



TOWN OF LOS GATOS
TOWN COUNCIL FINANCE COMMITTEE
AGENDA

Finance Committee – 2009

*Mike Wasserman, Mayor
Barbara Spector, Council Member*

TOWN COUNCIL CHAMBERS
110 EAST MAIN STREET
FEBRUARY 24, 2009 – 3:30 P.M.

VERBAL COMMUNICATIONS *(Three minute time limit)*

1. Discuss and accept Comprehensive Annual Financial Report (CAFR) for the Fiscal Year ended June 30, 2008 (including Independent Auditor's Report)
2. Discuss and accept Auditor Management Letter

ADJOURNMENT

cc: Post *(also post on Town Web)*
Town Council



MEMORANDUM

OFFICE OF THE TOWN MANAGER

To: Council Finance Committee
Barbara Spector
Mike Wasserman

From: Greg Larson, Town Manager

By: Stephen Conway, Director of Finance & Administrative Services

Subject: Finance Committee Meeting to Review the Town's FY 2007/2008 Financial Statements and the Auditor's Report to Management and Town Council

Date: February 20, 2009

Attached is the Town's Comprehensive Annual Financial Report (CAFR) for FY 2007/08, including the Independent Auditor's Report in preparation for the Council Finance Committee's February 24 meeting. Staff will provide a detailed overview of the report and an update of the implementation status of the recommendations made by the auditors in their Report to Management. After review of the reports, the Committee may recommend the report's acceptance by the Town Council at its March 16, 2009 Council meeting.

Staff believes the report continues to meet the criteria necessary to receive both the Government Finance Officer's Association and the California Society of Municipal Finance Officers awards for Excellence in Financial Reporting. The Comprehensive Annual Financial Report (CAFR) is considered by the Governmental Accounting Standards Board (GASB) to be the "official annual report" of the Town.

The Comprehensive Annual Financial Report contains three basic sections. The first is the Introductory Section, which provides general information on the Town's financial position, including management's discussion and analysis of the fiscal years financial highlights. The Financial Section provides information on both fund types and individual funds and account groups. The final Statistical Section provides a broad range of trend data covering key financial indicators from the past ten fiscal years and demographic and miscellaneous data used to assess a municipality's financial situation.

New requirements for financial reporting and government auditing are imposed each year. The Town has complied with implementing Governmental Accounting Standards Board Statement 34 (GASBS), which required changes in the financial reporting model. The Town also implemented GASB 44 to include more financial and economic trending information in the Statistical Section of the report. Work on GASBS 45 relating to enhanced disclosure on future liabilities for post retirement benefits is required to be implemented this fiscal year ending June 30, 2009.

Page 2

Town Council

Subject: Finance Committee Meeting to Review the Town's FY 2007/2008 Financial
Statements and the Auditor's Report to Management and Town Council
February 20, 2009

As mentioned, included in the CAFR is the Independent Auditor's Report reflecting the examination of the Town's financial statements by C.G. Uhlenberg & Company. They have found the Town's financial statements to be in conformance with generally accepted accounting principles (GAAP), presenting fairly in all material respects, the financial position of the Town as of June 30, 2008, the results of its operations, and the cash flows of its proprietary fund types.

Should you have any questions about the CAFR or Independent Auditor's Report, please contact Steve Conway, Finance Director at (408) 354-6828.

SC:pg

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Attachments

**TOWN OF LOS GATOS
CALIFORNIA**

**REPORT TO MANAGEMENT
AND TOWN COUNCIL**

**FOR THE FISCAL YEAR
ENDED JUNE 30, 2008**

Submitted by:



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Contact: Jeffrey J. Ira

February 19, 2009

TOWN OF LOS GATOS

**REPORT TO MANAGEMENT AND TOWN CONCIL
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

TABLE OF CONTENTS

TITLE	PAGE
Transmittal Letter	1 - 2
Current Year Control Deficiencies	3
Prior Year Control Deficiencies	4
Required Communication to the Council (SAS 114)	5 - 7



C. G. UHLENBERG LLP
CERTIFIED PUBLIC ACCOUNTANTS & CONSULTANTS

PEGGY H. CHEN, C.P.A. JEFFREY J. IRA, C.P.A. KATHERINE CHAO, C.P.A. JULIE T. LIN, C.P.A.

February 19, 2009

The Honorable Mayor and Members of the Town Council
Town of Los Gatos, California

We have audited the basic financial statements of the Town of Los Gatos California (the "Town"), as of and for the year ended June 30, 2008, and have issued our reports thereon dated January 15, 2009.

In planning and performing our audit of the financial statements of the Town of Los Gatos as of and for the year ended June 30, 2008, in accordance with auditing standards generally accepted in the United States of America, we considered the Town's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Governmental Unit's internal control. Accordingly, we do not express an opinion on the effectiveness of the Governmental Unit's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. Control deficiencies in internal control indentified in the audit are discussed on page 3 of this report.

