget.

The transportation fund balance decreased by \$39,587. Fund balance that remains in the transportation fund will be used to fund transportation related capital projects and expenditures in future years.

The Capital Project Fund was increased at mid-year to account for the proceeds from the Coronavirus Local Fiscal Recovery Fund (CLFRF) as provided for by the American Rescue Plan Act (ARPA). Along with budgeting grant revenue, the City budgeted for capital outlay in the Capital Projects Fund. The Capital Projects Fund did not have any revenues or expenditures recorded at fiscal year-end. The City had budgeted for \$2,748,254 in federal grants to recognize the receipt of funds from the American Rescue Plan Act (ARPA). While the City has received \$3,275,583 in cash in ARPA funds, none of the revenue has been recognized as it is unearned revenue. Once the City spends money on ARPA eligible expenditures, the revenues will be recognized.

Capital Assets

One of the major components of the financial recovery has been continued deferral of maintenance and capital replacement. To create a sustainable capital plan, the City considered all capital needs, assessed its fiscal capacity, is planning for potential debt issuance while understanding the potential impact on reserves and operating budgets.

At fiscal year-end 2021 machinery and equipment in governmental activities is 69% depreciated. Original cost of the machinery and equipment was \$4,523,3305 less accumulated depreciation of \$3,134,400 resulting in a net book value of \$1,338,905 (page 67, note 9 capital assets).

Conclusion

Overall, the City is trending in a positive direction, but the City needs to stay the course to achieve the desired financial stability adopted by the financial policies as listed in Resolution No. 2020-34. The Utility Service Fund needs to follow the recommended rate increase of scenario 8 as approved in September 2019 and adjust the rates accordingly to reflect potential changes in the new contract with Daytona Beach for wholesale purchases. The General Fund will need to maintain or increase its millage rate to fund capital replacement, offset the increase cost of products used for maintenance, and the pending \$15 minimum wage.