

CITY OF NAPLES, FLORIDA

Auditor's Discussion and Analysis Presentation of Financial and Compliance Audit Results September 30, 2019



Presented by:

**Wade P. Sansbury, CPA
Daniel Anderson, CPA**

**MAULDIN
& JENKINS**

CITY OF NAPLES, FLORIDA
AUDITOR'S DISCUSSION AND ANALYSIS
SEPTEMBER 30, 2019

PURPOSE OF THE AUDITOR'S DISCUSSION AND ANALYSIS

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

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MAULDIN & JENKINS – GOVERNMENTAL PRACTICE

General Information:

- Founded in 1918. Approximately 320 personnel. Large regional southeastern firm.
- Offices located in Bradenton, FL; Macon, Atlanta, Albany, Savannah, GA; Birmingham, AL; Columbia, SC; and Chattanooga, TN.



Governmental Sector:

- Serve a significant amount of governmental entities in the Southeast with over 100,000 hours provided 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 125+ 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.
- Joel Black, Governmental Partner, was recently appointed to serve as Chair of the Governmental Accounting Standards Board, effective July 1, 2020.

Engagement Team Leaders for the City Include:

- Wade Sansbury, Engagement Lead Partner: 25 years of experience, 100% governmental
- Daniel Anderson, Engagement Manager: 12 years of experience, 100% governmental
- Meredith Lipson, Quality Assurance Partner: 28 years of experience, 100% gov.

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MAULDIN & JENKINS – ADDITIONAL INFORMATION

Other Industries and 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

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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, 2019.

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.

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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 2018 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 2019 fiscal year CAFR, and is included in the Introductory Section.

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OVERVIEW OF FINANCIAL STATEMENTS

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: governmental funds, proprietary funds, and fiduciary funds.

COMPLIANCE REPORTS

The financial report package contains two compliance reports.

