CITY OF HALLANDALE BEACH, FLORIDA
MEMORANDUM

CM18-133

DATE: January 23, 2018

TO: Honorable Mayor and City Commissioners/HBCRA Directors

FROM: Roger M. Carlton, City Manager/Executive Director of HBCRA

SUBJECT: Transmittal of Foodman Associates Forensic Audit of Certain Matters Related to the HBCRA and FY 2015/16 Marcum Comprehensive Annual Financial Report (CAFR).

Background:

Florida Statutes requires municipalities to complete a Comprehensive Annual Financial Report (CAFR) by June 30th of each year for the previous fiscal year. The FY 15/16 CAFR for the City of Hallandale Beach and the HBCRA should have been completed and submitted to the State of Florida and other entities by June 30, 2017.

The City and the HBCRA did not meet the requirement for complex reasons as follows:

1. The audit and actuarial report for the Police and Fire Pension was late by at least two months. The audit is prepared by one firm and the actuarial report stating what contribution the City must make and other required disclosures is prepared by a different firm. These documents are a requirement for inclusion in the City's CAFR prepared by Marcum. The control of the process is solely the responsibility of the Police and Fire Pension Board (two members are City Commissioners, two members are appointed by the Police and Fire Unions and the four appoint the fifth). Many requests by staff to complete the audit and actuarial report dating back to November 2015 were not successful.

2. The HBCRA Board (same members as the City Commission) determined to request an independent forensic review of certain items related to the HBCRA beginning in FY 11/12 and including all subsequent fiscal years to FY 15/16. Mr. Foodman was contracted to complete an independent review and, based on his initial report, the HBCRA Board determined to direct a second more detailed review which was completed on November 10, 2017. This time frame added significantly to the time necessary to complete the Marcum CAFR as explained in #3 below.

3. Marcum would not complete the FY 15/16 CAFR until the firm's quality assurance and legal staff could review the Foodman forensic audit results. This process took some time and resulted in an additional finding to the FY 15/16 compliance report regarding the delay in issuance of the CAFR due to the forensic audit. The forensic

audit did not change the overall outcome of the CAFR. The final CAFR was delivered on December 6, 2017 and forwarded to the State and other regulatory agencies.

4. The outcome of the late submission to the State and various agencies is still unfolding. With the help of our new state lobbyist Stephanie Grutman, Ballard Partners, the Joint Legislative Audit Committee granted the City/HBCRA an extension until January 15, 2018 to submit the CAFR. We were able to beat that deadline by nearly one month. The CAFR and Annual Financial Report (AFR) were submitted to the Florida Auditor General fulfilling our financial reporting requirements. The FDOT's response was that the CAFR has been received and that they are reviewing the corrective action plan that was submitted by Finance Department staff to resolve previous findings. This is a hopeful sign and kudos to the good work of our first Grant Coordinator Noemy Sandoval and her newly established Grants Development Program for demonstrating that the City means business in resolving issues with our grants management.

5. In the past, to the best of my knowledge, the level of detail and analysis of the information included in the CAFR collectively spent by the City Commission and the HBCRA Board was less than needed to provide firm policy direction to rectify many issues which the Foodman forensic audit and the FY 15/16 CAFR present. This is understandable to a degree since the FY 15/16 CAFR includes nearly 200 pages of very droll and complex information as required by GASB, Florida Statute and a number of entities which provide grants and loans to the City and the HBCRA. To make this situation even more daunting the Foodman forensic audit includes more than 250 pages and 29 exhibits. My goal, which took the better part of the holiday season and January, was to prepare a road map for review of both documents by both the City Commission/HBCRA Board and our citizens.

6. It has been said that this City Manager does not "own" either the content of the Foodman forensic audit or the findings of the FY 15/16 CAFR. While this may be true from a timing standpoint since I did not join the City until more than four months of FY 16/17 were complete, this City Manager does "own" the solutions that are required to implement the corrections recommended in the CAFR and to resolve the findings of the Foodman audit. This cannot be done without an understanding of the issues and collegial discussions by the City Commission and HBCRA Board of the many policy decisions that are necessary to resolve historic questionable use of HBCRA funds to fill deficits in the City budgets. To support this correction, the Finance Department is undergoing a complete reorganization which has been discussed by the City Commission including adopting a transitional program with substantial allocated resources to resolve the longstanding problems. I want to take this opportunity to thank Celeste Lucia, Barbara Trinka, and the Finance Department Staff for helping to resolve this situation.

