CITY OF MARCO ISLAND, FLORIDA

Auditor's Discussion and Analysis Presentation of Financial and Compliance Audit Results September 30, 2018

Presented by:
Wade Sansbury, CPA

MAULDIN & JENKINS

www.mjcpa.com

PURPOSE OF ANNUAL AUDIT AGENDA

- Engagement Team and Firm Information.
- Overview of:
  - Audit Opinion;
  - Financial Statements, Footnotes and Supplementary Information;
  - Compliance Reports;
  - Audit Scopes & Procedures.
- Required Communications under *Government Auditing Standards.*
- Other Matters for Communication.
- Answer Questions.

MAULDIN & JENKINS – GOVERNMENTAL PRACTICE

General Information:

- Founded in 1918. Approximately 300 personnel. Large regional Southeastern firm.
- Offices located in Bradenton, FL; Macon, Atlanta, Albany, Savannah, GA; Birmingham, AL; Columbia, SC; and Chattanooga, TN.

Governmental Sector:

- We are one of the largest providers to governmental entities in the Southeast with over 100,000 hours annually.
- Largest industry niche served by Firm (28% of Firm).
- Over 100 people with current government experience.
- In the past three years, have served approximately 450 governments in the Southeast, including:
  - ✓ 115 cities;
  - ✓ 55 counties;
  - ✓ 55 school systems and 30 Charter Schools;
  - ✓ 40 state entities;
  - ✓ 185 special purpose entities (stand-alone business type entities: water/sewer, transit, gas, electric, airports, housing development, retirement, libraries, etc);
  - ✓ Inclusive of the above, we serve 115 governments receiving the GFOA's Certificate of Achievement for Excellence in Financial Reporting.
- Experience performing forensic audit services and information technology consultations.
- Experience performing municipal bond debt issuance attestation services serving approximately 50 clients with over $11 billion in aggregate publicly issued debt instruments.
- Considered to be in the top 20 total number of single audits conducted in the U.S.A.

Engagement Team Leaders for the City Include:

- Wade Sansbury, Engagement Lead Partner: 23 years of experience, 100% governmental
- Daniel Anderson, Engagement Manager: 10 years of experience, 100% governmental
- Meredith Lipson, Quality Assurance Engagement Partner: 26 years of experience, 100% governmental

MAULDIN & JENKINS–ADDITIONAL INFORMATION

Other Industries & Services by Mauldin & Jenkins:

Each of Mauldin & Jenkins' offices provides a wide variety of services to a broad range of clientele. We have partners and managers who are responsible for specialized practice areas of auditing and accounting, taxes and management advisory services. Their purpose, as leaders in the particular practice area, is to establish policies with respect to technical matters in these specific areas and ensure that the quality of the Firm's practice is maintained.

Industries Served: Over the years our partners have developed expertise in certain industries representative of a cross section of the Florida economy, including:

- Governmental Entities (state entities, cities, counties, school systems, business type operations, libraries, and other special purpose entities)
- SEC Registrants
- Wholesale Distribution
- Agri-Businesses
- Manufacturing
- Professional Services
- Employee Benefit Plans
- Financial Institutions (community banks, savings and loans, thrifts, credit unions, mortgage companies, and finance companies)
- Non-profit Organizations
- Retail Businesses
- Long-term Healthcare
- Construction and Development
- Individuals, Estates and Trusts
- Real Estate Management

Services Provided: This diversity of practice enables our personnel to experience a wide variety of business, accounting and tax situations. We provide the traditional and non-traditional services such as:

- Financial Audit/Review/Compilation
- Compliance Audits and Single Audits
- Agreed-Upon Procedures
- Forensic Audits
- Bond Issuance Services
- Performance Audits
- State Sales Tax Matters
- International Tax Matters
- Business and Strategic Planning
- Profitability Consulting
- Budgeting
- Buy-Sell Agreements and Business Valuation Issues
- Income Tax Planning and Preparation
- Multi-State Income Tax Issues
- Information Systems Consulting
- Cost Accounting Analysis
- Healthcare Cost Reimbursement
- Outsourced Billing Services
- Fixed Asset Inventories
- Succession and Exit Strategy Consulting
- Estate Planning
- Management Information Systems
- Employee Benefit Plan Administration
- Merger/Acquisition and Expansion Financing

INDEPENDENT AUDITOR'S REPORT

The standard independent auditor's report for governmental units has specific sections of significance to readers of the financial report.

Management's Responsibility for the Financial Statements

The financial statements are the responsibility of management.

Auditor's Responsibility

Our responsibility, as external auditors, is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. We planned and performed our audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

Opinion

We have issued an unmodified audit report which is the highest form of assurance we can render with regard to the fairness of financial information on which we are opining. The financial statements are considered to present fairly the financial position and results of operations as of, and for the year ended September 30, 2018. Additionally, we included an emphasis of matter paragraph in this year's report regarding the City's implementation of GASB Statement No. 75 regarding other post-employment benefits. Our opinion was not modified with respect to this matter.

Other Matters

Certain required supplementary information and other information is included in the financial report, and as directed by relevant auditing standards, we have not expressed an opinion or provided any assurance on the respective information.

Other Reporting

Government Auditing Standards require auditors to issue a report on our consideration of internal control over financial reporting and on our tests of compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. We have issued such a report and reference to this report is included in the independent auditor's report.

REVIEW OF COMPREHENSIVE ANNUAL FINANCIAL REPORT

General Information About the CAFR

For some time, the City has issued a Comprehensive Annual Financial Report (CAFR). A CAFR goes beyond the normal financial reporting required by accounting principles generally accepted in the United States. A CAFR includes at a minimum the following elements/sections:

- **Introductory Section:** general information on the City's structure and the services it provides.
  - Letter of Transmittal
  - Organizational Chart
  - Directory of Officials
  - Certificate of Achievement for Excellence in Financial Reporting
- **Financial Section:** basic financial statements, footnotes and required supplementary information along with the auditor's report.
  - Independent Auditor's Report
  - Management Discussion & Analysis (MD&A)
  - Financial Statements and Footnotes
- **Statistical Section:** broad range of financial, demographic information useful in assessing the City's economic condition, and this information covers multiple years.
  - Financial Trends Information
  - Revenue Capacity Information
  - Debt Capacity Information
  - Operating Information

In the end, a CAFR goes far beyond the basic requirements of annual financial reporting, and the City should be commended for going beyond the minimum and providing such a report.

Recognition and Award

Once completed, the fiscal year 2017 CAFR was submitted to the Government Finance Officers Association (GFOA) for determination if the report would merit the GFOA's Certificate of Achievement for Excellence in Financial Reporting. We are happy to inform everyone that the GFOA did indeed review the CAFR and awarded the City with the sought after Certificate.

