

January 20, 2011

Honorable Mayor and Members of
the Hermosa Beach City Council

City Council Meeting of
January 25, 2011

**2009-10 COMPREHENSIVE ANNUAL FINANCIAL REPORT (CAFR)
(Including Report from Independent Auditor)**

RECOMMENDATION

It is recommended that the City Council:

1. Receive and file the 2009-10 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".

Our Independent Auditors, Caporicci and Larson, CPAs, have gone through two mergers this year, the latest with Marcum LLP. With the changes in the firm's staff, processes and quality review procedures, they requested additional time to complete the audit. They issued the report to us within the 30-day extension window, however it is later than we typically present the report. The good news is, that with change, we had two sets of auditors looking at our records this year, which is a plus for us.

For 2009-10, 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. The City has received the award since 1990. 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 eight years ago:

- presents financial information in new formats, namely, the Government Wide Financial Statements, beginning on page 19. 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 12. **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 2008-09 and 2009-10 is not included in the CAFR, it is presented below.**

General Fund Revenue

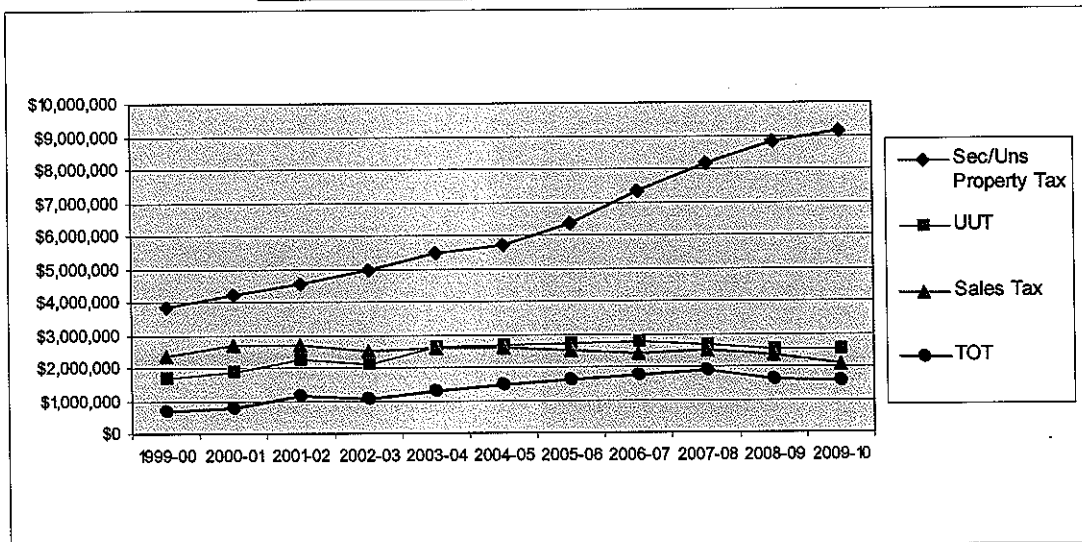
General Fund revenue decreased 1.06% over 2008-09 and was 2% over budget estimates.

REVENUE SOURCE	Revenue FY 09-10 Amount	Increase (Decrease) Over FY 08-09	% Of Increase (Decrease)	% Of Total
Property Taxes	\$11,407,964	\$219,587	1.96	42.42
Sales Taxes	2,112,971	(277,687)	(11.62)	7.85
Utility User Tax	2,559,369	(15,840)	(.62)	9.52
Transient Occupancy Tax	1,559,048	(86,523)	(5.26)	5.80
Other Taxes	1,844,559	(4,000)	(.22)	6.86
Licenses & Permits	556,737	(121,740)	(17.94)	2.07
Fines & Forfeitures	2,040,336	(34,902)	(1.68)	7.59
Use of Money and Property	309,946	6,631	2.19	1.15
Intergovernmental Revenue	164,496	(7,059)	(4.11)	.61
Charges for Services	3,998,342	(9,016)	(.22)	14.87
Miscellaneous	314,113	57,196	22.26	1.17
Interest	16,033	(13,439)	(45.60)	.06
Total	\$26,883,914	(\$286,792)	(1.06)%	100.00%

Taxes

Revenue from taxes generates 72% of General Fund revenue. The graph below tracks the four largest revenue sources over the past eleven years.

General Fund – Largest Revenue Sources



Total property tax revenue increased 2%. The graph above shows secured and unsecured tax only, which increased 4% and 5%, respectively. Hermosa Beach had the fifteenth highest assessed valuation out of 88 cities in Los Angeles even though the growth of .3% in assessed valuation is the lowest since 1999 at 5.25%. Lower values and sales prices are to be expected in the current economic environment. Median home prices in Hermosa Beach for June 2010 were \$900,000 as compared to Los Angeles County's median price of \$336,000. The continuation of lower growth has been anticipated in the 2010-11 budget.

Sales Tax revenue is 12% down from 2008-09 and 28% down from the highest year of 2000-01. Eating and Drinking Places, the #1 revenue-generating category, declined by 6%. Virtually every category declined, with the greatest decreases in the Auto, Other Retail, and Furniture/Appliance categories.