The balance of the memorandum will be an explanation of the major points of both the Foodman forensic audit and the FY 15/16 CAFR. This will be a road map that will allow the reader in approximately 90 minutes to understand both documents. This reflects the transparency of financial operations the City Commission and HBCRA Board have directed the administration to provide. The greatest challenge will be to reach closure (policy direction) on the findings of the forensic audit. The financial impact on the City and the HBCRA will be explained and a path to put the distrust and allegations behind us will be provided. It is suggested to hold off on this discussion until after the March election to allow a full City Commission and HBCRA Board to set the direction for long term financial stability for both entities. We have come a long way towards this goal by greatly improving accountability and auditability for the Interlocal Agreements (ILA's) and Memoranda of Understanding (MOU's) both retroactively for FY 16/17 and prospectively for FY 17/18. So, with this long background and setting of the stage let us move forward first on understanding the Foodman forensic audit.

The Foodman Forensic Audit:

A forensic audit is needed when there is suspicion that monies have been stolen misappropriated (waste and abuse) or illegally spent. When these allegations are made, the only way to restore public trust is to have an independent audit process that digs deeper into a situation than the annual CAFR is required by GAAP accounting practices to provide.

The CAFR, which will be explained later in this memorandum, is a look at the entire financial management and reporting practices of the City and HBCRA for a specific period of time using GAAP and accounting information provided by the City and HBCRA's administrations. There were substantial concerns on the part of several City Commissioners/HBCRA Board members, expressed during early 2017 that certain very substantial high dollar value journal entries, accounting for transfer of real estate properties from the City to HBCRA, payment by the HBCRA of a City bond issue, the record keeping for ILA's and MOU's and whether or not a large cash transfer was made in FY 11/12 when the HBCRA finances were separated from the City or at least purported to be separated were collectively not fully disclosed. All of these concerns led to a question regarding whether or not the work of Marcum was compliant with best practices in reviewing and making recommendations on the above concerns. As a result of this, Foodman Associates was retained on June 12, 2017 to analyze these concerns and do an in-depth forensic audit of the HBCRA over a five fiscal year period.

The results of the process are summarized below and the page numbers of the related exhibits are provided to the reader for a quick roadmap to the pertinent points in the forensic audit document.

1) Pages 1-27 includes a summary of the results of the forensic audit.

2) Page 1 and 2 list 13 issues that the forensic audit analyzed.

3) Pages 3 lists the 29 exhibits to the forensic audit. In addition, Mr. Foodman interviewed many City employees both past and present including the members of the City Commission/HBCRA Board who were available. Documents provided by Mayor Cooper were also reviewed as were minutes and videos of meetings.

4) Page 4-8 reviews the indirect cost methodology for calculating the amount charged by the City to the HBCRA for services such as financial management, space rental and other administrative services that were approved by both the City Commission

and the HBCRA Board. The outcome of this analysis is that a “true-up” should be made in the amount of $490,376. The methodology to calculate this amount using the McCue/Topinka study rather than the Maximus study is fully explained. The most salient point appears in the chart on page 8 wherein a payment was made to the City by the HBCRA which exceeded the McCue/Topinka calculation by $700,279 in one fiscal year. In subsequent years the HBCRA actually underpaid resulting in a net of $490,376 for the “true-up” due the HBCRA by the City.

5) Pages 8-12 analyze 39 MOU’s (Exhibit 9 to the Foodman forensic audit). The MOU’s are different than the ILA’s since the MOU’s relate to direct services such as extra police protection, code enforcement and other services of direct benefit within the boundaries of the HBCRA. It should be noted that the direct benefit test is relatively easy to meet from a geographic sense since the boundaries of the HBCRA encompass approximately 76 percent of the entire City.

   It is most important to note that the geographic test is not the only test to meet. The direct services must be measurable and quantifiable and must be adopted in a CRA vision plan as required by Florida Statutes Chapter 163. One note before this audit finding is explained is very important. All but four of the MOU’s reviewed by Mr. Foodman were signed as legally sufficient by the HBCRA Attorney and City Attorneys at the time. This was done before our current City Attorney joined the City. It is assumed that the City Administration and City Commission /HBCRA Board relied on these reviews.

   An even more important test then the previous two is whether or not the MOU’s meet the requirements of Florida Statutes Chapter 163 which govern CRA’s. The requirements are documented on page 10 and the Foodman conclusion is that $7,275,959 of the MOU’s total expense over four fiscal years does not meet the requirements of Chapter 163 and therefore should be reimbursed by the City to the HBCRA. This finding is documented on Page 12. It is important to note that solutions to this finding will be suggested later in this memorandum.