The GFOA Certificate has been made a part of the City's 2018 fiscal year CAFR, and is included in the Introductory Section. The City has received this prestigious award for the past 15 consecutive years.

REQUIRED COMMUNICATIONS

The Auditor's Responsibility Under *Government Auditing Standards* and Auditing Standards Generally Accepted in the United States of America

Our audit of the financial statements of the City of Marco Island, Florida (the "City") for the year ended September 30, 2018, was conducted in accordance with auditing standards generally accepted in the United States of America and *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether caused by error, fraudulent financial reporting or misappropriation of assets. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. Accordingly, the audit was designed to obtain reasonable, rather than absolute, assurance about the financial statements. We believe our audit accomplishes that objective.

In accordance with *Government Auditing Standards*, we have also performed tests of controls and compliance with laws and regulations that contribute to the evidence supporting our opinion on the financial statements. However, they do not provide a basis for opining on the City's internal control or compliance with laws and regulations.

Accounting Policies

Management has the ultimate responsibility for the appropriateness of the accounting policies used by the City. There are new accounting standards which will be required to be implemented in the coming years. These are discussed later in this document.

In considering the qualitative aspects of the City's accounting policies, we did not identify any significant or unusual transactions or significant accounting policies in controversial or emerging areas for which there is a lack of authoritative guidance or consensus. The City's policies relative to the timing of recording of transactions are consistent with GAAP and typical government organizations.

Management Judgments and Accounting Estimates

Accounting estimates are an integral part of the preparation of financial statements and are based upon management's current judgment. The process used by management encompasses their knowledge and experience about past and current events and certain assumptions about future events. Management has informed us they used all the relevant facts available to them at the time to make the best judgments about accounting estimates and we considered this information in the scope of our audit. We considered this information and the qualitative aspects of management's calculations in evaluating the City's significant accounting policies. Estimates significant to the financial statements include such items as the estimated lives of depreciable assets, the estimated allowance for uncollectible accounts, and the assumptions used in the actuarial valuations for the defined benefit plans and other post-employment benefits.

Financial Statement Disclosures

The footnote disclosures to the financial statements are also an integral part of the financial statements. The process used by management to accumulate the information included in the disclosures was the same process used in accumulating the financial statements, and the accounting policies described above are included in those disclosures. The overall neutrality, consistency and clarity of the disclosures was considered as part our audit and in forming our opinion on the financial statements.

Significant Difficulties Encountered in Performing the Audit

We encountered no difficulties in dealing with management relating to the performance of the audit.

Audit Adjustments

During our audit of the City's basic financial statements as of and for the year ended September 30, 2018, there were no adjustments prepared and proposed by the firm as a result of this year's audit.

Uncorrected Misstatements

During our audit of the City's basic financial statements as of and for the year ended September 30, 2018, there was one adjustment proposed by the firm which management elected not to post. This adjustment would increase assets and investment income by approximately $70,000 in the Police Pension Fund. The adjustment was proposed as a result of a timing difference between Investment Manager/Custodian year-end Statements and the Fund's year-end statement. The Financial Statements are not materially misstated as a result of this uncorrected misstatement.

Disagreements with Management

We encountered no disagreements with management over the application of significant accounting principles, the basis for management's judgments on significant matters, the scope of the audit or significant disclosures to be included in the financial statements.

Representation from Management

We requested written representations from management relating to the accuracy of information included in the financial statements and the completeness and accuracy of various information requested by us, during the audit. Management provided those written representations without delay and in an organized manner.

Management's Consultations with Other Accountants

We are not aware of any consultations management had with other accountants about accounting or auditing matters.

Significant Issues Discussed with Management

There were no significant issues discussed with management related to business conditions, plans or strategies that may have affected the risk of material misstatement of the financial statements. We are not aware of any consultations management had with us or other accountants about accounting or auditing matters. No major issues were discussed with management prior to our retention to perform the aforementioned audit.

Independence

We are independent of the City, and all related organizations, in accordance with auditing standards promulgated by the American Institute of Public Accountants and *Government Auditing Standards*, issued by the Comptroller General of the United States.

Other Information in Documents Containing Audited Financial Statements

We are not aware of any other documents that contain the audited basic financial statements. If such documents were to be published, we would have a responsibility to determine that such financial information was not materially inconsistent with the audited statements of the City.

OVERVIEW OF FINANCIAL STATEMENTS

A single audit report is included in this year's report as the City expended in excess of $750,000 of federal expenditures and state financial assistance. We noted no findings or questioned costs in performance of the Single Audits.

The financial statements as presented to you today include the basic financial statements as well as Management's Discussion and Analysis as prepared by City management.

The City's basic financial statements include three components: (1) government-wide financial statements; (2) fund financial statements; and (3) notes to the financial statements.

The **government-wide financial statements** provide a broad overview of all of the City's activities. The *Statement of Net Position* presents information on all assets and liabilities of the City, with the difference between the two reported as net position. The *Statement of Activities* presents information showing how the City's net position changed during the most recent fiscal year. Revenues are categorized as program revenues or general revenues. Expenses are categorized by function.

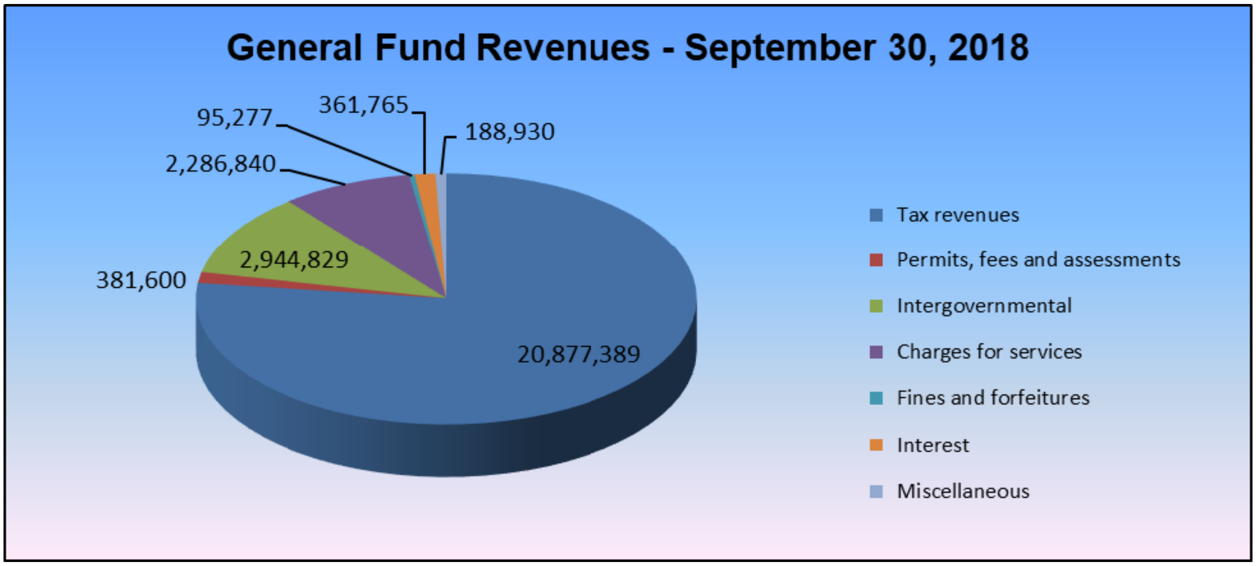
The **fund financial statements** more closely resemble the financial statements as presented prior to the adoption of GASB Statement No. 34. All of the funds of the City can be divided into three categories: (1) governmental funds, (2) proprietary funds, and (3) fiduciary funds.