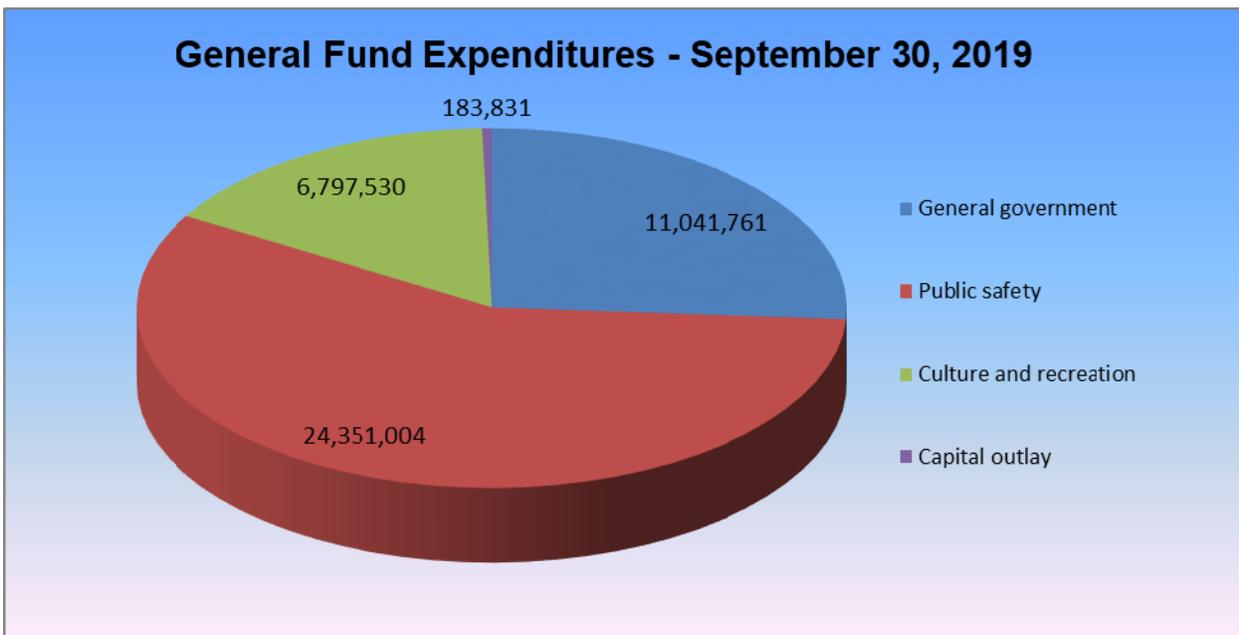
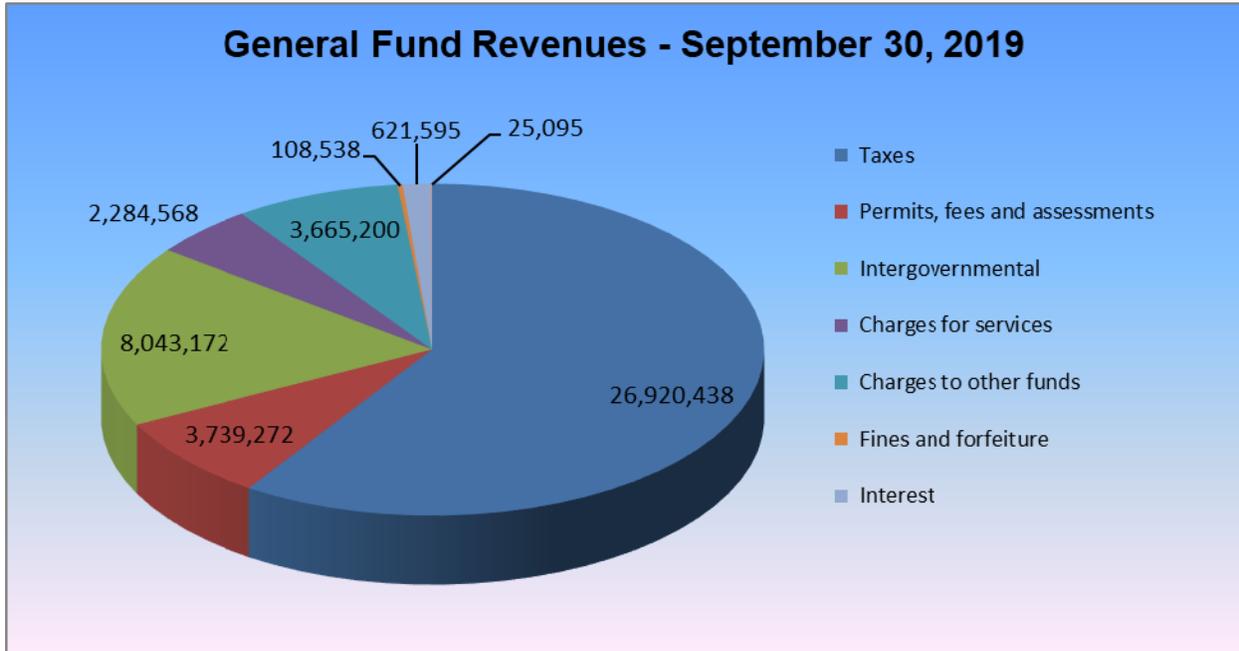
Yellow Book Report: The first compliance report is a report on our tests of the City's internal controls and compliance with laws, regulations, etc. The tests of internal controls were those we determined to be required as a basis for designing our financial statement auditing procedures. Such tests also considered the City's compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. In accordance with the respective standards, 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.

Single Audit Report: The second compliance report is a report on our tests of the City's internal controls and compliance with laws, regulations, etc. relative to certain federal grant programs and the respective expenditures. Our tests were performed on the City's major program (as defined by the relevant federal guidelines), and were not applied to each and every federal grant expended by the City. In accordance with the respective standards, we did provide an unmodified (or positive) opinion on the City's compliance based on our audit. However, we were not required to provide an opinion on the relevant internal controls, but to provide a form of negative assurance on such controls.