6) Page 12-14 discusses a complex journal entry made at the recommendation of Marcum to correct an error wherein many parcels acquired with HBCRA funds were actually titled to the City. FS Chapter 163 allows CRA’s to acquire “assets held for resale” but does not require those assets to be sold in any specific period of time. As an example, the land owned by the HBCRA that will eventually be turned over to the City Center project is an “asset held for resale” (“sale” does not preclude donation). When the project meets all the requirements for transfer per an approved development or redevelopment agreement, the land is transferred and the asset is removed from the HBCRA books. The impact of the incorrect titling is that the balance sheet of the City is inflated and the balance sheet of the HBCRA is deflated. This matter is closed out on page 13 of the forensic audit with the statement “we do not consider the Title of “Assets Held for Resale to be a materially misleading classification.” This statement clears up a perception that Marcum was incorrect in how the transfer from the City to the HBCRA was handled from an accounting standpoint.

7) Page 14-15 clarifies a $5 million transfer from the HBCRA to the City in FY 14/15. Until the Foodman forensic audit was completed this transfer was difficult to explain. The actual amount of the transfer was $4,900,623. This amount was a compilation of what are known as “due to/due froms” (DT/DF’s) which are methods for settling accounts between related entities such as the City and HBCRA when payments are made in a lump sum from “pooled cash” rather than in smaller amounts one at a time. The book-keeping for these amounts was less than up to par, however, the forensic audit was able to reconcile (validate) the $4,900,623 amount. (See Exhibit 14). The forensic audit does recommend improved procedures to allow better audit trails. These procedures are being put in place.

8) Page 15-16 details an alleged $2.5 million “incentive payment” that was made by the City to the HBCRA to get it started when the finances were separated in FY 11/12. The actual amount was $150,000 and the details of how the forensic audit validated the amount can be found in Exhibit 16-19. Your attention is drawn to Exhibit 17 in which former HBCRA Director Dr. Jackson made certain incorrect representations to the Broward OIG and to Exhibit 16 pages 5-6 in which questions by HBCRA Board member Michele Lazarow were asked and left unanswered. Marcum to the best of our knowledge, was not in the audience or asked to explain the situation. It should also be noted that City staff at that time calculated a “true up” of $12,282,954 that was due to the HBCRA for the City and that amount was eventually paid.

9) Page 17-19 presents another complex subject regarding whether or not the HBCRA should pay the interest and principal on the Series 2007A 20 year bonds in the amount of $24,615,000. It should be clear that these bonds are City bonds and not HBCRA bonds. The revenue pledge is non-ad valorem (non-property tax revenues of the City’s General Fund). These funds for repayment may not be committed to essential services like police and fire rescue. While it may have been acceptable to do this when City reserve funds were at high levels in 2007, the long term strategy was fiscally irresponsible. When the Great Recession set in, the property tax roll decreased and reserves began to be depleted at the same time as the debt service was being absorbed by the HBCRA. There will be more about this revenue pledge and other similar commitments against the General Fund in the Marcum CAFR portion of this memorandum. The key point to be considered is whether or not the use of HBCRA funds in the average amount of 76 percent of the total debt service over the life of the 2007A Bonds represent prudent fiscal policy or is this decision even allowed under Chapter 163. The Foodman forensic audit concludes that the HBCRA payments to fund the City’s debt, which was used for various park related capital expenses, was not appropriate and the “true-up” should be $3,331,774 to be paid to the HBCRA by the City. Your attention is drawn to Exhibit 21-25 which, when taken collectively, show that bond documents, minutes of meetings, video of meetings, transcripts of the meetings all result in what can best be described as a confused policy discussion regarding whether or not the HBCRA should pay all or a portion of the debt service for the Series 2007A bonds.

10) Pages 19-24 make a series of recommendations to improve record keeping, grants management, accuracy of minutes and other housekeeping items. Staff concurs

with these recommendations with some minor exceptions and is in the process of implementing the recommendations on a priority basis.

11) A major question included in the Foodman scope of work was to give an opinion on whether the Marcum work product met the Standard of Field Work that is customary for the audit process. The standard may be found in Exhibit 28. Mr. Foodman leaves this question unanswered because Marcum would not give up its work papers for him to review. Foodman leaves to the discretion of the Administration and Board members of the City/HBCRA and both legal counsels to answer the quality of work question. As City Manager and HBCRA Director my recommendation is that this matter should be concluded without further analysis. There has been considerable turnover in City/HBCRA staff and members of the City Commission and HBCRA Board. The records audited are not without weakness and most importantly, the potential for recovery of fees paid to Marcum is limited and the cost to litigate would have a very low potential of recovery. Should any person involved in decision making regarding the forensic audit wish to proffer a different view, that position should be discussed when the City Commission/HBCRA vacancy is filled and the full bodies can determine how the forensic audit and CAFR are accepted and what actions, if any, should be taken.