A significant deficiency is a control deficiency, or a combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or a combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control. We did not identify any deficiencies in internal control that we consider to be material weakness as defined above.

Our comments contained herein are based solely on observations made during our audit of the Town's 2007-2008 basic financial statements and, accordingly, are not based on the results of any special studies designed to report on these matters. Accordingly, additional information and study may be required before acting on our suggestions.



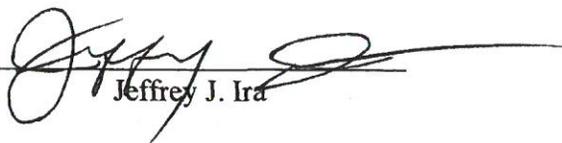
This letter is intended solely for the information and use of management, the Mayor, and Town Council and should not be used for any other purpose. However, this restriction is not intended to limit the distribution of this letter, which is a matter of public record.

We would be pleased to discuss these matters in greater detail at your convenience.

Very truly yours,

C. G. UHLENBERG LLP

By


Jeffrey J. Ira

JJI/sc

**CURRENT YEAR
CONTROL DEFICIENCIES**

TOWN OF LOS GATOS

**REPORT TO MANAGEMENT AND TOWN COUNCIL
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

CURRENT YEAR CONTROL DEFICIENCIES

Deficiency 08-01: Repeat Recommendation - Pursuant to Health and Safety Code Section 33334.12(g), "excess surplus" means any unexpended and unencumbered amount in an agency's Low and Moderate Income Housing Fund that exceeds the greater of: one million dollars (\$1,000,000), or the aggregate amount of tax increment deposited into the Low and Moderate Income Housing Fund during the agency's preceding four fiscal years (pursuant to Sections 33334.2 and 33334.6). It was determined that the Agency retained an excess surplus of approximately \$1,795,145 and \$1,037,474 for the fiscal years ended June 30, 2008 and 2007, respectively, based on the aggregate amount of tax increment deposited in the Low and Moderate Income Housing Fund.

Recommendation - Pursuant to Health and Safety Code Section 33334.12(a)(1)(B), we recommend that the Agency encumber the excess surplus within two years. The funds should be encumbered to carry out activities consistent with a redevelopment agency as defined in Health and Safety Code Sections 33334.2 and 33334.3. The excess surplus has been increasing since 2006, the Town should review and identify how much of the excess surplus needs to be encumbered by the end of 2009 versus 2010. Since the Agency's Low-Mod fund had an increase in fund balance of \$1.784 million for the fiscal year ended June 30, 2008, only a portion of the excess surplus since 2006 may still be unencumbered.

**PRIOR YEAR
CONTROL DEFICIENCIES**

TOWN OF LOS GATOS

REPORT TO MANAGEMENT AND TOWN COUNCIL FOR THE FISCAL YEAR ENDED JUNE 30, 2008

PRIOR YEAR CONTROL DEFICIENCIES

TOWN OF LOS GATOS REDEVELOPMENT AGENCY (THE AGENCY)

Deficiency 07-01: Repeat Recommendation - Pursuant to Health and Safety Code Section 33334.12(g), "excess surplus" means any unexpended and unencumbered amount in an agency's Low and Moderate Income Housing Fund that exceeds the greater of: one million dollars (\$1,000,000), or the aggregate amount of tax increment deposited into the Low and Moderate Income Housing Fund during the agency's preceding four fiscal years (pursuant to Sections 33334.2 and 33334.6). It was determined that the Agency retained an excess surplus of approximately \$1,037,474 and \$518,803 for the fiscal years ended June 30, 2007 and 2006, respectively, based on the aggregate amount of tax increment deposited in the Low and Moderate Income Housing Fund.

Recommendation - Pursuant to Health and Safety Code Section 33334.12(a)(1)(B), we recommend that the Agency encumber the excess surplus within two years. The funds should be encumbered to carry out activities consistent with a redevelopment agency as defined in Health and Safety Code Sections 33334.2 and 33334.3. Since the excess surplus increased from 2006 to 2007, the Town should review and identify how much of the excess surplus needs to be encumbered by the end of 2008 versus 2009. Since the Agency's Low-Mod fund had an increase in fund balance of \$1.445 million for the fiscal year ended June 30, 2007, only a portion of the excess surplus from 2006 may still be unencumbered.

Town Response - The Town agrees with this finding and acknowledges the need to expend and encumber these funds. The Redevelopment Agency (RDA) is working with Seifel Consulting to develop affordable housing strategies. Recently, the RDA negotiated an agreement to loan \$777,000 of RDA low and moderate housing funds to Senior Housing Solutions for very low-income senior housing. Within the next two years, the Agency intends to initiate affordable housing projects and work with local non-profit developers to produce affordable housing units.