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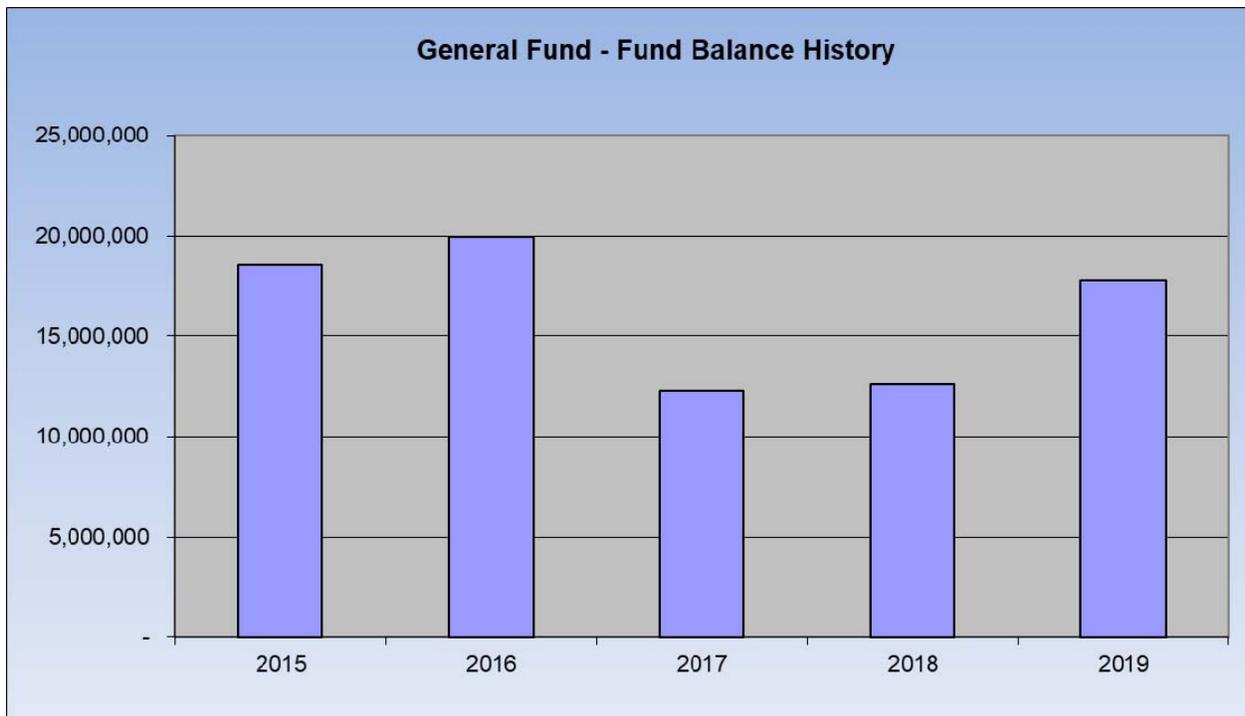
General Fund

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, 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, 2019:



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Total fund balance of the General Fund at September 30, 2019, was a positive \$17,769,061. As discussed in prior years, fund balance does not necessarily equal cash on hand and available to spend. Fund balance is the difference between assets plus deferred outflows and liabilities plus deferred inflows, only a portion of which is cash available to be spent. While the City has cash and investments on hand at September 30, 2019, of \$15,758,774, the City also has approximately \$3.7 million in current liabilities due to outside parties and employees. Additionally, the General Fund incurs expenditures of approximately \$3.53 million per month. A large part of the cash on hand at September 30, 2019, will be needed in subsequent months to fund these and other monthly expenditures, until the City's 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:



