



MEMORANDUM

TO: The Mayor, Members of City Council and City Manager
FROM: Karl Daughtrey, Director of Finance
RE: Financial Results, FYE June 30, 2015
Date: December 4, 2015

It is my pleasure, on the behalf of the City's Finance Department staff, to present the Comprehensive Annual Financial Report (CAFR) for the City of Hampton for the fiscal year ended June 30, 2015.

The CAFR is organized in five (5) major sections: 1) Introduction (pages 1 to 16); 2) Financial section including the Independent Auditor's Report (pages 17 to 123); 3) Combining and Individual Statements (pages 124-146); 4) Supplementary Information (pages 147 to 166); 5) Statistical Tables with historical financial data and demographic information about the City (pages 167 to 186); and 6) Independent Auditor's Compliance and Internal Control Reports and Schedule of Findings and Questioned Costs (pages 187 to 196).

Key Sections to Review:

Pages 12 to 13 contain the actual results for compliance with the City's five (5) financial policies. We are in compliance with all financial policies.

The Independent Auditors' Opinion is on pages 17 and 19 of the report. The Auditors have issued an unmodified opinion, or "clean" opinion on the City's CAFR.

Pages 20 to 26 contain the **Management's Discussion and Analysis (MD&A)**, a narrative introduction and analytical overview of the City's financial activities, similar to the analysis provided by publicly traded companies in their annual reports.

Component units are entities that are legally separate from the City, but for which the City is financially accountable, and whose relationship with the City is such exclusion would cause the City's financial statements to be misleading or incomplete. We report the following component units in the CAFR: Hampton School Board, Coliseum Central Business Improvement District, Inc., the Downtown Hampton Development Partnership, Inc. and the Economic Development Authority. Their financial statements are on pages 42 to 43.

Pages 124 to 133 contain the Balance Sheet, Statement of Revenues, Expenditures and Changes in Fund Balance-Budget and Actual, Schedule of Revenues and Other Credits-Budget and Actual, and Schedule of Appropriations and Expenditures for the General Fund.

The School Board financial statements are on pages 144 to 146.

The Schedule of Treasurer's Accountability, Schedule 1, on page 147, **reflects that cash and investments are in balance with the Treasurer's Office as of June 30, 2015.**

Pages 191 to 196 contain a Schedule of Findings and Questioned Costs. **There are five findings for fiscal year 2015.**

Finding #1: The auditors discovered a transaction that we had not properly recorded in the governmental activities in the Government-Wide Statement of Net of Position and Statement of Activities. During fiscal year 2015, we refunded a previous bond issue and the premiums associated with these bonds were written off to amortization expense in error. In the future, Finance staff will review the current accounting standards for non-routine accounting transactions to make sure that these transactions are properly accounted for in the financial statements.

Finding #2: The City is required to perform certain monitoring activities for subrecipients that receive Community Development Block Grant (CDBG) funds. During the testing of the CDBG program, the auditors noted that four of the expense reimbursements from a subrecipient did not have documentation of approval. In addition, the auditors noted that the City had not conducted any other subrecipient monitoring in fiscal year 2015 except for reviewing the information received for the reimbursement requests. The City staff plan to improve the system for subrecipient monitoring during fiscal year 2016.

Finding #3: During the testing of the Community Development Block Grant (CDBG) program, the auditors noted that the City did not have any certifications or personnel activity reports for CDBG employees.

When an employee is expected to work solely on a single Federal program like CDBG, their salary and wages should be supported by at least semi-annual certifications signed by the employee or employee's supervisor. When an employee works on multiple activities which includes federal programs, their salary and wages should be supported by personnel activity reports (i.e. time sheets) or similar documentation.

We will implement a certified monthly activity report for all CDBG funded personnel.

Finding #4: When an employee leaves the Department of Social Services their access privileges must be removed from all state systems within three working days of employment termination. Out of a sample of 3 employees tested by the auditors, there was 1 instance of noncompliance where access was removed after 4 business days. Social Services staff stated that this occurrence was due to extenuating circumstances. They had to ensure all of the emails for this employee were properly saved so that no information would be lost.

Finding #5: Social Services is required by the State to have a Local Security Officer (LSO) review all employees' access to each software application with the employees' supervisors on an annual basis to ensure that the access is properly aligned with job responsibilities. During the audit, the auditors noted that that this requirement was not part of the department's policies and procedures. Social Services staff have updated their policies and procedures to incorporate this requirement.