12) Page 26 of the transmittal letter provides a summary of the findings in Nos. 4, 5 and 9 above that represent a total "true-up" due the HBCRA by the City in the amount of $11,098,110 for four fiscal years from FY 11/12 to FY 14/15. FY 15/16 is not included because the MOU's were not paid. FY 16/17 and 17/18 were developed by the current City Manager and Assistant City Manager and reviewed by both the current City Attorney and HBCRA Attorney and are both auditable. It should also be clear that the $2.5 million "incentive payment" difference of $2.35 million more than was actually paid is not included in this number (See #8 above).

As your City Manager and HBCRA Director my goal in providing this summary is to facilitate your understanding of a very lengthy and complex document in a roadmap that could be quickly read and understood. This distillation of the forensic audit should not ignore the fact that staff spent more than 1000 hours researching and responding to requests by Mr. Foodman and that the HBCRA invested $125,000 in the forensic study. Was it worth the investment? The reader of this memorandum will have to draw their own conclusion. While doing that, it is important to consider that the "true-up" recommended represents 28.3 percent of the funds generated during the forensic review period and that many questions raised have been answered and should be put behind us as we move forward to develop the vision for the remaining life of the HBCRA.

The big question is what to do with the recommended "true-up" in the amount of $11,098,110. If that amount is to be paid in one year by the City to the HBCRA, the impact on the City budget will be devastating not to mention the potential for claims made by the other governments that contribute to TIF revenues. The level of General Fund reserves as well as many factors which will impact the FY 18/19 and beyond budgets such as collective bargaining negotiations, capital needs for beach nourishment, BSO mandated radio replacements, settlement of legal cases, implementation of the three forms of photo surveillance approved in the FY 17/18 budget and the desperate need to address our mobility issues will all be impacted. One possibility is that a "true-up" payment, if made at all, should be done over a long period and the annual amount included in the HBCRA vision plan being developed. While the City Attorney and HBCRA Attorney were both interviewed during the development of the forensic audit, their recommended solutions are important to the ultimate resolution of the Foodman audit findings. This is a key reason why the City Commission/HBCRA Board review of the document should await the seating of a fifth member after the March 2018 special election.

Before the process to resolve the "true-up" and other findings of the forensic audit is discussed by the full City Commission/HBCRA Board, it is important to gain an understanding of the Marcum CAFR and related documents for FY 15/16. The road map to understanding this document and related reports follows:

FY 15/16 Marcum Comprehensive Annual Financial Report (CAFR):

The CAFR is required by State law and its main purpose is to provide our citizens/taxpayers with reliable financial information about the City/HBCRA. Financial institutions that have or may loan money to the City/HBCRA are ensured that their collateral is secure. Previous year findings regarding financial control weakness as well as new findings are discussed. The balance sheet (assets vs. labilities) and operating statements of the City/HBCRA are also presented in great detail. It is most important for the reader of this memorandum to understand that this is a "clean audit" which means that there are no findings of any great concern that could lead the reader to not rely on the City's financial representations.

It should be clear from the Transmittal Letter (Page i – viiii) that the City prepares and is responsible for the financial statements. Marcum relies on information provided by the City/HBCRA and uses sampling and other techniques to verify the financial information provided. To audit every transaction would be extremely costly.

The next section of the FY 15/16 CAFR is the "Management's Discussion and Analysis" commonly referred to as "MD&A." This is an unaudited discussion by the City (Page 4-21). The financial highlights on Page 4-5 provide a brief summary of the detail. For example the total assets of the City/HBCRA exceed the total liabilities by approximately $107 million which is a $6.8 million decrease over the previous fiscal year. This number is comprised of a decrease of $2.7 million from governmental operations (predominantly the General Fund) and $4.1 million from business type activities which are predominantly the utility funds and operations like the storm water utility and the solid waste collection program. Many of these operations performed at deficit levels during FY 15/16 which was a major cause of the decrease in the balance sheet of assets (which includes reserves) over liabilities. This situation was discussed in great detail with the City Commission/HBCRA Board during many workshops held in the summer of 2017 that provided City Commission/HBCRA direction for the preparation of the FY 17/18 Budget. That direction was clear... develop a budget without deficit spending. The 17 Summer Studies that were reviewed during the workshops provided detail for the solutions for years of deficit spending. Fifteen of those studies were eventually incorporated in the FY 17/18 Budget. One of the most important comments in the CAFR relates to use of fund balance (reserves) in the General Fund. This is the second bullet on Page 5. This item projects a $6.0 million deficit in the General Fund for FY 16/17. While the unassigned fund balance was 22.9 percent of operating expenditures at the time of the audit, that amount has diminished to approximately 16 percent (the lowest amount allowed by City Commission policy) by the end of FY 16/17.