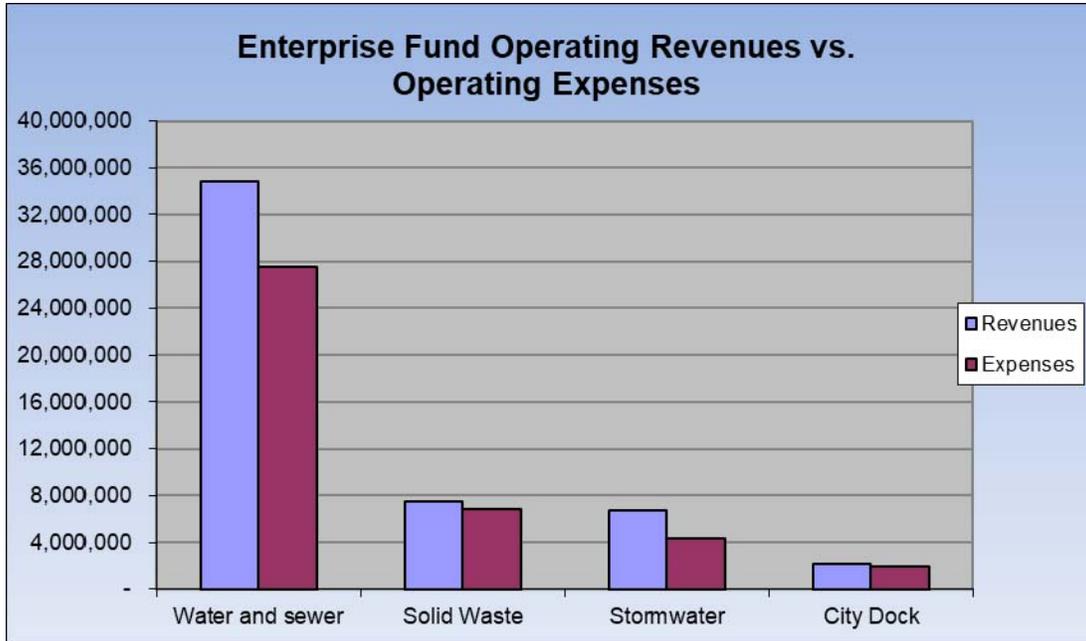
Other Governmental Funds

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. The City also maintains debt service funds which are used to account for the accumulation of resources for, and the payment of, general long term debt principal and interest.

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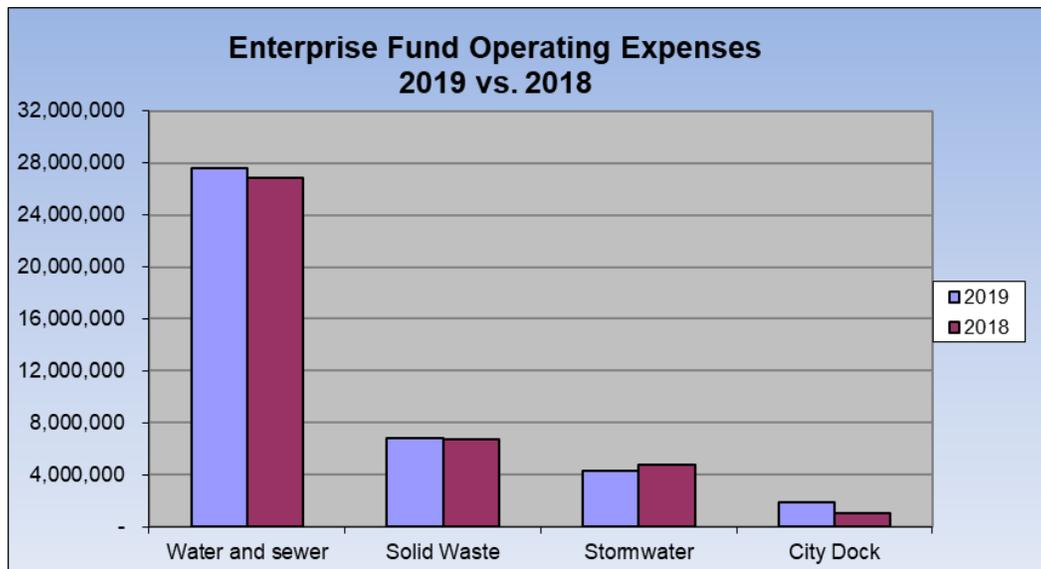
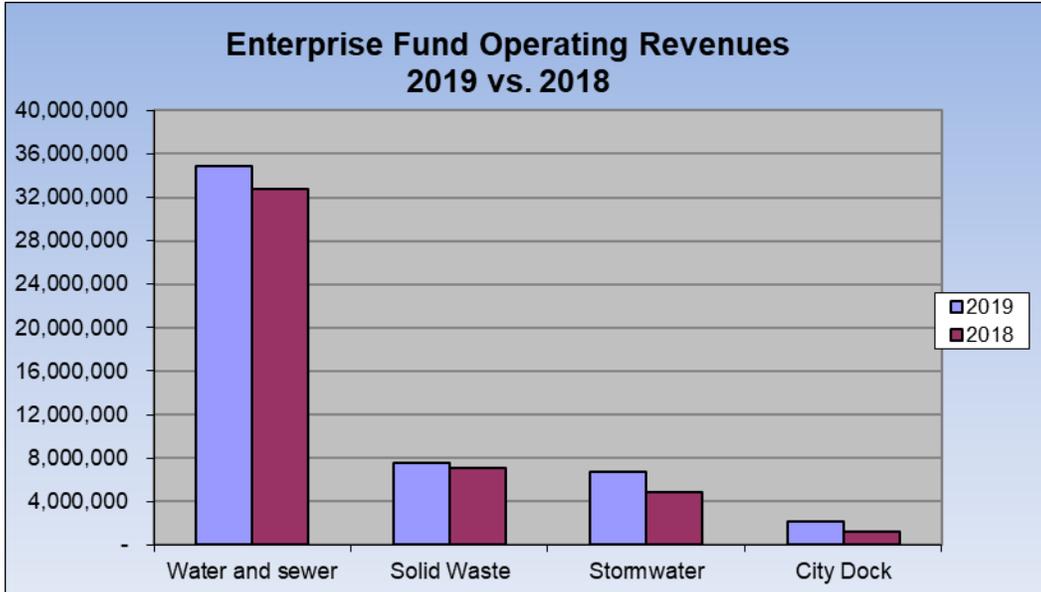
Enterprise Funds

