



**MANAGER'S BRIEFING SESSION
HIGH POINT MUNICIPAL BUILDING
DECEMBER 19, 2016 – 4:00 P.M.
3RD FLOOR LOBBY CONFERENCE ROOM**

Present:

Mayor William S. Bencini, Jr.; Mayor Pro Tem Golden (Ward 1); and Council Members Latimer Alexander (At-Large); Cynthia Davis (At-Large); Jason Ewing (Ward 6) (Joined the meeting at 4:10 p.m.); Alyce Hill (Ward 3); Council Members Jay Wagner (Ward 4) and Jim Davis (Ward 5) and Chris Williams (Ward 2)

Staff Present:

Greg Demko, City Manager; Randy McCaslin, Deputy City Manager; Randy Hemann, Assistant City Manager; JoAnne Carlyle, City Attorney; Eric Olmedo, Budget & Administrative Director; Jeron Hollis, Director of Communications & Public Engagement; Jeff Moore, Director of Financial Services; Loren Hill, President- High Point Economic Development Corporation; Maria Smith, Deputy City Clerk; and Lisa Vierling, City Clerk

Others Present:

Fred Baggett
Eddie Burke, CPA, Audit Partner, Cherry Bekaert

News Media:

Pat Kimbrough, High Point Enterprise

Handouts: *Audit Presentation FY2015-16 Budget (Audit Wrap-Up)*
 CAFR (Comprehensive Audit Financial Report) for FY End June 30, 2016- This document
 will be not be attached due to the volume of the information, but will be on file in the
 Financial Services Director's Office and City Clerk's Office
 Stand Alone Audit Letter
 Discussion on the upcoming 2017 North Carolina Legislative session

Note: *These handouts will be attached as a permanent part of these proceedings.*

Greg Demko, City Manager called the Manager's Briefing meeting to order and introduced Eddie Burke, CPA, Audit Partner with Cherry Bekaert.

Audit Presentation FY2015-16 Budget

Mr. Burke made reference to the Financial Statements that were provided to Council, the stand alone letter, and the presentation (audit wrap-up). He explained in order for any CPA to be able to issue an opinion on financial statements, there has to be some level of internal control environment that can be relied upon. The auditors spent a majority of their time on the significant audit areas. He pointed out as part of the quality

control process in their firm, they have an individual partner who is not associated with the engagement, but reviews the audit quality to make sure that current policy and professional standards have been followed.

He advised there are three primary things external auditors are responsible for:

- 1) To plan and perform the audit in accordance to the GASB standards
- 2) Once the audit is planned and completed, they issue an opinion on the financial statements
- 3) From a communication perspective, the standards require that they communicate certain things to the oversight body on an annual basis.

From an overall perspective, there were four audit opinions expressed: opinion on the financial statements; a yellow book opinion (review and compliance); single audit opinion (federal and state dollars received and administered during the current year); and two single audit opinions (administrative controls and compliance). Mr. Burke noted that the city did receive an unmodified or what is referred to as a *clean opinion* on all four of those reports.

From an **internal control** perspective on the financial statements, they did not identify any significant deficiencies or material weaknesses. As far as the **single audit** was concerned, there was one non-material, non-compliance issue that had to do with one of the funds that was administered during the year where the budget was over expended (the Health and Wellness fund). There was also a significant deficiency reported having to do with the Powell Bill report. Mr. Burke advised there were some costs on the Powell Bill report that were not allowable, but it did get corrected before the Powell Bill report was actually filed with the state.

From a **reporting perspective**, there were two new GASB statements that had to be implemented this year with the first being GASB Statement 72. He explained the biggest impact on the City was the change and the note disclosure over investments. He reported GASB 73 also had to be implemented and this was the biggest impact in the financial statements. He reported that historically the city had been reporting the LEOSSA Fund (the Law Enforcement Separation Allowance) as a Pension Trust Fund, but GASB 73 required in order for this to continue to be reported as a Pension Trust Fund, the funds had to be in an irrevocable trust. These funds were not, so GASB 73 requires that this fund be reported as a sub fund of the General Fund.