Page 6 provides an overview of the major elements of the CAFR. Page 7-11 provide a discussion of the change in Net Position of the City. Page 12-19 provides highlights of the FY 15/16 budget year. The bar chart at the top of Page 18 reflects the General Fund spending in excess of available revenues, however, by the end of the fiscal year, the actual amount of the deficit was less than the amended budget projections. Page 20 and 21 provide a look into the future of FY 16/17 which is the nest fiscal year to be audited. The second bullet on Page 21 reflects concerns of the Finance Department relative to four difficulties that were addressed in the FY 17/18 Budget.

Basic Financial Analysis:

Page 22 – 34 include the actual audited information that Marcum provides. The format and method for presentation are prescribed by GASB. The highlights of the section include:

1) The Statement of Net Position (Page 22) reflects a positive balance in the City/HBCRA combined balance sheet of $106,994,368.

2) The statement on Page 23 shows the net financial impact of various operations of the City/HBCRA and how those operations are funded.

3) The statement on Page 26 provides detail on the Governmental operations, including the General Fund and the statement on Page 30 provides detail on the Proprietary Fund operations.

4) The statements on Page 33 and 34 provide detail on the fiduciary funds which include the pension funds. It should be noted on Page 34 that the total additions to the pension funds were $29,788,239 while the expenses were $13,707,235. The increase is due in large part to investment earnings from the long term bull market and related increases in security valuations. It is important to note that Marcum relies on other auditor's pension audits for the Police and Fire Pension Trust and does not perform its own audit of that pension.

Notes to Financial Statements:

This section of the CAFR appears on Page 35-93. The notes and the detail provided are very helpful to understanding the complex statements in the previous section of the CAFR. Key highlights of the notes include:

1) The Golden Isles Safe Neighborhood District and the Three Islands Safe Neighborhood District (which are both entities which provide additional security levels at resident expense) are explained on Page 35. The HBCRA is also explained on Page 35. The audit of these entities which are called the "Blended Component Units" are included in the overall CAFR.

2) Page 37 and 38 list the 10 major funds that are enumerated in the audit.

3) The depreciation cycle for capital assets is listed on Page 40. The range is 5 years for vehicles and equipment to 42 years for certain very long term assets. Depreciation is viewed as an expense for the enterprise funds because capital assets are expensed over their useful lives instead of 100% in the year purchased. This may allow funds to be set aside each year for replacement as assets near the end of their useful life. This has not been the consistent financial reality of the City.

4) Note J on Page 40 is important as it explains the "Assets Held for Resale" which was a question further clarified in the Foodman forensic audit regarding the transfer of wrongly titled real estate assets to the HBCRA from the City.

5) The City's accounting policies related to pension plans are explained in Note Q on Page 42. The Self Insurance funds for liability and workers compensation are explained in Note S on Page 43.

6) The City's cash position (both restricted and unrestricted) is enumerated in Note 3 on Page 45. It should be understood that only a small portion of these funds are available for use for unforeseen emergencies or budget amendments if the drawdown over the entire fiscal year is considered and if the 16 percent minimum balance policy in the General Fund is to be respected. Page 46 explains the risk level for investing these funds as defined in the adopted investment policy. The invested funds comply with this policy. Interest rate risk is explained on Page 47 – 54. This analysis ensures that the Finance Department invests available and restricted funds to maximize returns with reasonable risk levels and to ensure that cash is available when needed to operate the government and meet all financial obligations such as bond debt service.

7) Receivables are documented in Note 4 on Page 55-56. There are no major past due receivables and write-offs of uncollectables are made by the City Commission/HBCRA Board as needed. There is a comment on Page 55 relative to the HBCRA Affordable Housing Loan Program which says that the debt for mortgage buy-downs is not reported. This will change as the program expands and more funds are generated from developers in-lieu contributions are made. The payment in lieu (PILOT) program study currently underway will soon be presented to the City Commission and HBCRA Board. A briefing regarding affordable/workforce housing was held for the joint meeting of the two boards on January 10, 2018.