The City maintains various enterprise funds 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 City's Water & Sewer, Solid Waste, Stormwater, and City Dock Funds again generated revenues sufficient to cover the costs of operations for the year ended September 30, 2019.



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As noted within the following two tables, the City's enterprise fund's operating revenues and operating expenditures were very consistent with that of the previous year ending September 30, 2019.



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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 Naples, Florida (the "City") for the year ended September 30, 2019, 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 several 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.

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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 other post-employment benefit plans and pension actuarial reports.

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 were considered as part of 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, 2019, there were significant audit adjustments made to the financial statements of the City. A list of adjustments has been provided to management.

Uncorrected Misstatements

We had no passed adjustments.

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.

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Representations 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. No major issues were discussed with management prior to our retention to perform the aforementioned audit.

Independence

We are independent of the City in accordance with auditing standards promulgated by the American Institute of Certified 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.

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ACCOUNTING RELATED MATTERS

Recommendations for Improvement and Other Matters

During our audit of the financial statements as of and for the year ended September 30, 2019, we noted areas within the accounting and internal control systems that we believe can be improved. Additionally, we noted certain items management should consider as part of its decision making process. Our recommendations are presented in the following paragraphs. We believe consideration of these recommendations will help provide proper control over financial activities, and add effectiveness and efficiency to overall operations.

Findings

2019-001 Cash and Investments

Criteria: To ensure that financial statements properly present the financial position and results of operations of the City in accordance with generally accepted accounting principles (GAAP), in addition to providing meaningful financial reports to City Council and management, the City should ensure that their review process over journal entries includes a final reconciliation to the general ledger subsequent to posting.

Condition: Our audit procedures over investments disclosed that, while the City prepared and posted the adjustment for the change in market value of City investments in the proper amount, the entry was posted as a reduction to City investments, instead of an increase.

Context/Cause: Investment balances for the City were understated at September 30, 2019.

Effect: Material audit adjustments were required to be posted within the reporting units participating in the City's Pooled Investments to ensure the fair presentation of the financial statements.

Recommendation: We recommend the City's review process include a reconciliation of ending balances to the General Ledger subsequent to posting a journal entry to ensure that the accounting records were properly adjusted.

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2019-002 New Revenues Streams

Criteria: To ensure that financial statements properly present the financial position and results of operations of the City in accordance with generally accepted accounting principles (GAAP), in addition to providing meaningful financial reports to City Council and management, the City should ensure that they are reviewing activity in the months surrounding year-end to ensure that a proper cutoff is achieved for all receivable transactions.

Condition: Our testing of the City's new Sales Tax Revenue and new Assessments levied indicated that receivables and related revenues/unearned revenues were understated in the City's Capital Projects Fund, Sales Tax Capital Projects Fund, and Water & Sewer Fund.

Context/Cause: The City's new Sales Tax & Assessment Revenues were understated for the period.

Effect: Material audit adjustments in the amount of \$389,743 (Sales Tax Capital Projects), \$965,434 (Capital Projects) and \$3,810,943 (Water & Sewer) were required to ensure the fair presentation of the financial statements.

Recommendation: We recommend the City's finance department monitor new revenue streams to ensure that they recognize the related transactions properly within the financial records.

2019-003 Solid Waste Fund Capital Assets

Criteria: To ensure that financial statements properly present the financial position and results of operations of the City in accordance with generally accepted accounting principles (GAAP), in addition to providing meaningful financial reports to City Council and management, the City should reconcile the general ledger accounts to subsidiary ledgers and other supporting documentation on a periodic basis. Additionally, reconciliations should be reviewed by management to ensure proper preparation of reconciliations, and that balance sheet accounts are properly supported. The benefit of periodic reconciliations is that errors do not accumulate but can be identified and attributed to a particular period, which makes it easier to perform future reconciliations.