He reviewed three past adjusting journal entries that were recorded. One had to do with loans, where all governmental agencies across the state had to change the way the loans were reported. He explained when this adjustment was made last year, some loans that were not picked up properly from a generated report. This was caught by the city and was immaterial. Another had to do with the stipend liability. He noted a question arose last year as to whether or not this would be classified as a retirement plan benefit or compensated absences. City staff researched this and it was determined to be more like compensated absences, so the entire liability needed to be approved with part of this in the period of June 30, 2015. The third item had to do with GASB 68 and some numbers were not picked up for the deferred outflow of funds. Mr. Burke pointed out this was a statewide issue.

Mr. Burke advised that the city is actually in a very good spot with many positive things going on such as High Point University and the Furniture Market. He noted these are great revenue generators and encouraged the city to continue to leverage off of these as much as possible. He also mentioned the HB2 law that might get repealed in the state and it was hopeful that this would change the market a little in High Point as far as businesses coming in. He informed Council about some reports that were filed late with the Local Government Commission having to do with cash, deposit and investments.

As far as **Internal Controls** are concerned, Mr. Burke reported on the following four areas:

- 1) **Significant cycles (payroll; cash receipts/billings; accounts payable and accruals; cash disbursements; recording purchases; financial close and reporting; managing investments, grants, etc.....).** He explained key controls are identified in the processes and noted if they fail something could go wrong and not be caught internally.
- 2) **Testing of Controls (budgeting process; cash disbursements).** He reported the results from these tests indicated the control environment was working effectively for these two cycles in this particular year.
- 3) **Adjusted Journal Entries (AJEs) (active data).** This consisted of a data dump from all the adjusted journal entries that were posted from current year. This data was loaded into active data software, which sorted the journal entries and identified high risk journal entries. From a trending perspective, some of the things they look for are: who initiated the journal entry; who approved it to ensure there was segregation of duties; and the reason the journal entry was made; and to see if there were a lot of journal entries made to correct other journal entries and to see if there were any patterns. All tests conducted in this area came back clean
- 4) **IT Controls:** He shared they had an IT Auditor to come in and do this portion of the audit and they were looking for ways to see whether or not they could rely on the IT system control procedure that was in place. He added that they looked at the IT controls along with backup, recovery, access, and security (network and cyber). He also noted that IT needs to continue to monitor this and be aware of cyber security and hacking threats.

Council Member J. Davis mentioned the significant reporting issue with the Powell Bill and asked for an explanation. Mr. Burke explained they were basically looking at the administrative controls and when they reviewed the Powell Bill report, they noticed there were some streets/costs that were going to be inaccurately reported that were not allowable. Council Member J. Davis asked if the auditors saw any problems like this last year and Mr. Burke replied they did not. Jeff Moore, Director of Financial Services, attributed the issue with a turnover in staff and explained there were more than enough expenses to qualify.

Council Member J. Davis then addressed the reports that were not completed in a timely manner and asked if this was also attributed to being short staffed. Mr. Moore replied that it had been an ongoing problem and it had been highlighted over the last several years with both management and council. He noted he has been asking for additional staff since 2009 and asked for three additional staff people last year. He admitted that the responsiveness has deteriorated over the last several years as a result of staff's heavy workload. He explained if a financial penalty was involved, staff made sure those reports were done in a timely matter, but if no penalty was involved, the report would take a backseat. Mr. Moore assured Council that there was no penalty for the late reporting.

Mr. Burke reported that the key areas they focused most of their attention on were the Significant Audit Areas (assets; liabilities; and other items such as cash/investments, capital assets, accounts payable, long term debt, net position, related parties, estimates, legal, etc....) and shared that they conducted a number of tests to verify these numbers.

From a **Single Audit Perspective**, they did a single audit over Federal dollars and State dollars. He explained this was another new auditing standard that was required to be implemented and it used to be referred to as *Circular A133*, but this was replaced this year and was replaced by the Uniform Grant Guidance, which basically changed the criteria that was used to determine which programs were to be audited and changed the threshold of what had to be looked at. It also changed the percent of coverage in

the number of programs that had to be audited in a particular year. He pointed out the one piece that affects the city is it changed the wording in the audit reports away from the *A133* to *Uniform Grant Guidance*.

He mentioned there were two **Federal** programs that were looked at: ***Section 108 Loans; and Assistance to Firefighters***

They also looked at the Powell Bill in the **State programs**, which resulted in the one finding. He noted they looked at a number of things for each of the grants such as the administrative controls, monitoring reports, compliance matrix, compliance testing.

