



MEMORANDUM

TO: The Mayor, Members of City Council and City Manager
FROM: Karl Daughtrey, Director of Finance
RE: Financial Results, FYE June 30, 2017
Date: December 8, 2017

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, 2017.

The CAFR is organized in six (6) major sections: 1) Introduction (pages 1 to 15); 2) Financial section including the Independent Auditor's Report (pages 16 to 110); 3) Required Supplemental Information (pages 111 to 119); 4) Combining and Individual Financial Statements (pages 120 to 142); 4) Supplementary Information (pages 143 to 162); 5) Statistical Tables with historical financial data and demographic information about the City (pages 163 to 182); and 6) Independent Auditor's Compliance and Internal Control Reports and Schedule of Findings and Questioned Costs (pages 183 to 191).

Key Sections to Review:

Page 12 contains 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 16 to 18 of the report. The Auditors have issued an unmodified opinion, or "clean" opinion on the City's CAFR.

Pages 19 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 that 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 120 to 129 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 140 to 142.

The Schedule of Treasurer's Accountability, Schedule 1, on page 143, **reflects that cash and investments are in balance with the Treasurer's Office as of June 30, 2017.**

Pages 187 to 191 contain a Schedule of Findings and Questioned Costs. **There are four findings for fiscal year 2017.**

Finding 2017-001: During fiscal year 2017, we decided to perform a more extensive analysis of the real estate properties owned by the Economic Development Authority (EDA). Staff was tasked with comparing all of the EDA properties per the City's books to all of the EDA's properties per the City Assessor's records as of June 30, 2017. As a result of this analysis, we discovered two parcels (one from 2005 and one from 2007) that were not recorded on the EDA's and the City's books. These two property transactions were for transfers from the City to the EDA - approximately \$5.6 million in value. Because of the dollar value of these two transactions, we had to report them as prior period adjustments (corrections of errors that occurred in a past fiscal year) in this year's CAFR. We had to adjust the beginning net position (net worth) for the EDA and Government Activities and disclose the details of the adjustments in footnote 16 in the CAFR. The Auditor reported the prior period adjustments as a "material weakness in internal control over financial reporting –correction of errors". In the future, we will continue to reconcile all of the EDA's properties per the books to all of the EDA's properties per the Assessor's records.

Finding 2017-002: During the testing of the Community Development Block Grant (CDBG) program, the Auditor noted that the City did not have an executed fiscal 2017 sub-receipt agreement in place with the Hampton Redevelopment and Housing Authority (HRHA) for the CDBG and Home programs. The agreement was delayed due to some technical assistance that we requested from HUD in reference to the release of funds. The agreement has been sent to HRHA for their execution.

Finding 2017-003: The Virginia Security for Public Deposits Act requires banks to report public deposits (bank accounts that belong to public entities like the City) to the State's Treasury Department on a quarterly basis. The state uses this information to determine the bank's collateralization requirements for public deposits. Our bank, Old Point National Bank, inadvertently did not report the Hampton Coliseum Cash Order checking account as a public deposit to the state for the second and third quarters of 2017. The bank's staff contacted the Treasury Department to determine if there was a process to correct the reporting for these quarters and was informed that there was no process in place for correcting past quarters. In the future, the bank's staff will review the file for accuracy and will send the Treasurer a report that we will review.

Finding 2017-004: In accordance with Section 2.2-4407 of the Code of Virginia when a user leaves the Local Department of Social Services (LDSS), their access privileges must be removed from all systems they were authorized to use within three business days. The City had one terminated employee whose system access privileges were not removed within three business days. The Department of Social Services will be implementing procedures to monitor the removal of system access for terminated employees.

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 approximately \$70,000.

Actual revenues were slightly more than estimated revenues (excluding Appropriations from Fund Balance and Schools) by \$223,000, or approximately .06%. Actual expenditures were under appropriations (including Transfers and excluding Budget Savings) by \$12.5 million, or 3.7%.

During fiscal year 2017, the City's unassigned fund balance (formerly referred to as undesignated fund balance) increased by \$29,735 to \$54,330,481. The unassigned fund balance represents 11.9% of actual revenues for the General and School Operating Funds which exceeds the 10% policy threshold by 1.9%. For the committed fund balance – budget savings program, we added approximately \$1.6 million from savings generated by departments during fiscal year 2017.

Revenues (in millions):

	FY17 Budget	FY17 Actual	FY17 Actual As a % of Budget	FY16 Actual As a % of Budget
General Property Taxes	\$ 159.5	\$ 160.8	100.8%	100.8%
Meal Tax	20.1	20.4	101.5%	103.6%
Sales & Use Taxes	15.6	15.0	96.2%	102.0%
Business License Tax	12.4	12.3	99.2%	97.5%
Communication Sales Tax	8.9	8.6	96.6%	96.7%
Lodging	3.6	3.7	102.8%	102.9%
Special Assessments	5.7	4.8	84.2%	136.2%
State/Federal Revenues	65.0	65.0	100.0%	99.4%
Other Revenues	<u>37.4</u>	<u>37.8</u>	101.1%	100.8%
Total:	<u>\$ 328.2</u>	<u>\$ 328.4</u>	100.1%	101.1%

(1) Excludes appropriations from fund balance

General Property Taxes, Meal Tax, Lodging, and Other Revenues tracked favorably, above budget. The unfavorable variances in revenues are primarily attributable to Sales and Use Tax, Business License Tax, Communication Sales Tax and Special Assessments.