Condition: While testing capital assets, we noted that the City purchased equipment in its Solid Waste Fund, and failed to Capitalize it during the fiscal year. An audit adjustment to increase capital assets and decrease expenses in the amount of \$178,791 was recorded in the Solid Waste Fund to ensure proper financial statement presentation.

Context/Cause: Finance Department oversight caused these accounts to be misstated.

Effect: A material audit adjustment was required to be posted within the Solid Waste for the fair presentation of the financial statements.

Recommendation: We recommend the City evaluate its period closing process to ensure subsidiary ledger reconciliations are being performed timely, properly, and are being reviewed by management.

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Other Matters only Cited within this Annual Audit Agenda

Cyber-Attack

During our preliminary procedures, we noted and discussed with management a cyber-attack against the City that resulted in the loss of approximately \$700,000 during the fiscal year. We noted that the funds affected by the attack may be made whole through a reimbursement from the City's Risk Management Fund, however it is unsure whether insurance will be available to reimburse the Risk Management Fund. The uncertainty of any insurance reimbursement is such that, the financial statements reflect the assumption of no reimbursement. Management has updated its internal controls over the disbursement process to help mitigate the risk against future attacks of a similar nature. We have evaluated internal controls over the City's disbursement process and feel that, while sound controls are in place, the City should constantly be monitoring and updating its internal control structure to ensure sound financial reporting is provided to management and governance so that prevention of such losses is ensured. We recommend the City ensure adequate training is also involved so that all employees are well versed in these controls and preventative measures. Additionally, we recommend the City consider obtaining independent third party testing and verification of controls surrounding the City's cyber security and information technology.

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. A functioning Cybersecurity Risk Management Program 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 City continue to investigate, develop 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.

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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, 2019, 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.

Looking Forward: New Governmental Accounting Standard Board (GASB) Standards and 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. 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.

- b. **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.

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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.

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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.

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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.

- c. **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.

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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.

d. **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 was early implemented as part of fiscal year 2019.

e. **Statement No. 90, *Major Equity Interests*** was issued in August 2018, and is effective for the first reporting period beginning after December 15, 2018 (meaning September 30, 2020). Under this standard, an equity interest is: (a) a financial interest in a legally separate organization by the ownership shares of the organization's stock; or (b) by otherwise having an explicit, measurable right to the net resources of the organization that is usually based on an investment of financial or capital resources by a government. An equity interest is explicit and measurable if: (a) the government has a present or future claim to the net resources of the entity, and (b) the method for measuring the government's share of the entity's net resources is determinable.

If the interest is deemed to be an investment under GASB No. 72, paragraph 64, then the interest should be reported as an investment and measured using the equity method. If the interest is held by a special-purpose government engaged in fiduciary activities, a fiduciary fund, or an endowment or permanent fund, then the amount should be measured at fair value. If interest is 100% of entity, then it is a component unit. We do not expect this new standard to have a significant effect on the City.

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- f. **Statement No. 91, *Conduit Debt Obligations*** was issued in May 2019, and is effective for the first reporting period beginning after December 15, 2020 (meaning September 30, 2022).

The primary objectives of this statement are to provide a single method of reporting conduit debt obligations by issuers and eliminate diversity in practice associated with: (1) commitments extended by issuers, (2) arrangements associated with conduit debt obligations, and (3) related note disclosures. This statement achieves those objectives by clarifying the existing definition of a conduit debt obligation; establishing that a conduit debt obligation is not a liability of the issuer; establishing standards for accounting and financial reporting of additional commitments and voluntary commitments extended by issuers and arrangements associated with conduit debt obligations; and improving required note disclosures.

A conduit debt obligation is defined as a debt instrument meeting **all** of the following characteristics:

- There are at least three parties involved: (1) an issuer, (2) a third-party obligor, and (3) a debt holder (or a debt trustee);
- The issuer and the third-party obligor are not within the same financial reporting entity;
- The debt obligation is not a parity bond of the issuer, nor is it cross-collateralized with other debt of the issuer;
- The third-party obligor (or its agent), not the issuer, ultimately receives the proceeds from the debt issuance;
- The third-party obligor, not the issuer, is primarily obligated for the payment of all amounts associated with the debt obligation (debt service payments).