8) Capital asset activity is explained in Note 6 on Page 56 – 57. This information is important to understand how the City is investing in the community by funding long term projects to keep infrastructure up to date and to provide needed projects for a growing population with changing demographics.

9) The City/HBCRA's long term debt obligations are explained in Note 9 on Page 59 – 62. The total governmental debt of the City/HBCRA as of September 30, 2016 was $103,826,351. Business-type (proprietary funds) debt totaled $6,795,000. Interest rates ranging from as low as 1.31 percent to as high as 5 percent with maturities ranging from short term to as long as 2046 for the voter approved Parks

General Obligation Bonds. Generally, up to 10 percent of taxable valuation for general obligation bonds and proprietary fund debt service annual payments of 1.15 times annual debt service requirements is considered prudent. The City/HBCRA are well within these levels with the exception of a technical default on certain Water/Sewer/Storm Drainage obligations. This situation is being remedied during FY 17/18 with an independent rate study and an increase in rates that was included in the FY 17/18 budget. This statement may need to be modified because the recently approved federal "tax reform" will increase our debt service costs. The amount of increase is being analyzed and a separate report will be issued.

An important note appears on Page 62 which is a chart showing the revenues pledged for the current outstanding debt. It highlights the revenue received during the fiscal year, the associated debt service payment for that same debt and the percentage of debt service to revenue. The HBCRA Redevelopment Revenue Note (for OB Johnson) revenue bond pledge by the City to cover this payment requires 14.81 percent of HBCRA revenues. The two Water/Sewer/Storm Drainage bonds require 64.28 and 35.27 of these pledged revenues which is too high and could have been avoided if rates were adjusted during prior fiscal years.

10) The City/HBCRA pension plans are explained in Note 10 on Page 63 – 77. The City's General Employee Retirement plan has a total of 335 members of which 123 are retires and receiving benefits, 72 are entitled but not yet receiving benefits and 140 are still working. The Police Officers and Firefighters Retirement plan has a total of 336 members of which 166 are receiving benefits, 10 are entitled but not yet receiving benefits and 160 are active. It is important to understand that the ratio of young workers to retired or qualified for benefits workers is very low. That is a major reason why the City's pension costs are high. Other jurisdictions have younger workers contributing into the plan than older workers who are either retired or in the DROP program.

Required contributions by the City/HBCRA for the General Employee Retirement plan were $3,331,672 and the Police Officers and Firefighters $7,908,910. The total of the two is $11,240,582 for FY 15/16. The employees also contribute and income from a State of Florida tax on insurance policies is used to make a total contribution of $13,330,511. There is also a Professional Management Plan which covers eight retirees, 22 of the members are entitled but not yet receiving benefits and eight are active members. The City's contribution to this plan is $691,355 and the employees contribute $58,625 bringing the total City pension cost to $14,080,491. The sheer size of this number (nearly 10 percent of the City's entire budget) and its absorption of resources as well as the continued growth in costs should be of great concern to the City Commission/HBCRA Board and to the employees to whom we have a fiduciary obligation to keep the retirement plans fiscally solvent.

The chart at the bottom of Page 69 is important as it defines the "Total Net Pension Liability" for all three pensions as $84,956,833. The Professional Management Plan is the best funded at 81.4 percent of full funding. The Police Officers and Fire

Fighters Pension Plan is funded at 67.94 percent of full funding and the General Employees Retirement Plan is funded at 79.35 percent of full funding. The table on page 73 presents a sensitivity analysis of how the pension liability would change based on a 1% increase or decrease in the discount rate. The discount rate is the assumed rate of investment return on pension plan assets. As you can see, the changes have a significant impact on the pension liability.

There are many municipalities and states nationwide that show pension liabilities for worse than these percentages. Having said this the pension costs for the City/HBCRA will continue to grow at an alarming rate using the current assumptions that form the basis of actuarial analysis. See the analysis of the Deferred Retirement Option Plan (DROP) and the earning expectations on various pages of Note 10 to understand that these assumptions increase cost factors significantly.