Key Financial Results:

General Fund

The City's General Fund finished the fiscal year with revenues exceeding expenditures (an increase in overall fund balance) by \$1.5 million. This increase in overall fund balance resulted primarily from actual expenditures being less than the budgeted amount.

Actual revenues were less than estimated revenues (excluding Appropriations from Fund Balance and Schools) by \$1.5 million, or approximately 0.45%. Actual expenditures were under appropriations (including Transfers and excluding Budget Savings) by \$15.8 million, or 4.8%.

During fiscal year 2015, the City's unassigned fund balance (formerly referred to as undesignated fund balance) increased by \$523,257 to \$52.1 million. The unassigned fund balance represents 11.8% of actual revenues for the General and School Operating Funds which exceeds the 10% policy threshold by 1.8%. For the committed fund balance – budget savings program, we added approximately \$2.3 million from savings generated by departments during fiscal year 2015.

Revenues (in millions):

| | <u>FY15 Budget</u> | <u>FY15 Actual</u> | <u>FY15 Actual As a % of Budget</u> | <u>FY14 Actual As a % of Budget</u> |
|------------------------|------------------------|------------------------|---|---|
| General Property Taxes | \$ 155.3 | \$ 155.5 | 100.0% | 99.1% |
| Sales & Use Taxes | 14.5 | 15.1 | 104.1% | 101.4% |
| Meal Tax | 18.9 | 19.5 | 103.2% | 105.6% |
| Business License Tax | 12.4 | 11.4 | 91.9% | 97.6% |
| State/Federal Revenues | 63.3 | 61.9 | 97.8% | 97.8% |
| Other Revenues | <u>54.3</u> | <u>53.8</u> | 99.1% | 100.9% |
| Total: | <u>\$ 318.7</u> | <u>\$ 317.2</u> | 99.5% | 99.6% |

(1) Excludes appropriations from fund balance

General Property Taxes, Meal Tax and Sales and Use Taxes tracked favorably, slightly above budget. The unfavorable variances in revenues are primarily attributable to State and Federal Revenues, Business License Tax and Other Revenues.

Some of the more significant favorable (actual exceeds budget) and unfavorable (actual is less than budget) variances in revenues for fiscal year 2015 are as follows:

| | VARIANCE FAVORABLE (UNFAVORABLE) |
|--|--|
| MEAL TAXES: This revenue was 3% over the budget primarily from an improving economy. | \$0.6M |
| SALES TAXES: This revenue was 4% over the budget primarily from an improving economy. | \$0.6M |
| PUBLIC ASSISTANCE STATE/FEDERAL REVENUES: Revenues are a function of the level of expenditures and the federal reimbursement rate for various programs. Expenditures were less than budget; however, the reimbursement rate was greater than what was budgeted. | (\$0.5M) |
| LOCAL AID TO THE COMMONWEALTH: Mid-year adjustment approved by the General Assembly. | (\$0.7M) |
| BUSINESS LICENSE TAX: Revenues were under the budget estimate due to some significant refunds that were made in 2015. | (\$1M) |
| SPECIAL ASSESSMENTS FOR THE COMMUNITY DEVELOPMENT AUTHORITIES: Collections were less than the revenue estimate. | (\$0.7M) |

Expenditures (in millions):

| | FY15 <u>Appropriations</u> | FY15 <u>Actual Expenditures</u> | Favorable <u>Variance</u> |
|---------------------------|-------------------------------|------------------------------------|------------------------------|
| City Departments* | \$ 195.5 | \$ 187.5 | \$ (8.0) |
| Transfer to Schools | 71.1 | 71.1 | - |
| Transfer to Other Funds** | <u>64.9</u> | <u>57.1</u> | <u>(7.8)</u> |
| Total: | <u>\$ 331.5</u> | <u>\$ 315.7</u> | <u>\$ (15.8)</u> |

*Excludes budget savings

**Transfer to Other Funds includes the following transfers: transfer to the Debt Service Fund, transfer to fund Capital Projects, contributions to match City Grants, annual transfer to the Hamptons Golf Course and the transfer of 2+2 lodging and meal taxes to pay Convention Center debt.