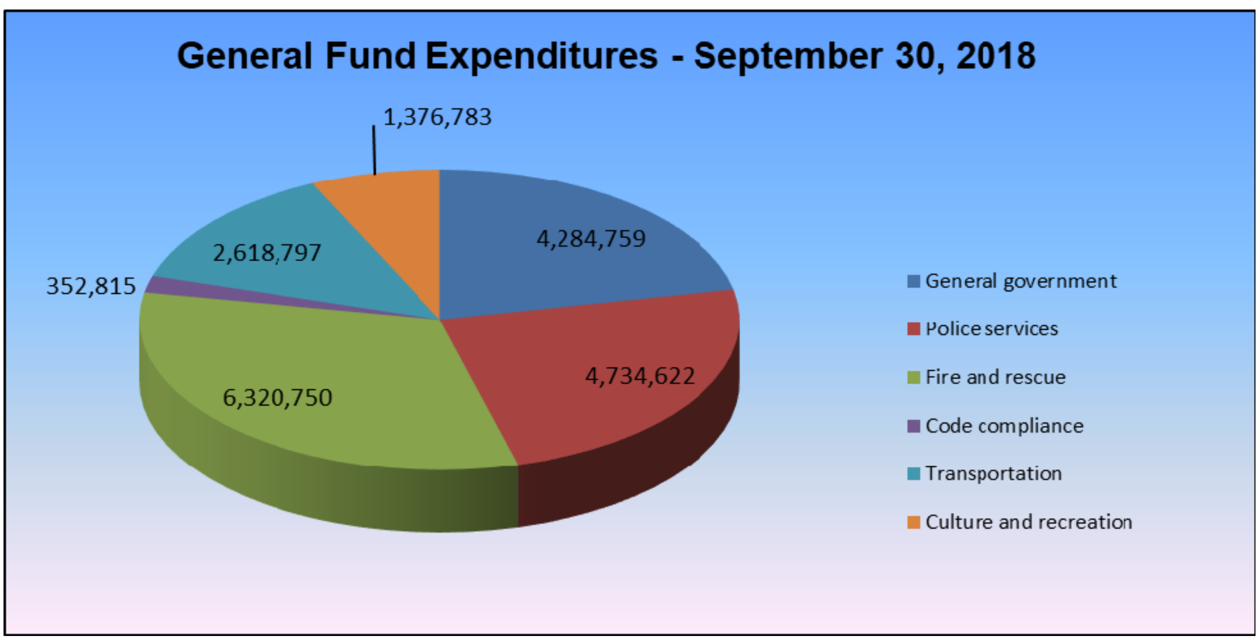
COMPLIANCE REPORTS

Included in the CAFR is our report based on our tests of the City's internal controls and compliance with laws, regulations, etc. The report is not intended to provide an opinion, but to provide a form of negative assurance as to the City's internal controls and compliance with applicable rules and regulations. This report and the procedures performed are required by *Government Auditing Standards* as issued by the U. S. Government Accountability Office (GAO).

General Fund

Of primary interest to the City is the General Fund, which accounts for the majority of revenues received and funds expended in the operations of the City, including administration, public safety, transportation, economic environment, and culture and recreation. The following charts present the sources of revenues and the expenditures of the General Fund for the fiscal year ended September 30, 2018:

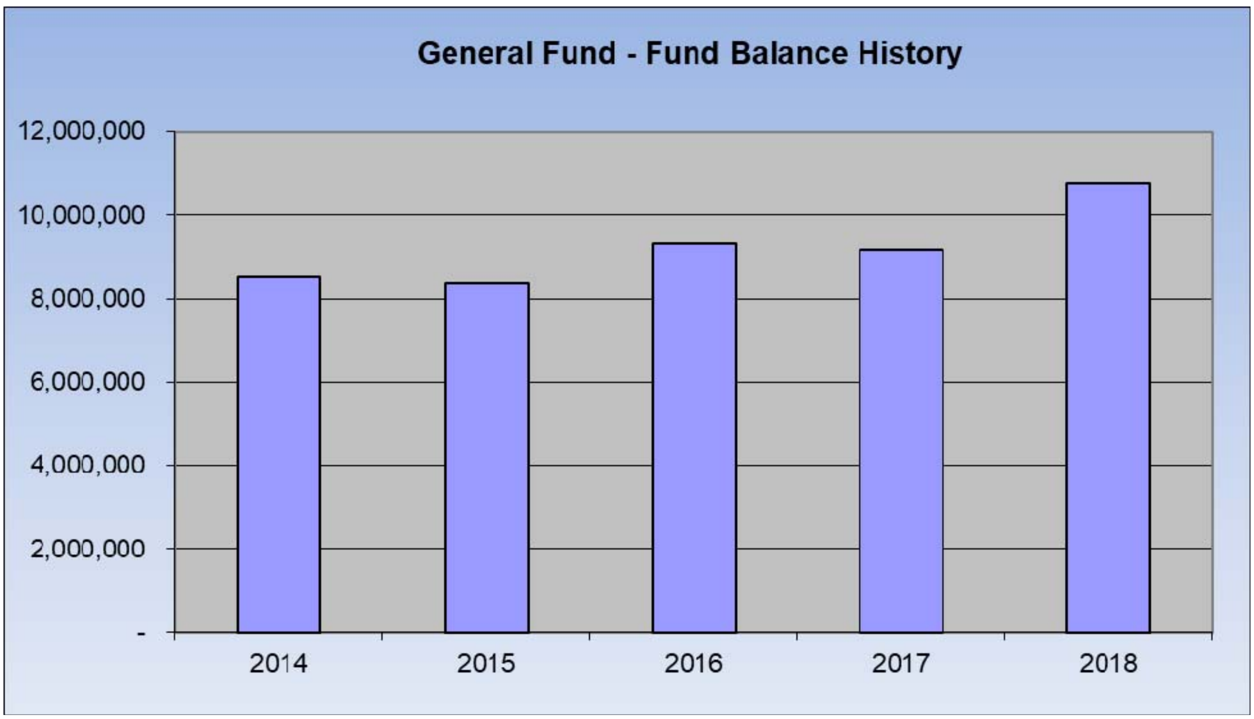




MAULDIN & JENKINS

Total fund balance of the General Fund at September 30, 2018, was a positive $10,773,399. Fund balance does not necessarily equal cash on hand and available to spend. Fund balance is the difference between assets and liabilities, of which only a portion of cash is available to be spent. While the City's General Fund has unrestricted cash and investments on hand at September 30, 2018, of $6,144,760, the City also has $1,697,578 in current liabilities due to outside parties and employees. Additionally, the General Fund incurs expenditures of approximately $1,650,000 per month. A large part of the cash on hand at September 30, 2018, will be needed in subsequent months to fund these expenditures, until the City's property tax revenues are collected beginning in November and December.