Sales Tax By Class*

Top Ten Categories

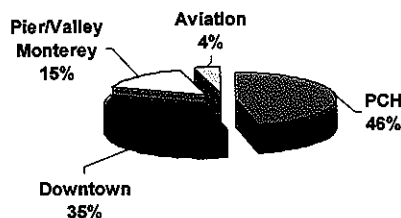
RANK/BUSINESS CLASS	Sales Tax 2009-10	Increase/ (Decrease)	% of Change Prev. Yr.	% of Total
1. Eating /Drinking Places	\$783,021	(\$53,235)	(6.37)	41.82
2. Other Retail	268,079	(81,379)	(23.29)	14.32
3. Food Stores	180,089	(8,379)	(4.45)	9.62
4. Auto Dealers and Supplies	153,067	(61,239)	(28.58)	8.18
5. Service Stations	#	#	(10.19)	#
6. Building Materials	115,897	(46,001)	(28.41)	6.19
7. Business, Service & Repair	74,245	(3,193)	(4.12)	3.97
8. Drug Stores	#	#	(6.45)	#
9. Furniture/Appliance	50,807	(14,640)	(22.37)	2.71
10. Apparel Stores	45,892	(3,982)	(7.98)	2.45

* 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 2008-09	% of Total	% Chg	Revenue 2009-10	% of Total
PCH	900,720	48%	(-16)%	759,497	46%
Downtown	603,007	32%	(-6)%	566,302	35%
Pier/Valley/Monterey	273,247	15%	(-10)%	244,677	15%
Aviation	83,669	5%	(-17)%	69,579	4%



Transient occupancy tax decreased 5% with overall hotel occupancy at 66%, compared to 68% last year.

The License and Permit category decreased 18%. Building Permit revenue alone decreased by 36%. The number of residential building permits issued decreased by 9%.

Intergovernmental Revenue decreased because 2009-10 Police Officer Standards Training (POST) revenue was less and there was a continued decline in In lieu Motor Vehicle Revenue.

The Miscellaneous category increased primarily because of a one-time restitution payment that was received in 2009-10.

General Fund Expenditures

General Fund expenditures decreased 2% from 2008-09 and were 1% under budget.

GENERAL FUND	Expenditures FY 09-10 Amount	Increase (Decrease) Over FY 08-09	% Of Increase (Decrease)	% Of Total
Legislative & Legal	\$976,862	(\$80,230)	(7.59)	3.83
General Government	2,205,661	(141,047)	(6.01)	8.65
Public Safety	17,065,312	168,975	1.00	66.94
Community Development	1,198,904	(176,329)	(12.82)	4.70
Culture & Recreation	1,170,057	(151,859)	(11.49)	4.59
Public Works	2,871,141	(121,224)	(4.05)	11.26
Capital Outlay	4,237	(100,763)	(95.96)	0.02
Total	\$25,492,174	(\$602,477)	(2.31)%	100.00%

The Legislative/Legal category decreased primarily due to a one-time contribution to the Hermosa Beach School District in 2008-09 and decreased City Attorney costs for the MacPherson Oil Lawsuit.

General Government costs decreased due to lower personnel legal costs and less Affordable Housing Funds given to Marineland Mobile Home Park Association for the purchase of the mobile home park. The Personnel Director position and one Account Clerk in the Finance Cashier division were also unfilled during 2009-10.

Public Safety costs increased primarily due to the reinstatement and settlement costs for two safety employees and increases in insurance user charges for 2009-10. This category also had a total of six vacancies during the year (five Police Officers and the Assistant Fire Chief position).

Community Development costs decreased primarily because there were fewer costs for plan check services due to a decline in building activity and three vacancies remained unfilled during the year (a Senior Building Inspector, an Office Assistant and a Planning Associate).

Culture and Recreation decreased because of a decrease in recreation class instructor payments because of ongoing construction at the facility, fewer excursions and vacancies in the Community Resources Director and Recreation Supervisor positions.

The Public Works category decreased due to lower costs for landscape and street maintenance and a one-time software upgrade to the Geographic Information System (GIS) in 2008-09. The Public Works Inspector position also remained unfilled at year end.

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 and depending on where funds are needed. For 2009-10, \$1,227,569 was transferred to the Insurance Fund to cover estimated claims liabilities and legal expenses related to the MacPherson Oil case. Funds were available in the General Fund at year end primarily due to the unfilled positions that were mentioned above.

Insurance Fund

Since the CAFR contains no real discussion of Insurance Fund activity because Internal Service Funds are allocated across all activities, the chart below shows the change in claims expense for Workers Compensation and Liability. Claims payments for both liability and workers compensation are lower in 2009-10. Although the year end liability for workers compensation increased, there was an overall reduction in liability for General Liability. As seen in the chart, total claims expense for 2009-10 declined by \$209,533.

Changes to Claims Expense

DEPARTMENT/DIVISION	2008-09	2009-10	Increase (Decrease)
Workers Compensation Division			
Change to:			
Claims Paid	\$800,614	\$744,211	(\$56,403)
Year-end Liability	120,821	485,408	364,587
	<u>921,435</u>	<u>1,229,619</u>	<u>308,184</u>
Liability Division			
Change to:			
Claims Paid	740,022	164,427	(575,595)
Year-end Liability	(240,720)	(182,842)	57,878
	<u>499,302</u>	<u>(18,415)</u>	<u>(517,717)</u>
Total Claims Expense	<u>\$1,420,737</u>	<u>\$1,211,204</u>	<u>(\$209,533)</u>

Next Financial Review

The next opportunity to review our financial picture will be Midyear Budget Review on February 8, 2011, at which time we will review progress on the financial goals and make any adjustments or transfers, as necessary.

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

CONCUR:



Stephen R. Burrell,
City Manager



Viki Copeland,
Finance Director

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