An analysis of the significant favorable variances in appropriations reveals the following:

| | VARIANCE FAVORABLE (UNFAVORABLE) |
|--|--|
| HUMAN SERVICE APPROPRIATIONS THAT RELATE TO PUBLIC ASSISTANCE STATE/FEDERAL REVENUES | \$1.3M |
| TRANSFERS TO OTHER FUNDS: Projects in the Capital Projects Fund were at various stages of completion; most of this funding was re-appropriated in FY16 to complete the various projects (\$6.85M). Debt Service savings (\$738K). | \$7.6M |
| POSITION AND BENEFIT SAVINGS PRIMARILY FROM VACANT POSITIONS | \$3.1M |
| SPECIAL ASSESSMENTS FOR THE COMMUNITY DEVELOPMENT AUTHORITIES: Collections were less than the revenue estimate | \$0.7K |

Hampton Roads Convention Center (HRCC)

The Convention Center's financial statements are presented on pages **34-39**. The Convention Center Fund is accounted for as an Enterprise Fund which functions similar to private for profit business units. The Convention Center Fund generated a change in net position of \$277,559 (previously referred to as "net income"). HRCC's attendance was higher in FY15 than FY14 however; event days were 66 lower than budgeted due to the improvement in the quality of the events HRCC has been able to book thus phasing out the numerous small events which generated very little in revenue. On the expenditure side, a \$100,000 utilities savings was obtained due to increased efficiencies related to a new HVAC provider and a \$5,000 refund was received from an energy savings program. Some of the FY15 events generating event-related income over \$50,000 included: Bodacious Bazaar & Art Festival, SGK Gun Shows, Annual VA RV Show and the VA Section American Water Works Association and VA Water Environment Association's 2014 Water Jam.

Woodlands Golf Course

The Woodlands Golf Course's financial statements are presented on pages **136-138**. The Woodlands Golf Course is accounted for as an Enterprise Fund which functions similar to private for profit business units. The Woodlands Golf Course incurred a net operating loss of \$141,797 before depreciation expense. The weather conditions were one of the factors that contributed to the loss. The golf course experienced 35 days of closure due to bad weather and 29 days of very little play due to adverse weather conditions. Also, 17 tournaments were transferred to the Hampton's Golf Course to encourage more tournament play at this course which resulted in a loss of tournament revenue for the Woodlands. Although operating expenses have increased over the years, Green Fees have remained the same since fiscal year 2006.

Steam Plant

The Steam Plant's financial statements are presented on pages **136-138**. The Steam Plant is an Enterprise fund with revenues are derived from solid waste disposal fee (tipping fee) charged to the Solid Waste Fund, the sale of steam to the US Government and user fees charged to other external customers. The Steam Plant sustained a \$553,000 operating loss in fiscal year 2015. The loss is due to the protracted shutdowns as a result of the overhaul of #1 Boiler. Repair work to the boiler resulted in a two month cease for commercial traffic for #1 Boiler. The resulting loss of revenue while on single boiler operations, Boiler #2, for nearly half a year was anticipated by the Joint Board of Oversight and was on track with expectations.

Solid Waste

The Solid Waste's financial statements are presented on pages **136-138**. The Solid Waste Fund is accounted for as an Enterprise Fund which functions similar to private for profit business units. The Solid Waste Fund incurred a net loss of \$1,352,089. The decrease in revenue of approximately \$1 million from fiscal year 2014 is due to the inclement weather in the month of February, revenue reductions related to the Hampton tax relief program and vacancies in residential properties throughout the year which impacts the total number of customers and revenue. For FY16, Council approved a rate increase for residential solid waste user fees, which will help offset the loss of revenues.

New Accounting Standards for Pensions

For fiscal year 2015 the Governmental Accounting Standards Board (GASB), the standard-setting body for governmental accounting principles, requires state and local governments to implement GASB Statement No. 68, "Accounting and Financial Reporting for Pensions - an amendment of GASB Statement No. 27" and GASB Statement No. 71, "Pension Transition for Contributions Made Subsequent to the Measurement Date." These new statements require the City and School Board to record a net pension liability for HERS and VRS in the Government-Wide Statement of Net Position (often referred to as "Balance Sheet"), report additional information in the notes and provide additional supplementary information. These new accounting standards will have no impact on the pension funding requirements by HERS and VRS and will not have any impact on the General or School Operating Funds.

Closing Comments

I would like to thank the Finance Department staff for their dedication and untiring efforts in maintaining accurate financial records, the long hours they worked to close the City's funds, assisting the external auditors, and preparing the CAFR. I feel honored to have each of them on my team.

If you have any questions concerning the report, please contact me.