Financial Results in the General Fund Revenues

General Fund Revenues for 2016 were approximately \$101 Million which was almost identical to the prior year. The final budget in the General Fund was roughly \$99.5 Million; actual was a little over \$101 Million which resulted in a positive variance of about \$1.2 Million for this year over what the final budget was. He noted this was driven by the utility sales tax coming in over budget by about \$800,000 and the ABC Board revenue also came in over budget around \$330,000.

From an expense perspective, Mr. Burke noted expenses for 2016 in the General Fund were around \$96 reviewed for the year in the General Fund \$96 Million versus around \$90 Million from the prior year. The final budget for the General Fund was a little over \$102 Million. The actual expenses were \$96 Million with a positive variance of \$6.2 Million. The areas with the biggest difference in as far as being under budget were General Government around \$2.6 Million and Public Services & Transportation which was around \$1.7 Million.

He explained between revenues coming in over and expenses coming in under, the city did not have to sink into the fund balance as much as anticipated. (\$6 million was appropriated in the current year, with only \$700,000 being used).

The **Fund Balance** for the **General Fund** at the end of the year was around \$32 Million and around \$33.6 million the prior year. He pointed out a majority of the restricted \$10.2 million was actually reserved by state statute. Out of the \$6 million, the city had appropriated about \$3.8 million in this current year's budget with the unassigned amount being roughly \$13.4 million at the end of the year. He stated the city has a policy of maintaining at least a 10% unassigned fund balance and the city was in compliance with this at the end of the fiscal year.

Regarding the **Proprietary Funds**, he reported the overall revenues for the year were around \$192 million versus \$194 million. Charges for services did not change that much, but in looking at the individual components, the water/sewer was actually up about \$1.5 Million with the other funds up at about \$2.1 million. He reported that the Electric revenues were actually down \$3.4 million primarily due to consumption in the current year. He noted the intergovernmental revenues went down about \$3 Million due primarily to Mass Transit.

Mr. Burke reported from an expense perspective, the expenses overall from the **Proprietary Funds** were around \$98 million versus \$104 million with the biggest change in power purchased (went from \$103.7 million to \$97.9 million) and this had to do with ElectriCities being purchased by Duke Power.

Council Member Alexander interjected and advised that was an inaccurate statement regarding ElectriCities. He explained that the Eastern Agency actually sold its generational assets, but High Point is actually part of Agency One (NCMPA1). He noted the difference was the refinancing of the long-term debt by ElectriCities and had nothing to do with the purchase or sale.

Council Member J. Davis asked about the \$6 million loss in revenue and asked if this had to do with energy consumption. Council Member Alexander explained there was an overall rate reduction of about 7% and regarding the static sale, he explained the number of electrons were not increasing and this was primarily driven by energy efficiency. He further explained that this is a reflection in the drop of refinancing and the long-term debt.

As far as **Cash Investments**, Mr. Burke reported that the overall cash investments at the end of the year was around \$220 million versus \$236 million. He explained the slide shows at a high level where the money was invested and that the city is taking this portfolio, diversifying it and trying to earn what it can on those funds. Council Member Ewing asked if there was any specific strategy or reason behind the shift from the North Carolina Fund to the US Treasury. Mr. Moore replied that since January/February, there was talk in the market projecting Fed rate hikes, so staff went ahead and tried to reposition the city's portfolio laddering in some maturities and increasing the diversification. He explained one of the benefits of this was that the investment income almost doubled.

From a **Capital Assets** perspective, Mr. Burke noted the capital assets at the end of the year was at \$1.4 million versus \$1.4 million. with the biggest change being additions in CIPs (Capital Improvement Projects) that were going on, infrastructure assets, equipment purchases, etc.... which was offset by depreciation expense this year.

He noted from a long-term debt (**Outstanding Debt**) perspective (Go Bonds, Revenue bonds, notes payable and installment contracts outstanding at the end of the year). At the end of the year, it was roughly \$261 million with the versus \$273 million with about \$5.7 million in this fiscal year of note installment obligations that were new along with the normal pay down of the debt.

In summary, Mr. Burke reported clean opinions with all four reports and noted they did receive full cooperation with staff throughout the year.