The following is a history of the total ending fund balance of the General Fund over the past five years:

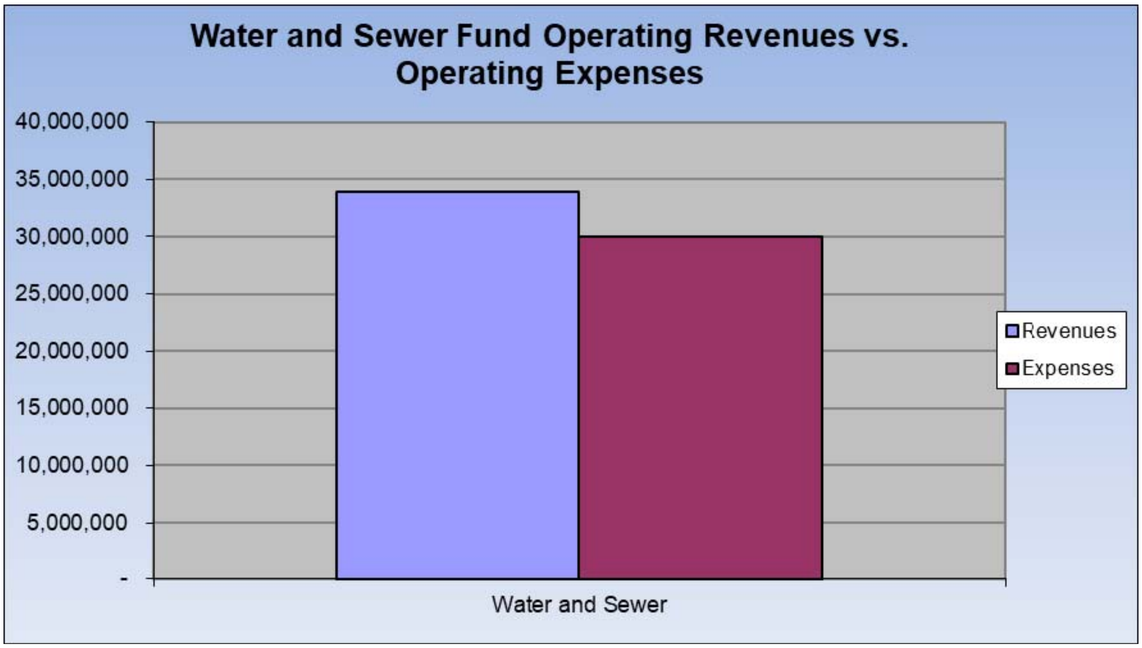


Other Governmental Funds

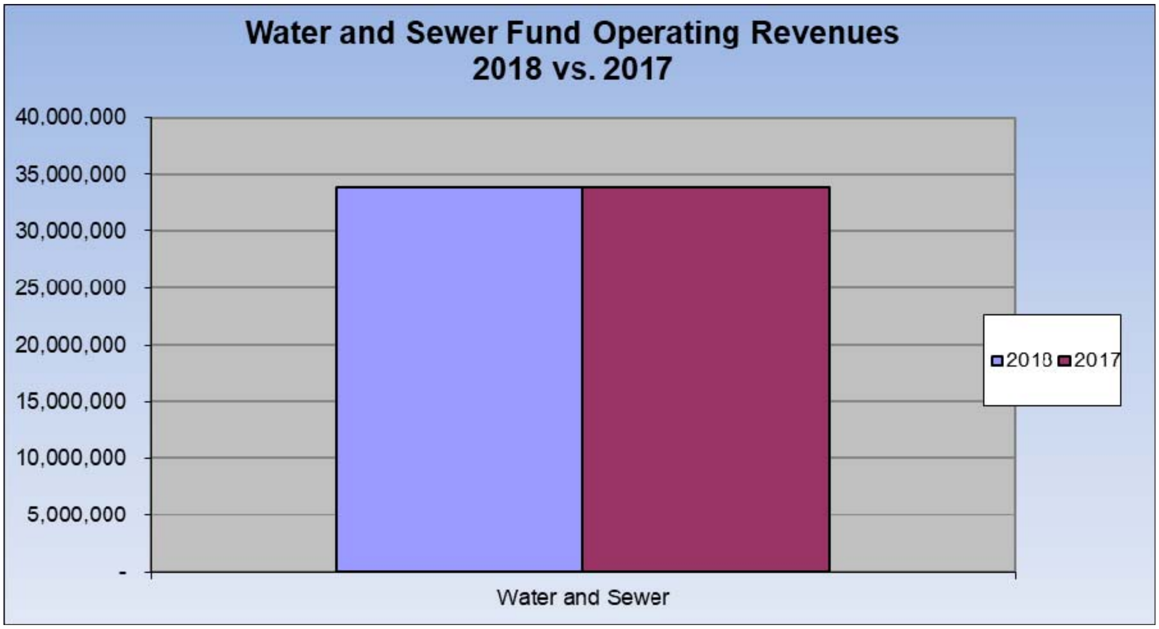
The City maintains various special revenue funds. These funds account for revenues derived from specific sources which are legally restricted to finance particular functions or activities. Capital projects funds are used to account for revenues and expenditures related to the renovation and/or construction of major capital assets.

