

November 29, 2007

Honorable Mayor and Members of  
the Hermosa Beach City Council

City Council Meeting of  
December 11, 2007

**2006-07 COMPREHENSIVE ANNUAL FINANCIAL REPORT (CAFR)  
(Including Report from Independent Auditor)**

**RECOMMENDATION**

It is recommended that the City Council:

Receive and file the 2006-07 Comprehensive Annual Financial Report (CAFR), which includes the report from Caporicci and Larson, our independent auditors.

**BACKGROUND**

Annually the City has a financial audit performed by an independent, certified public accounting firm. The auditor's report is located behind the second divider that is labeled "Financial Section".

For the second year, we have met our goal of presenting this report to you in December, which is 1 month earlier than in the past. Staff believes this is the earliest date possible for us to present the report.

For 2006-07, the City again received an unqualified opinion, which indicates that the auditor believes the financial statements present a fair picture of the financial position of the City, as opposed to a qualified opinion, in which the auditor "qualifies" or limits his opinion for specific reasons, such as lack of capital asset accounting, significant internal control deficiencies or non-compliance with other Government Accounting Standards Board (GASB) requirements.

The report will again be submitted to the Government Finance Officers Association (GFOA) to qualify for the Certificate of Achievement for Excellence in Financial Reporting for the seventeenth time. The award program requires a high level of compliance with governmental standards, inclusion of information well beyond the general-purpose financial statements and an unqualified audit opinion.

**ANALYSIS**

As a reminder, the new reporting model (GASB 34) that was implemented five years ago:

- presents financial information in new formats, namely, the Government Wide Financial Statements, beginning on page 17. These are designed to show net assets and equity of the City as a whole, provide information on the cost of services and show how programs are financed.
- requires a new section, Management's Discussion and Analysis (MD &A) to present financial highlights and assess performance for the year.
- requires reporting on "major" funds rather than aggregate fund types.
- requires accrual accounting for all governmental funds, meaning that long term assets and liabilities (such as capital assets, including infrastructure) are included in addition to short term assets and liabilities. All revenues and all costs of providing services are also reported, not just those received or paid in or soon after year-end.

Additional information and analysis can be found in the Transmittal Letter starting on page v and in the Management Discussion and Analysis (MD & A) starting on page 3. General Fund information is found on page 10. **Some of the comments are repeated herein for the purpose of having this staff report stand alone. Since comparative information for the General Fund for 2005-06 and 2006-07 is not included in the CAFR, it is presented below.**

### General Fund Revenue

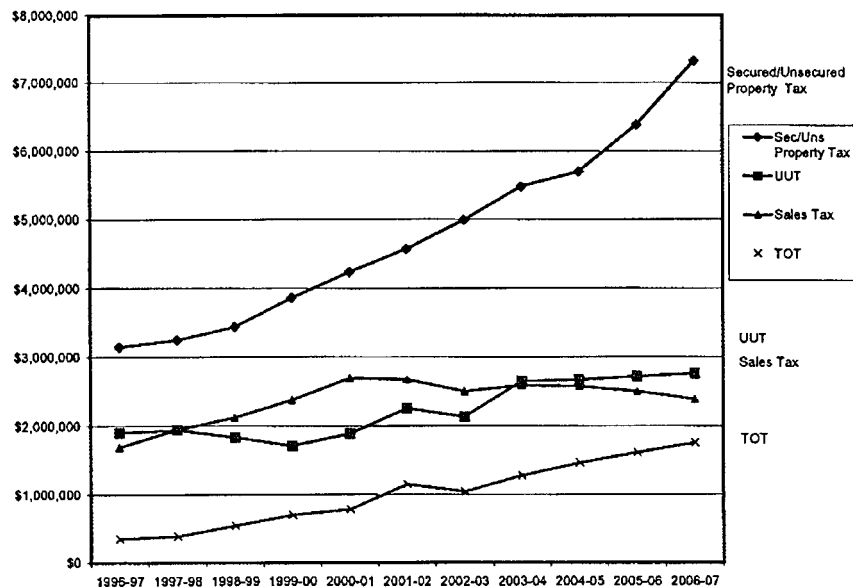
General Fund revenue increased 5% over 2005-06 and was 1% over budget estimates.

REVENUE SOURCE	Revenue FY 06-07 Amount	Increase (Decrease) Over FY 05-06	% Of Increase (Decrease)	% Of Total
Property Taxes	\$9,383,544	\$1,021,656	12.22	36.85
Sales Tax	2,395,390	(115,614)	(4.60)	9.41
Utility User Tax	2,769,113	43,028	1.58	10.87
Transient Occupancy Tax	1,769,015	140,621	8.64	6.95
Other Taxes	1,876,406	44,244	2.41	7.37
Licenses & Permits	772,832	(95,253)	(10.97)	3.04
Fines & Forfeitures	1,596,025	7,210	.45	6.27
Use of Money and Property	356,966	44,718	14.32	1.40
Intergovernmental Revenue	259,922	(300,011)	(53.58)	1.02
Charges for Services	4,016,375	250,480	6.65	15.77
Miscellaneous	145,833	74,515	104.48	0.57
Interest	122,533	4,803	4.08	0.48
<b>Total</b>	<b>\$25,463,954</b>	<b>\$1,120,397</b>	<b>4.60%</b>	<b>100.00%</b>

### Taxes

Revenue from taxes generates 71% of General Fund revenue. The graph below tracks the four largest revenue sources over the past ten years.

**General Fund – Largest Revenue Sources**



Total property tax revenue increased 12%. The graph above shows secured and unsecured tax only, which increased 13% and decreased 1%, respectively. With a median home price in June of \$1,205,000 compared to Los Angeles County's median price of \$550,000 and the high rate of turnover, the increase in the property tax is no surprise. With the subprime mortgage debacle that is occurring nationwide, some slowing in sales and decline in the value of homes is to be expected.