Council Member J. Davis expressed appreciation to staff and to Mr. Burke for all the hard work. Mr. Demko added that Mr. Burke and his staff blended well with Mr. Moore and his staff in working with the audit and providing a very thorough report on the internal controls. Council Member J. Davis mentioned the staffing issues in the Finance Department and felt Council should look at getting Mr. Moore some additional help. Mr. Demko agreed and suggested staffing levels would be looked into in the upcoming budget.

Council Member Alexander asked if there was any undesignated fund balance that could be put with the savings found in **street resurfacing** and possibly go back for a second round of contracts. He noted that \$2.2 million was budgeted with a contract being let for \$1.9 million, which resulted in a \$300,000 savings. He asked about the possibility of finding \$750,000 to couple with the \$300,000 for street resurfacing. He noted the reason why we came under was because it was a favorable time to do it. Mr. Demko reiterated that staff would certainly take a look at it.

Preview of the 2017 North Carolina Legislative Session

Fred Baggett distributed a brief outline on the legislative topics that could affect High Point. He pointed out the Legislature will convene on January 11th for the long session (7-8 months) to take up many topics. He mentioned the political structure with a Democratic governor, veto proof House and Senate led by Republicans and the ill-will that was existing pre-election, aside from the partisan nature of the differences between the Legislature and the Governor. He advised that HB2 was still looming and this would also increase the animosity. He believed that if HB2 is repealed that it would still have lingering effects and hoped the cloud would be dispelled and the Furniture Market relieved of it.

Market Funding

Mr. Baggett felt that the Market funding would remain intact for the 2016 short session. He shared that the budget adopted this past year increased Market funding by over \$500,000 from the previous years and there was no reason to expect this to change in 2017-2018. He reiterated that the Market funding seems to be in good shape and pointed out there are great advocates in the General Assembly (Representative Faircloth and Senator Wade) that are strongly supportive of the market funding.

Sales tax Distribution

He reported that this will come under review again and the issue is whether the existing sales tax and distribution method available to counties and cities should be changed in some way to skew it more away from urban areas to rural areas. He advised this is not a new issue, but it continues to be a threat that should be watched as High Point could suffer if a change is made.

Future Transportation Bond

Mr. Baggett noted this was a big one for highways and local roadways. There is a sentiment that it needs to be further studied and possibly 2019 would be a more appropriate time to authorize a big transportation bond. He advised that he would continue to watch this legislation and definitely would support it if it proves to be good for High Point.

Repealed Privilege License Tax (Business Registration Fee)

He mentioned the effort underway by Representative Faircloth to replace for High Point the repealed privilege license tax by instituting a business registration fee. He advised that the bill introduced by Representative Faircloth did not get any traction.

Doughnut Hole Annexations

He mentioned that there may be a statewide bill to authorize the involuntary annexation of doughnut holes. He added that according to Lee Burnette, Planning Director, there are 16-18 such doughnut holes in the City of High Point. These are areas that are not within the Corporate Limits, but are surrounded either completely or almost completely by corporate limits. He shared that this causes several problems: the loss of revenue from the areas that are essentially or for most purposes in the city but do not pay taxes; delivery of services, solid waste collection, emergency response, code compliance, housing codes, and minimum housing do not apply. He added that the League is supporting this legislation and noted it would be a statewide bill. Other cities in the State have expressed interest in having the authority to close doughnut holes. He further explained it would be optional and not mandatory, but if the bill passes, it would give municipalities the authority to do it if they choose to.

Council Member Williams inquired why it would not also include business and why it had to be residential only. Mr. Baggett explained the problems associated with doughnut holes that have arisen in the past have historically involved residential, rather than business. Deputy City Manager Randy McCaslin also added that High Point does not have any that have business as the primary zoning because they need the services, utilities and most are already in. Mr. Baggett advised there would be criteria in place that would have to be met and felt certain that a service report as well as a service requirement would be required to provide services immediately upon annexation. Council Member C. Davis asked if the city would be required to pay for running the utility lines and Mr. Baggett stated that is yet to be determined.

Mandated Redistricting

Council Member Alexander asked what will happen with the redistricting that the courts have now ordered. Mr. Baggett responded this means that the city's 2017 ballot would be shared with legislative races. He explained until the Legislature redraws the 28 districts it is unknown exactly how many districts will actually be affected. According to the existing court order, the Legislature has mandated these districts

have to be redrawn before March 15, 2017; however, this order is currently on Appeal to the US Supreme Court and it was requested it be delayed until 2018 to be implemented. Mr. Baggett pointed out the deadline for redrawing these districts would then be extended until the normal election cycle, but all this is yet to be decided. Council Member C. Davis asked if the city should be concerned regarding its ward lines that were redrawn several years ago and Mr. Baggett replied, no, because they were redrawn in response to the 2010 Census.