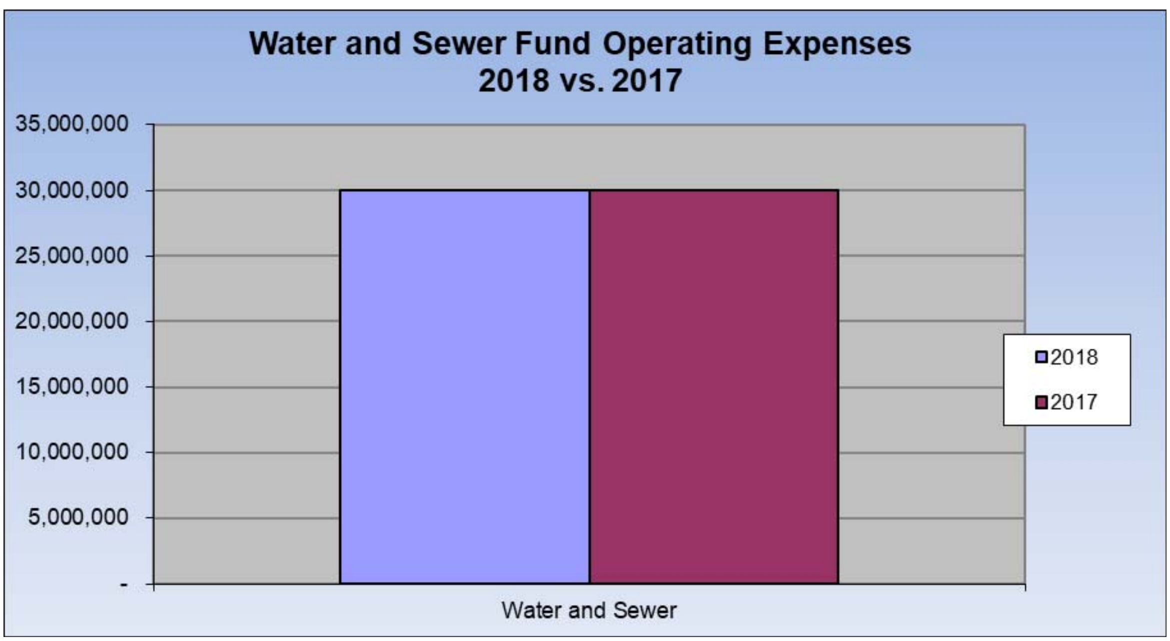
Enterprise Funds

The City maintains one major enterprise fund which is used to account for operations in a manner similar to private business enterprises – where the intent is that the costs of providing the goods or services to the general public on a continuing basis be financed or recovered primarily through user charges. The Water and Sewer Fund generally generates revenues sufficient to cover the costs of operations.



As noted within the following two tables, the City's Water and Sewer fund's operating revenues increased due to an increase in consumption in Fiscal Year 2018. The increase in Operating expenditures was primarily attributable to the 2% salary increase in Fiscal Year 2018.





MAULDIN & JENKINS

ACCOUNTING RELATED MATTERS

Other Matters Listed Only Within this Annual Auditor's Discussion and Analysis:

Disaster Preparedness – Disaster preparedness has become an increasingly important issue for local jurisdictions. Entrusted with mitigating the effects of disasters, local jurisdictions regard a quick response and effective recovery a paramount goal of disaster planning. For local jurisdictions, the concept of resiliency should be an integral part of disaster preparedness. Resiliency emphasizes the capacity of infrastructure, operations, and even social systems to respond to and recover from extreme events. Resilient systems reduce the probabilities of failure, the consequences of failure (such as deaths and injuries, physical damage, and negative economic and social effects), and the time for recovery. A resiliency-based approach is not reactionary to the effects of a disaster, but establishes parameters to contain the effects and because of this, a jurisdiction can measure its resiliency by how quickly it can rebound.

Traditional disaster preparedness emphasizes reacting to a disaster to effectively minimize losses rather than establishing a capital program to invest in assets that can better withstand and recover from extreme events. A growing sentiment within local jurisdictions recognizes that reactive policies may not be enough. Instituting a resiliency-based approach to capital planning can help sustain local services and assure that local jurisdictions remain functional or recover more rapidly following a disaster.

Building resiliency into the capital planning process includes setting appropriate parameters for new construction and the continued maintenance of key assets and infrastructure in order to strengthen a community's ability to withstand and respond to a disaster. Establishing a resilient capital program can aid the City by identifying costs associated with building, rebuilding or retrofitting infrastructure prior to disasters, and emphasizes the constant need for continued maintenance and improvement. A resiliency-based capital program can help the City identify critical assets, prioritize infrastructure risk, build in the appropriate and necessary costs, and establish a system that reduces the impact of disasters and the time required for a community to recover and get critical services back up and running.

We recommend the City incorporate resiliency into the capital planning process to produce a sustainable community and mitigate the effects of disasters. Ways of incorporating resiliency in the capital planning process include:

a) **Raising the visibility of resiliency by including in capital plans**. Resiliency-based capital planning recognizes the likelihood of disasters and operates proactively to reduce effects on the community. In planning for new capital projects, resiliency should be among the factors considered in prioritizing the construction, maintenance, or replacement of infrastructure and assets.

b) **Establishing roles and engaging the general public**. It is essential for the City to promote financial literacy to its citizens and its governing board so they understand the trade-offs associated with resiliency investments. For that reason, a program seeking to build a resilient community must include at a minimum the following participants: finance and budget officers, public safety officers, emergency management and business continuity officers, utility departments, engineers and construction project managers, public works officials, building regulations staff and planning and risk management staff as well as the public.
c) **Developing a resiliency plan**. Identifying the types of extreme events likely to befall upon the City and the type of infrastructure most likely to be affected provides the basis for resiliency investment and initiates the process for establishing measures of success.
d) **Planning begins by identifying resiliency needs**. To properly establish a resiliency-based approach to capital projects, the City should prepare a comprehensive inventory of its physical assets, create a system to determine critical assets and respective resiliency, and establish a scoring system that evaluates levels of resiliency. By doing so, the City can assess the ability of **infrastructure** and operational systems to withstand disasters.
e) **Funding decisions should be pursued after resiliency plans and project prioritization have been finalized**. Funding and building resiliency into infrastructure assets and operational systems can proceed in two basic ways. First, the City can use the rating system and prioritization to determine if resilient practices can be funded by capital budgets. This step should consider both resilient projects and non-resilient projects, and base funding decisions on the critical nature and need of the project. Second, if resiliency funding falls outside the scope of the capital budget, the City can pursue alternative funding mechanisms such as federal or state grants.

Including the Finance Department as Part of Disaster Preparedness

Planning for a disaster is no easy task. Calamity, man-made or natural, may strike at any time, threatening public safety or property, and recovery can be difficult and costly. The challenges the City could face could be even greater if the City's emergency operations plan does not specify the roles and responsibilities the Finance Department should play an emergency. Upon determining the potential financial impact of a disaster, the City should consider incorporating the Finance Department into its emergency operations plan and spell out four phases of its emergency management process: mitigation, preparedness, response, and recovery:

a) Mitigation. The finance team actively participates in the disaster mitigation process by allocating financial resources such as hazard mitigation grants to reduce the risk of identified hazards.
b) Preparedness. The team conducts annual disaster workshops for all city departments to review the City's policies and guidelines.
c) Response. Preparing City staff and the community at large before an emergency takes place makes it easier for the City to coordinate response when a disaster occurs.
d) Recovery. Because recovery can be a lengthy and costly process, the city manages its resources efficiently and tracks costs for reimbursement that will help return it to pre-disaster conditions.