Some of the more significant favorable (actual exceeds budget) and unfavorable (actual is less than budget) variances in revenues for fiscal year 2017 are as follows:

	VARIANCE FAVORABLE (UNFAVORABLE)
GENERAL PROPERTY TAXES: Real estate property tax collections exceeded the budget because of supplemental assessments from new construction and abatements were less than anticipated. On the other hand, personal property tax revenues were less than estimated revenues.	\$1.3M
MEAL TAXES: We continue to experience inflationary growth in this tax.	\$0.3M
INTEREST FROM INVESTMENTS: The Federal Reserve increased their interest rates three times during fiscal year 2017. This has positively impacted some of the investment interest rates.	\$0.4M
SALES AND USE TAX: The impact of e-commerce on retail stores	(\$0.6M)
SPECIAL ASSESSMENT FOR THE COMMUNITY DEVELOPMENT AUTHORITIES: Collections were less than revenue estimates for Peninsula Towne Center CDA.	(\$0.9M)

Expenditures (in millions):

	<u>FY17 Appropriations</u>	<u>FY17 Actual Expenditures</u>	<u>Favorable Variance</u>
City Departments*	\$ 204.1	\$ 195.8	\$ (8.3)
Transfer to Schools	71.5	71.5	-
Transfer to Other Funds**	<u>65.3</u>	<u>61.1</u>	<u>(4.2)</u>
Total:	<u>\$ 340.9</u>	<u>\$ 328.4</u>	<u>\$ (12.5)</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, 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)
TRANSFERS TO OTHER FUNDS: Projects in the Capital Projects Fund were at various stages of completion; most of this funding was re-appropriated in FY18 to complete these projects (\$3.0M). Debt Service savings (\$915K), CSA Match (\$194K), EDA Fund (\$106K), and Bass Pro (\$89K) reductions	\$4.2M
POSITION AND BENEFIT SAVINGS PRIMARILY FROM VACANT POSITIONS	\$3.7M
PAYMENTS TO THE CDA'S: The City bills and collects the special assessment on behalf of the CDA's and all collections are paid to the CDA's	\$0.9M
HUMAN SERVICES APPROPRIATIONS	\$0.9M
CONTINGENCY	\$0.4M

Hampton Roads Coliseum/Hampton Arts Commission

The Hampton Coliseum/Hampton Arts Commission's financial statements are presented on pages 132-134. The Hampton Coliseum/Hampton Arts Commission Fund is accounted for as an Enterprise Fund which functions similar to private for profit business. The Hampton Coliseum/Hampton Arts Commission Fund generated a net loss of \$669,783 in fiscal year 2017. Total operating revenues declined by \$616,033 from fiscal year 2016 primarily due to a drop in ticket sales. The following major shows were not held during fiscal year 2017: Carrie Underwood, Pearl Jam and Amy Schumer. While on the other hand, expenses increased by \$234,409 from fiscal year 2016. Most of the increase in expenses is related to pension expense.

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 \$534,239 (previously referred to as "net income"). The 2+2 meal and lodging taxes exceeded the revenue budget by \$123,177. Exhibit Hall Rental and Facility Fees both increased over fiscal year 2016 by \$106,000 and \$11,000, respectively. Some of the fiscal year 2017 events generating event-related income over \$75,000 included: Discover the Dinosaurs, Fall Bodacious Bazaar & Art Festival, SGK Gun Shows, 2016 NekoCon, Hampton Roads Tattoo and Art Convention and the 2017 Mid-Atlantic Quilt Festival.

The Hamptons and Woodlands Golf Courses

The Hamptons and Woodlands Golf Courses financial statements are presented on pages 34-39 and 132-134, respectively. Both golf courses are accounted for as an Enterprise fund which functions similar to a for profit business. The Hamptons and Woodlands incurred a net loss of \$407,601 and \$312,662, respectively, during fiscal year 2017. The total rounds of golf decreased by 17% for The Hamptons and 24% for the Woodlands during fiscal year 2017. Several factors are impacting the decline in rounds: reduction in number of tournaments; competing golf courses are discounting prices to attract players; and interest in golf from younger players has waned considerably.

Steam Plant

The Steam Plant's financial statements are presented on pages 132-134. The Steam Plant is an Enterprise fund with revenues that are derived from solid waste disposal fee (tipping fee) charged to the Solid Waste Fund, the sale of steam to the U.S. Government and user fees charged to other external customers. The Steam Plant generated net income of \$400,666 in fiscal year 2017.

Solid Waste

The Solid Waste's financial statements are presented on pages 132-134. The Solid Waste Fund is accounted for as an Enterprise Fund which functions similar to private for profit business. The Solid Waste Fund generated net income of \$1.3 million in fiscal year 2017.

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.