All conduit debt obligations involve the issuer making a limited commitment. Some issuers extend additional commitments or voluntary commitments to support debt service in the event the third party is, or will be, unable to do so.

An issuer should not recognize a conduit debt obligation as a liability. However, an issuer should recognize a liability associated with an additional commitment or a voluntary commitment to support debt service if certain recognition criteria are met. As long as a conduit debt obligation is outstanding, an issuer that has made an additional commitment should evaluate at least annually whether those criteria are met. An issuer that has made only a limited commitment should evaluate whether those criteria are met when an event occurs that causes the issuer to reevaluate its willingness or ability to support the obligor's debt service through a voluntary commitment.

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This statement also addresses arrangements – often characterized as leases – that are associated with conduit debt obligations. In those arrangements, capital assets are constructed or acquired with the proceeds of a conduit debt obligation and used by third-party obligors in the course of their activities. Payments from third-party obligors are intended to cover and coincide with debt service payments. During those arrangements, issuers retain the titles to the capital assets. Those titles may or may not pass to the obligors at the end of the arrangements.

Issuers should not report those arrangements as leases, nor should they recognize a liability for the related conduit debt obligations or a receivable for the payments related to those arrangements. In addition, the following provisions apply:

- If the title passes to the third-party obligor at the end of the arrangement, an issuer should **not** recognize a capital asset.
- If the title does not pass to the third-party obligor and the third party has exclusive use of the entire capital asset during the arrangement, the issuer should **not** recognize a capital asset until the arrangement ends.
- If the title does not pass to the third-party obligor and the third-party has exclusive use of only portions of the capital asset during the arrangement, the issuer should recognize the entire capital asset and a deferred inflow of resources at the inception of the arrangement. The deferred inflow of resources should be reduced, and an inflow recognized, in a systematic and rational manner over the term of the arrangement.

This statement requires issuers to disclose general information about their conduit debt obligations, organized by type of commitment, including the aggregate outstanding principal amount of the issuers' conduit debt obligations and a description of each type of commitment. Issuers that recognize liabilities related to supporting the debt service of conduit debt obligations also should disclose information about the amount recognized and how the liabilities changed during the reporting period.

- g. Statement No. 92, *Omnibus 2020*** was issued in January 2020, and is effective for the first reporting period beginning after June 15, 2020 (meaning September 30, 2021).

The primary objectives are to enhance comparability in accounting and financial reporting and to improve the consistency of authoritative literature by addressing practice issues that have been identified during implementation and application of certain GASB Statements. This Statement addresses a variety of topics and includes specific provisions about the following:

- The effective date of Statement No. 87, Leases, and Implementation Guide No. 2019-3, Leases, for interim financial reports.

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- Reporting of intra-entity transfers of assets between a primary government employer and a component unit defined benefit pension plan or defined benefit other post-employment benefit (OPEB) plan.
 - The applicability of Statements No. 73, Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68, as amended, and No. 74, Financial Reporting for Post-employment Benefit Plans Other Than Pension Plans, as amended, to reporting assets accumulated for post-employment benefits.
 - The applicability of certain requirements of Statement No. 84, Fiduciary Activities, to post-employment benefit arrangements.
 - Measurement of liabilities (and assets, if any) related to asset retirement obligations (AROs) in a government acquisition.
 - Reporting by public entity risk pools for amounts that are recoverable from reinsurers or excess insurers.
 - Reference to nonrecurring fair value measurements of assets or liabilities in authoritative literature.
 - Terminology used to refer to derivative instruments. .
- h. 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 2019 with a final standard expected in early 2022.
 - **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 things 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. Final standard is expected in 2021.
 - **Revenue and Expense Recognition** is another long-term project where the GASB is working to develop a comprehensive application model for recognition of revenues and expenses from non-exchange, exchange, and exchange-like transactions. The final standard is expected in 2023.

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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 the City staff and officials can participate in this opportunity, and that it will be beneficial to them. 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 and the Revenue Cycle
18. Internal Revenue Service (IRS) Issues, Primarily Payroll Matters
19. Legal Considerations for Debt Issuances and 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.

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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

If you have any questions regarding any comments, suggestions or recommendations set forth in this discussion, 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 Naples, Florida and look forward to serving you in the future. Thank you.