Council Member Wagner mentioned that there was some discussion to save money by putting all the local elections to the even numbered years and wanted to know what the status was. Mr. Baggett does not expect that legislation to go anywhere and was unsure of the motive behind why they would have to do that. Mayor Pro Tem Golden asked how many municipalities hold their elections in odd years. It was noted there are currently only about two to three that hold elections in the even numbered years.

Local Government Retirement System

Mr. Baggett stated that some people think that there is a serious unfunded liability problem and this leads to the sentiment among some legislators that the state and the local retirement system should go to a defined contribution instead of a defined plan because this makes future obligations much more certain.

Local Control of Utility Extensions Outside Corporate Limits

He explained that High Point has always relied on voluntary annexation and no utilities are extended without an annexation petition. He advised there was an effort in the 2015 and 2016 session to change this to require cities with utility systems (water/sewer) to extend to customers outside whether the cities wanted to do that or not to serve those people. This was defeated on a statewide basis, but the issue can arise again.

HB2

Mr. Baggett advised that HB2 did cause the Market Authority concern and to some extent has had some effect on participation in the High Point Furniture Market. He explained Governor McCrory would be calling a special session for the Legislature either tomorrow or sometime this week and the leadership of the House and the Senate have said that they intend to look at HB2. It is possible that HB2 will be appealed in its entirety when the Legislature reconvenes. If this happens, it may restrict cities in the future as to their powers in certain areas and Mr. Baggett reminded Council that the State Constitution gives the authority to the Legislature to control municipal powers for every city in the state and they would exercise this power to avoid embarrassment over another HB2.

Receivership of Dilapidated Structures

He pointed out this effort rose out of High Point and it would allow the city to go to Guilford County Superior Court and ask for appointment of a receiver to take control over the effective ownership and control of dilapidated structures in cases where code enforcement has not been successful in getting the structure repaired, renovated, sold or demolished. The receiver would have to have the ability and financial wherewithal to undertake the repair, renovation, construction, disposition of a dilapidated property. A judge would appoint the receiver and the receiver would be charged in detail with what they will do with the property. Mr. Baggett advised this has been done in other states.

Mr. Baggett reported the bill got a limited hearing in the House Appropriations Committee with very little discussion. He noted if High Point is interested in pursuing it again, it can be done, but it would have to be on a statewide basis. He felt certain there would be resistance in the Legislature because of North Carolina being a property rights state.

Council Member C. Davis asked if the receivership program for dilapidated structures would apply to residential or commercial and Mr. Baggett stated it could apply to either.

2017 Legislative Elections

He mentioned the 2017 Elections and the fact that High Point would be sharing their 2017 ballot with local legislators in Guilford County that would be affected by the redistricting.

ABC Privatization

Mr. Baggett advised that he heard there will be renewed effort to do away with the State's regulation of alcohol sales and replace it with private sale of alcohol. He felt the opposition to this would be strenuous with the argument that State controlled liquor sales tend to reduce crime statistics and there would be fewer outlets to purchase it in a State store system versus a private retail establishment. He added that the ABC Board Association is strongly opposed to this and for High Point this means the revenue received from the local ABC system would change to a share of the State tax on liquor. He mentioned that there have been bills introduced before and have always included a cut of the State tax on liquor going back to municipalities. He noted that shared revenues generally go away over time. He advised that the League does not yet have a position on this, but he would work to oppose this unless Council directs otherwise.

ElectriCities

Mr. Baggett stated he was not aware of any legislation that would affect ElectriCities.

Mr. Baggett noted that although he takes direction from the city manager, city attorney and the mayor, he strongly encouraged Council to contact him with any questions/ideas.

NCLM Town Hall Day

Mr. Baggett mentioned the League Town Hall Day is scheduled for March 29th and encouraged involvement and attendance by Council.

The meeting adjourned at 5:22 p.m. upon motion duly made.

Respectfully Submitted,

Maria A. Smith
Deputy City Clerk