Sales Tax revenue is 5% down from 2005-06 and 11% down from the highest year of 2000-01. Eating and Drinking Places is the #1 revenue-generating category. At least three large pieces of property are possibly in play that may have sales tax or transient occupancy tax potential. Depending on the outcome, changes in these properties could have a positive longer-term financial impact on our revenue.

**Sales Tax By Class\***

**Top Ten Categories**

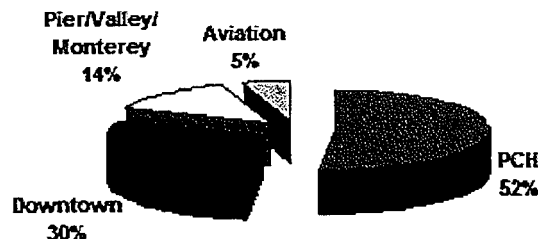
RANK/BUSINESS CLASS	Sales Tax 2006-07	Increase/ (Decrease)	% of Change Prev. Yr.	% of Total
1. Eating/Drinking Places	\$743,046	\$45,287	6.49	34.63
2. Other Retail	283,392	(705)	(0.25)	13.21
3. Auto Dealers and Supplies	257,201	(82,448)	(24.27)	11.99
4. Building Materials	216,730	3,750	1.76	10.10
5. Food Stores	208,327	3,005	1.46	9.71
6. Service Stations	#	#	16.81	#
7. Business, Service & Repair	113,023	(980)	(0.86)	5.27
8. Drug Stores	#	#	36.52	#
9. Furniture/Appliance	65,093	2,783	4.47	3.03
10. Apparel Stores	40,707	(2,062)	(4.82)	1.90

\* Threshold for inclusion, \$300 per quarter

# Information omitted if fewer than four businesses in the category per State Board of Equalization

**Sales Tax by Geographic Area**

LOCATION	Revenue 2005-06	% of Total	% Chg	Revenue 2006-07	% of Total
PCH	1,040,759	53%	(2)%	1,020,093	52%
Downtown	561,619	29%	4 %	585,720	30%
Pier/Valley/Monterey	263,314	13%	6 %	279,010	14%
Aviation	93,621	5%	(3)%	90,996	5%



Utility user tax revenue grew by 2%. Passage of Measure H to update our ordinance ensures that this important revenue source will continue.

Transient occupancy tax increased 9% with overall hotel occupancy at 76%.

The License and Permit category declined 11% due to a decrease in building permit revenue. The number of residential building permits issued decreased by 25%.

Use of Money and Property increased due to more special event revenue received for two Association of Volleyball Professionals (AVP) events held September 2006 and May 2007.

Intergovernmental Revenue decreased because of a one-time repayment of vehicle license fee revenue from the State in 2005-06.

Charges for Services increased consistent with the cost of living formula applied per the master fee resolution.

The Miscellaneous category increased for a variety of reasons. Some of the most significant reasons were an increase in donations of almost \$40,000, a one-time acceptance fee for the Verizon franchise and additional restitution from the fraudulent fire extinguisher court case.

**General Fund Expenditures**

General Fund expenditures increased 9% from 2005-06 and were 3% under budget.

GENERAL FUND	Expenditures FY 06-07 Amount	Increase (Decrease) Over FY 05-06	% Of Increase (Decrease)	% Of Total
Legislative & Legal	\$858,017	(\$105,014)	(10.90)	3.52
General Government	2,223,589	107,408	5.08	9.12
Public Safety	16,005,983	1,819,058	12.82	65.65
Community Development	1,398,378	70,989	5.35	5.74
Culture & Recreation	1,168,342	62,798	5.68	4.79
Public Works	2,680,646	140,250	5.52	10.99
Capital Outlay	46,977	(32,621)	(40.98)	0.19
<b>Total</b>	<b>\$24,381,932</b>	<b>\$2,062,868</b>	<b>9.24%</b>	<b>100.00%</b>

Negotiated salary and benefit increases for changes to employee bargaining units affect all categories. The City is also making the annual required contribution for all employee groups for post employment health benefits, as we do for retirement benefits, which affects all categories.

The Legislative/Legal category decreased primarily because there was no election expense and because legal costs were less than 2005-06. (The MacPherson Oil legal fees are in the Insurance Fund so are not included here).

A portion of the Public Safety cost increase was the result of previously vacant positions that were filled during 2006-07. Dispatch services also increased for the fiscal year.

## General Fund Unspent Funds

The policy of transferring unspent funds in the General Fund to the Insurance Fund, Equipment Replacement Fund (ERF) and Compensated Absences Fund was implemented in 1995-96 to build equity and provide funds for amounts owed to employees for accumulated leave. The policy was changed in 1998-99 to discontinue allocating funds to the Compensated Absences Fund (since the target amount was reached) and create a Capital Improvement Fund for street and other capital improvements.

The City Council amends the policy, as necessary, when goals or targets are met. For 2006-07, \$1,110,659 was transferred to the Contingency Fund, Insurance Fund, Equipment Replacement Fund and Capital Improvement Fund (\$277,665 each fund).

The next opportunity to review our financial picture will be Midyear Budget Review on February 12, 2008, at which time we will review progress on the financial goals and make any adjustments or transfers, as necessary.

Gary Caporicci, the partner in charge of our audit, will be available at the meeting for comments or questions.

*If you have particular questions about details in the reports, we would appreciate knowing them in advance so we can give you a complete answer.*

CONCUR:

  
\_\_\_\_\_  
Stephen R. Burrell,  
City Manager

  
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Viki Copeland,  
Finance Director

The reports are available for review in the library and the Finance Department.