Through clearly defined and designated roles, the City's Finance Department can play a key part in ensuring that the City mitigates its risks, is prepared, can effectively respond and quickly recover when disaster strikes.

Information Technology – The Information Technology environment is characterized by rapid change and there has been no shortage of headlines about cybersecurity attacks. While breaches of large organizations have been very high profile and have received a lot of press coverage, organizations of all sizes face the same types of threats and are experiencing similar breaches. Many organizations are still struggling to effectively address cybersecurity issues; however, they are no longer ignoring them. During the performance of our audit of the financial statements of the City, we noted that the organization is lacking some elements of a Cybersecurity Framework or Cybersecurity Risk Management Program (CRMP). A functioning CRMP will assist the City with comprehensively identifying cybersecurity weaknesses, potential threats and risks, and controls used to safeguard information and systems. We recommend that the entity investigate and consider implementation of a Cybersecurity Risk Management Program covering Cybersecurity risk assessment, identification of sensitive data, use of strong passwords, software updates/patching cadence, audit security measures, and monitoring and testing of controls in place.

Other Matters for Communication to the City Commission and Management

During our audit of the financial statements as of and for the year ended September 30, 2018, we noted other matters which we wish to communicate to you in an effort to keep the City abreast of accounting matters that could present challenges in financial reporting in future periods.

New Governmental Accounting Standards Board (GASB) Pronouncements

As has been the case for the past ten years, GASB has issued several other new pronouncements which will be effective in future years. The following is a brief summary of the new standards:

a. **Statement No. 75, *Accounting and Financial Reporting for Post-employment Benefits Other Than Pensions*** was issued in June of 2015, and is effective for financial statements for periods beginning after June 15, 2017, resulting in the City's fiscal year ending September 30, 2018. This statement could easily be described as the GASB No. 68 for post-employment benefit plans due to the fact that it will closely follow the provisions of GASB No. 68 for pension plans.

   The primary objective of this statement is to improve accounting and financial reporting by state and local governments for post-employment benefits other than pensions (other post-employment benefits or OPEB). It also improves information provided by state and local governmental employers about financial support for OPEB that is provided by other entities. This statement results from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for all post-employment benefits (pensions and OPEB) with regard to providing decision-useful information, supporting assessments of accountability and inter-period equity, and creating additional transparency.

   This statement replaces the requirements of Statements No. 45, *Accounting and Financial Reporting by Employers for Post-employment Benefits Other Than Pensions*, as amended, and No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans, for OPEB. Statement No. 74, Financial Reporting for Post-employment Benefit Plans Other Than Pension Plans*, establishes new accounting and financial reporting requirements for OPEB plans.

   The scope of this statement addresses accounting and financial reporting for OPEB that is provided to the employees of state and local governmental employers. This statement establishes standards for recognizing and measuring liabilities, deferred outflows of resources, deferred inflows of resources, and expense/expenditures. For defined benefit OPEB, this statement identifies the methods and assumptions that are required to be used to project benefit payments, discount projected benefit payments to their actuarial present value, and attribute that present value to periods of employee service. Note disclosure and required supplementary information requirements about defined benefit OPEB also are addressed.

In addition, this statement details the recognition and disclosure requirements for employers with payables to defined benefit OPEB plans that are administered through trusts that meet the specified criteria and for employers whose employees are provided with defined contribution OPEB. This statement also addresses certain circumstances in which a non-employer entity provides financial support for OPEB of employees of another entity.

In this statement, distinctions are made regarding the particular requirements depending upon whether the OPEB plans through which the benefits are provided are administered through trusts that meet the following criteria:

- Contributions from employers and non-employer contributing entities to the OPEB plan and earnings on those contributions are irrevocable.
- OPEB plan assets are dedicated to providing OPEB to plan members in accordance with the benefit terms.
- OPEB plan assets are legally protected from the creditors of employers, non-employer contributing entities, the OPEB plan administrator, and the plan members.

The requirements of this statement will improve the decision-usefulness of information in employer and governmental non-employer contributing entity financial reports and will enhance its value for assessing accountability and inter-period equity by requiring recognition of the entire OPEB liability and a more comprehensive measure of OPEB expense. Decision-usefulness and accountability also will be enhanced through new note disclosures and required supplementary information.

b. **Statement No. 81, *Irrevocable Split-Interest Agreements*** was issued in March of 2016, and is effective for financial statements for periods beginning after December 15, 2016, resulting in the City's fiscal year ending September 30, 2018.

   Irrevocable split-interest agreements (which are prevalent at colleges and universities) whereby split-interest agreements in which an asset is given to a government in trust. During stated term of the trust the income generated by the trust goes to the donor and when the trust ends then the assets become the governments. We do not expect this pronouncement to affect the financial reporting of the City.

c. **Statement No. 82, *Pension Plans*** was issued in April 2016, and is effective for the first reporting period in which the City's pension plan's measurement date is on or after June 15, 2017. No real significant matters noted in this standard which addresses:

   - Presentation of payroll-related measures in the Required Supplementary Information of the annual audited financial report. Covered payroll is defined as the payroll on which contributions are based;
   - Selection of actuarial assumptions. Any deviation from guidance of Actuarial Standards Board is not in conformity with GASB No. 67 & 68;

MAULDIN & JENKINS

- Classification of payments made by employers to satisfy contribution requirements:
  - Payments made by employer to satisfy contribution requirements that are identified as plan member contributions should be classified as "plan member contributions" for GASB No. 67, and as "employee contributions" for GASB No. 68; and,
  - Expense to be classified as other compensation elements.

d. Statement No. 83, *Certain Asset Retirement Obligations* was issued in November 2016, and is effective for the first reporting period beginning after June 15, 2018. An asset retirement obligation (ARO) is a legally enforceable liability associated with the retirement of a tangible capital asset. This statement establishes the criteria for determining the timing and pattern of recognition of a liability and a corresponding deferred outflow of resources for ARO's. Timing could be based on the occurrence of external laws, regulations, contracts or court judgments. Examples include the closure of a nuclear reactor or a sewage treatment facility. This statement addresses the financial reporting and accounting as well as the respective disclosures relative to ARO's.

e. Statement No. 84, *Fiduciary Activities* was issued in January 2017, and is effective for the first reporting period beginning after December 15, 2018. This statement establishes criteria for identifying fiduciary activities with a focus on: (1) whether a government is controlling the assets of the fiduciary activity; and, (2) the beneficiaries with whom a fiduciary relationship exists.