11) Other Post-Employment Benefits (OPEB) Note 11 on Page 78 – 79 reflects a liability of $6,941,414 for retiree health benefits. The City/HBCRA does not make contributions to this since the retirees pay the full cost of their health benefits at the same rates as current City employees as required by Florida Statutes. The question is whether the retirees' contribution is sufficient to pay their actual cost for health care benefits. Note 12 on Page 80 shows an increase of $1,902,645 or 47 percent in claims payable as of September 30, 2016. This means that the City/HBCRA contributions to the self-insurance funds need to be enhanced to cover future claims. The trend did not get better in FY 16/17.

12) The HBCRA operations separately represented is best defined in Note 14 on Page 81. Revenues to the HBCRA exceed expenses by $3,211,190. In future years, the policy goal should be that HBCRA revenue and expenses are more closely in alignment by the end of the fiscal year.

Required Supplementary Information:

This section provides information relative to budget to actual results for FY 15/16. The key chart for the General Fund is on Page 83 which reflects that the final adopted budget for FY 15/16 overstated General Fund revenues by $4,249,295 and understated expenses by $6,399,488 for a net positive difference from budget of $2,150,193. This number is offset by various transfers in and out and sale of capital assets for a FY 15/16 actual General Fund deficit of $1,815,845. This shortfall was taken from reserves.

The HBCRA budget to actual is stated on Page 84. The City/HBCRA pension liability change over three fiscal years is included on Page 87 – 92. The trend is that the total liability is increasing as well as the City's contributions in each of the three years reported.

Combining and Individual Fund Financial Statements and Schedules:

These charts appear on Page 94 – 102. There are a number of small funds included which is why they are called "non-major." Your attention is drawn to the Transportation Fund on Page 100. This fund shows a negative fund balance at the end of FY 15/16 which worsened in FY 16/17. The two security districts appear on Page 99 and 101 and both show strong balances at the end of FY 15/16. This is good news if we are to develop an underground utility project for Golden Isles.

Non Major Proprietary Funds:

This section which appears on Page 103 – 108 includes the Cemetery and Marina funds. There is nothing significant to report on these funds. It should be noted that the Marina fund was incorporated into the General Fund for FY 17/18.

Fiduciary Funds:

This section which appears on Page 109 – 113 includes the pension trust funds and the payroll and general trust fund which are used for holding monies due to employees, vendors and donors

Statistical Section:

This section provides very interesting statistics and trend analysis over long periods of time. The information begins on Page 114 and ends on Page 131 which is the last page of the CAFR. Highlights include:

1) Ten year data on the City/HBCRA net position show an increase in almost all areas from 2007 till 2011 and then a steady diminution from 2012 through 2016. This is due predominantly to debt issuance, deficit spending and the requirement to include pension liability. The detail of this trend can be seen on the charts on Page 114-116.

2) The trend over ten years in revenues and expenditures on Page 118 is illustrative of how deficit spending began in earnest in 2011. This parallels the decline in net position. The line at the bottom of the chart showing debt service as a percent of non-capital spending is interesting in that the percentage which is low by any standard doubled to 6.3 percent after voter approval of the Parks General Obligation debt.

3) The chart on Page 121 shows the principal tax payers in Hallandale Beach. Gulfstream Park is nearly 5 percent of the total tax base in 2016 up from 1.4 percent in 2007. This shows how important it is to nurture our large tax payers. It further shows that the top 12 tax payers in 2016 provide slightly above 10 percent of all property tax revenue.

4) The chart on Page 122 shows that the City consistently collects more than 99 percent of budgeted property taxes due with the exception of 2009-11 when the impacts of the Great Recession were being felt.

5) The chart on Page 123 provides important data on the relative growth of residential versus commercial property values. The City/HBCRA needs to accelerate the growth in commercial property values to offset the impact of long term financial needs on residential properties.

6) The chart on Page 130 reflects the number of Full Time Equivalent (FTE) positions in the City over a ten year period. The number has grown from 480.75 to 539.62 which reflects a growth rate of approximately 11 percent over the ten year period or a compounded rate of less than 2 percent per year. The detail by department is presented in the chart.

Compliance Reports:

This is a separate book because it is provided to grant agencies. The document comments on financial controls necessary to ensure that public funds are protected and that audit standards are met for grant agencies and other financial reports that are required. The report includes the auditor's findings and management's response as follows:

1) An overall explanation of this document appears on Page 1-5. There were deficiencies in management's internal controls during FY 15/16 which resulted in the need to provide a Corrective Action Plan (CAP).

2) The City expended $1,044,167 in federal awards in FY 15/16. The new Grants Development office should generate many times this amount during FY 17/18.

3) Page 8 lists the prior year (FY 14/15) findings related to closing out the financial year that were not corrected in FY 15/16. Two items from the previous year were corrected.

4) Page 9 lists negative findings such as material weakness (significant) and significant deficiencies (not as serious as material weakness). The results are that these findings must be reported to grant agencies and the City is not categorized as a "low risk" auditee which is a desirable status. This may impact our ability to obtain grants in a competitive process in the future.

5) Page 16-20 list the material weakness and significant deficiencies in detail. Management's response and how these issues will be remedied are also enumerated. These issues are numerous and do not need repetition from earlier elements of this memorandum. Suffice it to say that years of difficulty in the Finance Department will be rectified during FY 17/18 with continued support from the City Commission/HBCRA Board and with the appointment of Assistant City Manager Greg Chavarria as Interim Finance Director.

6) Page 24 – 26 includes new findings that are very concerning. These include misallocation of debt proceeds by the investment consultant, non-compliance with City investment policy for the City's excess benefit plan and non-compliance with reporting deadlines. Staff agrees with these findings and is working to resolve the auditor's concerns prior to the FY 16/17 audit.

7) Page 25 affirms that the CAFR was late in part due to the Foodman forensic audit. The multiple causes of this lack of timely submission have been documented throughout this memorandum.

8) Page 27 is a letter from Marcum to the City Commission and City Manager. Your attention is drawn to the second and third paragraph from the bottom. Marcum's key concern is noncompliance with the City's investment policy. The detail of this non-compliance is found on Page 25 and relates to change in arcane GASB rules. The accounting for this Excess Benefit Plan is not properly reported and the percentage of investment in international equities is too high. Staff will work with the auditors and investment managers to remedy both issues during FY 17/18.

9) The final element of the Compliance Reports is the Corrective Action Plan. This 5 page report enumerates how the findings from the audit will be resolved. Suffice it to say that staff is committed to achieving all the goals of the Corrective Action Plan during FY 17/18.

Conclusion:

With the eventual acceptance by the City Commission/HBCRA Board of the Foodman forensic audit and the Marcum CAFR and the commitment by the Administration to resolve long standing issues in the financial administration of both entities, it is time to close out FY 15/16 and prior years concerns and move forward.

FY 15/16 is the final year to be audited by Marcum after a long run. Marcum's audit fee was committed at $135,000. The firm states that it spent $286,408 to complete the CAFR. They have offered to reduce the $151,408 difference to $35,000 to settle out the account. This amount will be shared by the City and the HBCRA. This significant reduction is reasonable and the final negotiated amount will be paid. The new audit firm, selected under procedures required in State law is Mauldin & Jenkins, LLC. Their work will begin very soon for FY 16/17 and it is staff's goal to complete the CAFR timely.

The Foodman forensic audit and the Marcum CAFR present an enormous amount of data. The goal of this roadmap is to facilitate the reader's ability to dig deeply into any subject area using the page references included in the memorandum with the explanation of each section. The Administration plan is to respond to any questions that you may have on an individual basis and then place both documents and this memorandum on a joint City Commission/HBCRA meeting in April 2018. This will allow sufficient time to review the documents and become familiar with the many issues that are included and the solutions that will be recommended regarding the "true-up" suggested in the Foodman forensic audit and the financial controls that need improvement in the Marcum CAFR. It will also provide sufficient time for our new audit firm to become familiar with the issues.

In closing, it is important to thank the Marcum staff for their perseverance in completing the FY 15/16 and previous CAFR's and their service to the City/HBCRA. It is also important to thank Stanley Foodman for his detailed analysis of many issues that were questioned regarding the financial relationship of the City and the HBCRA. While there is much work to do to resolve the findings of the forensic audit, there is now an independent baseline to begin the discussion when the full City Commission/HBCRA Board is seated.

It would also be remiss not to thank staff in the Finance Department, Clerk's office and HBCRA for many hours of research required to provide information for both the forensic audit and the CAFR. There were many records that needed to be researched and hours of interviews with Mr. Foodman. Members of the City Commission/HBCRA Board, the City and HBCRA Attorneys and the City Manager's staff also provided valuable input and insight.

CC: Senior Staff
HBCRA Staff
City Attorney
HBCRA Attorney
Marcum
Stanley Foodman
Mauldin & Jenkins, LLC

Note: The Foodman forensic audit document may be found at the City website: https://fl-hallandalebeach3.civicplus.com/DocumentCenter/View/16372

The Marcum FY 15/16 CAFR and Compliance reports may be found at the City website: https://fl-hallandalebeach3.civicplus.com/DocumentCenter/View/16373