Further, this statement describes four fiduciary funds that should be reported, if applicable: (1) pension and other employee benefit trust funds; (2) investment trust funds; (3) private-purpose trust funds; and, (4) custodial funds. Custodial funds generally should report fiduciary activities that are not held in a trust or equivalent arrangement that meets specific criteria.

f. Statement No. 85, *Omnibus 2017* was issued in March 2017, and is effective for the first reporting period beginning after June 15, 2017. This statement addresses a variety of topics including issues related to:

- Component Units - blending a component unit in circumstances in which the primary government is a business-type activity that reports in a single column for financial statement presentation;
- Goodwill - reporting amounts previously reported as goodwill and "negative" goodwill;
- Real Estate - classifying real estate held by insurance entities;
- Fair Value Measurement and Application - measuring certain money market investments and participating interest earning investment contracts at amortized cost;
- Post-employment benefits (pensions and other post-employment benefits [OPEB]):

- Timing of the measurement of pension or OPEB liabilities and expenditures recognized in financial statements prepared using the current financial resources measurement focus;
- Recognizing on-behalf payments for pensions or OPEB in employer financial statements;
- Presenting payroll-related measures in Required Supplementary Information for purposes of reporting by OPEB plans and employers that provide OPEB;
- Classifying employer-paid member contributions for OPEB;
- Simplifying certain aspects of the alternative measurement method for OPEB; and,
- Accounting and financial reporting for OPEB provided through certain multiple-employer defined benefit OPEB plans.

g. **Statement No. 86, *Certain Debt Extinguishment Issues*** was issued in May 2017, and is effective for the first reporting period beginning after June 15, 2017. The primary objective of this statement is to improve consistency in accounting and financial reporting for in-substance defeasance of debt by providing guidance for transactions in which cash and other monetary assets acquired with only existing resources (resources other than the proceeds of refunding debt) are placed into an irrevocable trust for the sole purpose of extinguishing debt. This statement also addresses prepaid insurance on debt that is extinguished and the notes to financial statements for debt that is in-substance defeased.

h. **Statement No. 87, *Leases*** was issued in June 2017, and is effective for the first reporting period beginning after December 15, 2019. This statement increases the usefulness of governments' financial statements by requiring recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and recognized as inflows of resources or outflows of resources based on the payment provisions of the contract. It establishes a single model for lease accounting based on the principle that a lease is the financing of the right to use an underlying asset.

   Under this statement, a lessee is required to recognize a lease liability and an intangible right-to-use lease asset, and a lessor is required to recognize a lease receivable and a deferred inflow of resources, thereby enhancing the relevance and consistency of information about governments' leasing activities.

   Definition of a Lease: A lease is defined as a contract that conveys control of the right to use another entity's nonfinancial asset (the underlying asset) as specified in the contract for a period of time in an exchange or exchange-like transaction. Examples of nonfinancial assets include buildings, land, vehicles, and equipment. Any contract that meets this definition should be accounted for under the leases guidance, unless specifically excluded in this statement.

Lease Term: The lease term is defined as the period during which a lessee has a non-cancelable right to use an underlying asset, plus the following periods, if applicable:

- Periods covered by a lessee's option to extend the lease if it is reasonably certain, based on all relevant factors, that the lessee will exercise that option;
- Periods covered by a lessee's option to terminate the lease if it is reasonably certain, based on all relevant factors, that the lessee will not exercise that option;
- Periods covered by a lessor's option to extend the lease if it is reasonably certain, based on all relevant factors, that the lessor will exercise that option;
- Periods covered by a lessor's option to terminate the lease if it is reasonably certain, based on all relevant factors, that the lessor will not exercise that option.

A fiscal funding or cancellation clause should affect the lease term only when it is reasonably certain that the clause will be exercised. Lessees and lessors should reassess the lease term only if one or more of the following occur:

- The lessee or lessor elects to exercise an option even though it was previously determined that it was reasonably certain that the lessee or lessor would not exercise that option;
- The lessee or lessor elects not to exercise an option even though it was previously determined that it was reasonably certain that the lessee or lessor would exercise that option;
- An event specified in the lease contract that requires an extension or termination of the lease takes place.

Short-Term Leases: A short-term lease is defined as a lease that, at the commencement of the lease term, has a maximum possible term under the lease contract of 12 months (or less), including any options to extend, regardless of their probability of being exercised. Lessees and lessors should recognize short-term lease payments as outflows of resources or inflows of resources, respectively, based on the payment provisions of the lease contract.

Lessee Accounting: A *lessee* should recognize a lease liability and a lease asset at the commencement of the lease term, unless the lease is a short-term lease or it transfers ownership of the underlying asset. The lease liability should be measured at the present value of payments expected to be made during the lease term (less any lease incentives). The lease asset should be measured at the amount of the initial measurement of the lease liability, plus any payments made to the lessor at or before the commencement of the lease term and certain direct costs.

A *lessee* should reduce the lease liability as payments are made and recognize an outflow of resources (for example, expense) for interest on the liability. The lessee should amortize the lease asset in a systematic and rational manner over the shorter of the lease term or the useful life of the underlying asset. The notes to financial statements should include a description of leasing arrangements, the amount of lease assets recognized, and a schedule of future lease payments to be made.

Lessor Accounting: A *lessor* should recognize a lease receivable and a deferred inflow of resources at the commencement of the lease term, with certain exceptions for leases of assets held as investments, certain regulated leases, short-term leases, and leases that transfer ownership of the underlying asset. A lessor should not derecognize the asset underlying the lease. The lease receivable should be measured at the present value of lease payments expected to be received during the lease term. The deferred inflow of resources should be measured at the value of the lease receivable plus any payments received at or before the commencement of the lease term that relate to future periods.

A lessor should recognize interest revenue on the lease receivable and an inflow of resources (for example, revenue) from the deferred inflows of resources in a systematic and rational manner over the term of the lease. The notes to financial statements should include a description of leasing arrangements and the total amount of inflows of resources recognized from leases.

Contracts with Multiple Components and Contract Combinations: Generally, a government should account for the lease and non-lease components of a lease as separate contracts. If a lease involves multiple underlying assets, lessees and lessors in certain cases should account for each underlying asset as a separate lease contract. To allocate the contract price to different components, lessees and lessors should use contract prices for individual components as long as they do not appear to be unreasonable based on professional judgment, or use professional judgment to determine their best estimate if there are no stated prices or if stated prices appear to be unreasonable. If determining a best estimate is not practicable, multiple components in a lease contract should be accounted for as a single lease unit. Contracts that are entered into at or near the same time with the same counterparty and that meet certain criteria should be considered part of the same lease contract and should be evaluated in accordance with the guidance for contracts with multiple components.

Lease Modifications and Terminations: An *amendment* to a lease contract should be considered a lease modification, unless the lessee's right to use the underlying asset decreases, in which case it would be a partial or full lease termination. A lease termination should be accounted for by reducing the carrying values of the lease liability and lease asset by a lessee, or the lease receivable and deferred inflows of resources by the lessor, with any difference being recognized as a gain or loss. A lease modification that does not qualify as a separate lease should be accounted for by re-measuring the lease liability and adjusting the related lease asset by a lessee and re-measuring the lease receivable and adjusting the related deferred inflows of resources by a lessor.

Subleases and Leaseback Transactions: Subleases should be treated as transactions separate from the original lease. The original lessee that becomes the lessor in a sublease should account for the original lease and the sublease as separate transactions, as a lessee and lessor, respectively.

A transaction qualifies for sale-leaseback accounting only if it includes a sale. Otherwise, it is a borrowing. The sale and lease portions of a transaction should be accounted for as separate sale and lease transactions, except that any difference between the carrying value of the capital asset that was sold and the net proceeds from the sale should be reported as a deferred inflow of resources or a deferred outflow of resources and recognized over the term of the lease.

A lease-leaseback transaction should be accounted for as a net transaction. The gross amounts of each portion of the transaction should be disclosed.

i. **Statement 88, *Certain Disclosures Related to Debt, Including Direct Borrowings and Direct Placements*** was issued in March 2018, and is effective for reporting periods beginning after June 15, 2018 (meaning September 30, 2019). This standard defines debt for disclosure purposes and adds disclosures related to debt (it does not reduce any previously required disclosures).

Under Statement 88, debt for disclosure purposes is defined as a liability that arises from a contractual obligation to pay cash (or other assets) in one or more payments to settle an amount that is fixed at the date the contractual obligation is established. This would include, but is not limited to:

- Direct Borrowings: Entering into a loan agreement with a lender.
- Direct Placements: Issuing a debt security directly to an investor.

This excludes leases (except for contracts reported as a financed purchase) and accounts payable.

In addition to other disclosures related to debt, the notes to the financial statements should include:

- The amount of any unused lines of credit.
- Assets pledged as collateral for debt.
- Terms specified in the debt agreement related to significant:
  - Events of default with finance-related consequences
  - Termination events with finance-related consequences
  - Subjective acceleration clauses
- Debt disclosures should separate information regarding direct borrowings and direct placements from other debt.

j. **Statement 89, *Accounting for Interest Cost Incurred Before the End of a Construction Period*** was issued in June 2018, and is effective for reporting periods beginning after December 15, 2019 (meaning September 30, 2021). This standard eliminates the requirement/ability to capitalize construction period interest costs as part of the cost of a capital asset in enterprise funds. This standard should be applied prospectively with no restatement. This standard can be early implemented as part of fiscal year 2019.

k. **Other Pending or Current GASB Projects.** As noted by the numerous pronouncements issued by GASB over the past decade, the GASB continues to research various projects of interest to governmental units. Subjects of note include:

- **Re-Examination of the Financial Reporting Model.** GASB has added this project to its technical agenda to make improvements to the existing financial reporting model (established via GASB 34). Improvements are meant to enhance the effectiveness of the model in providing information for decision-making and assessing a government's accountability. GASB anticipates issuing an initial due process document on this project by the end of 2017.
- **Conceptual Framework** is a constant matter being looked at by GASB. Current measurement focus statements (for governmental funds) to change to near-term financial resources measurement. May dictate a period (such as 60 days) for revenue and expenditure recognition. May expense thing such as supplies and prepaid assets at acquisition. Will look into which balances (at all statement levels) are measured at acquisition and which need to be re-measured at year-end. Project placed on hold for now.
- **Economic Condition Reporting** is another long-term matter being looked into by GASB. Includes presentation of information on fiscal sustainability (including projections). Tabled for now pending resolution to issues raised on GASBs scope.

Summations of Thoughts Noted Above

We believe the implementation of these suggestions will enhance both the control environment and the financial reporting process, making both more effective. We also believe these recommendations can be easily implemented, and all problems resolved quite timely should management elect to employ the corrective measures.

COMPLIMENTARY CONTINUING EDUCATION AND NEWSLETTERS FOR GOVERNMENTAL CLIENTS

Complimentary Continuing Education. We provide complimentary continuing education for all of our governmental clients. Annually, we pick a couple of significant topics tailored to be of interest to governmental entities. We provide these complimentary services typically in the summer months over a two day period and typically see 40 to 50 people. We obtain the input and services of experienced outside speakers along with providing the instruction utilizing our in-house professionals. We hope City staff and officials have been able to participate in this opportunity, and that it has been beneficial to you. Examples of subjects addressed in the past include:

1. Accounting for Debt Issuances
2. American Recovery & Reinvestment Act (ARRA) Updates
3. Best Budgeting Practices, Policies and Processes
4. CAFR Preparation (several times including a two day hands-on course)
5. Capital Asset Accounting Processes and Controls
6. Collateralization of Deposits and Investments
7. Evaluating Financial and Non-Financial Health of a Local Government
8. GASB No. 51, Intangible Assets
9. GASB No. 54, Governmental Fund Balance (subject addressed twice)
10. GASB No. 60, Service Concession Arrangements (webcast)
11. GASB No. 61, the Financial Reporting Entity (webcast)
12. GASB No.'s 63 & 65, Deferred Inflows and Outflows (webcast)
13. GASB No.'s 67 & 68, New Pension Stds. (presented several occasions)
14. GASB Updates (ongoing and several sessions)
15. Grant Accounting Processes and Controls
16. Internal Controls Over Accounts Payable, Payroll and Cash Disbursements
17. Internal Controls Over Receivables & the Revenue Cycle
18. Internal Revenue Service (IRS) Issues, Primarily Payroll Matters
19. Legal Considerations for Debt Issuances & Disclosure Requirements
20. Policies and Procedures Manuals
21. Segregation of Duties
22. Single Audits for Auditees
23. Uniform Grant Reporting Requirements and the New Single Audit

Governmental Newsletters. We produce newsletters tailored to meet the needs of governments. The newsletters have addressed a variety of subjects and are intended to be timely in their subject matter. The newsletters are authored by Mauldin & Jenkins partners and managers, and are not purchased from an outside agency. The newsletters are produced and delivered periodically (approximately six times per year), and are intended to keep you informed of current developments in the government finance environment.

Communication. In an effort to better communicate our complimentary continuing education plans and newsletters, please email Paige Vercoe at Pvercoe@mjcpa.com and provide to her individual names, mailing addresses, email addresses, and phone numbers of anyone you wish to participate and be included in our database.

CLOSING

We believe the implementation of these suggestions will enhance both the control environment and the financial reporting process, making both more effective. We also believe these recommendations can be easily implemented, and all problems resolved quite timely should management elect to employ the corrective measures. If you have any questions regarding any comments, suggestions or recommendations set forth in this memorandum, we will be pleased to discuss it with you at your convenience.

This information is intended solely for the use of the City's management, and others within the City's organization and is not intended to be and should not be used by anyone other than these specified parties.

We appreciate the opportunity to serve the City of Marco Island, Florida, and look forward to serving the City in the future. Thank you.