Status - The implementation of our recommendation is in progress. However, we did note an increase in the surplus of \$757,671 during the fiscal year ended June 30, 2008. See finding 08-01 on page 3 for our repeat recommendation. This was also included as a finding in the Redevelopment Agency's audit report.

FORMAL PURCHASING POLICY

Deficiency 07-02: Repeat Recommendation - The purchasing policy that the Town currently follows was issued in 1997.

Recommendation - We recommend the purchasing policy be reviewed and updated to provide strict guidelines on current day issues such as petty cash, travel reimbursements, credit card purchases and the amount for which a formal purchase order is required. It should also designate those individuals that are authorized to have a Town credit card and who can approve purchases. Once these policies are established, the rules and guidelines must be enforced and staff training should be provided.

Town Response - The Town agrees. An update to the Town's purchasing policies is listed as item #3 in the Finance division's Work Plan approved for FY 2007/08. Staff anticipates incorporating the updates as part of a proposed comprehensive Financial Systems Upgrade planned for FY 2007/08.

Status - Our recommendation was fully implemented by the end of the 2007/08 fiscal year.

**REQUIRED
COMMUNICATION
TO THE COUNCIL
(SAS 114)**

TOWN OF LOS GATOS

**REPORT TO MANAGEMENT AND TOWN COUNCIL
FOR THE FISCAL YEAR ENDED JUNE 30, 2007**

REQUIRED COMMUNICATION TO THE COUNCIL (SAS 114)

Professional standards require that we provide you with the following information related to our audit.

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

We are responsible for forming and expressing an opinion about whether the financial statements that have been prepared by management with the oversight of those charged with governance are presented fairly, in all material respects, in conformity with generally accepted accounting principles. The audit of the financial statements does not relieve management or those charged with governance of their responsibilities.

Planned Scope and Timing of the Audit

We performed the audit according to the planned scope and timing previously communicated to you in our meeting about planning matters in May of 2009.

Significant Accounting Policies

Management has the responsibility for selection and use of appropriate accounting policies. In accordance with the terms of our engagement letter, we will advise management about the appropriateness of accounting policies and their application. The significant accounting policies used by the District are described in Note 1 to the financial statements. No new accounting policies were adopted and the application of existing policies was not changed during 2008. We noted no transactions entered into by the District during the year for which there is a lack of authoritative guidance or consensus. There are no significant transactions that have been recognized in the financial statements in a different period than when the transaction occurred.

The following is a summary of GASB statements to be implemented by the end of June 30, 2009:

- GASB Statement number 45 - *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions.*

This statement requires that governmental entities evaluate their current and past service liabilities for other post employment benefits (OPEB), such as health or vision plans offered to retirees, to determine the annual required contributions for the postemployment benefits. Liabilities or assets may result from the difference between the actual payments and the annual required contributions. The past service liability will be allocated prospectively, thus a liability will not be recorded for past service liabilities in the first year.

We recommend that the District review its OPEB plan(s) offered to employees upon retirement as well as OPEB offered to current retirees to determine whether or not GASB 45 will have an impact. If the District pays a significant amount toward OPEB each year and has a significant number of current and future participants, it should familiarize itself with GASB 45. In addition, the District should determine the options available to calculate the OPEB liability and annual required contribution. The District has the option of using a simplified method or obtaining an

TOWN OF LOS GATOS

REPORT TO MANAGEMENT AND TOWN COUNCIL FOR THE FISCAL YEAR ENDED JUNE 30, 2007

REQUIRED COMMUNICATION TO THE COUNCIL (SAS 114)

actuarial study if there are less than 100 participants in the OPEB plan. We recommend the use of an actuary in most cases unless it is obviously not cost effective.

This Statement is effective for periods beginning after December 15, 2006, for *phase 1 governments* (those with total annual revenues of \$100 million or more); after December 15, 2008, for *phase 2 governments* (those with total annual revenues of \$10 million or more but less than \$100 million); and after December 15, 2008, for *phase 3 governments* (those with total annual revenues of less than \$10 million).

Accounting Estimates

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected.

The most sensitive estimates affecting the financial statements were:

- Valuation methodology of infrastructure assets
- Accrual and disclosure of compensated absences
- Depreciation estimates for capital assets, including depreciation methods and useful lives assigned to depreciable property

Management's judgments and estimates were based on the following:

- Valuation methodology of infrastructure assets was based on the Town's consultant study adjusted for annual capital asset activity.
- Accrual and disclosures of compensated absences were based on accrued eligible hours of vacation and sick leave at current pay rates for eligible employees.
- Useful lives for depreciable property were determined by management based on the nature of the capital asset.

We evaluated the key factors and assumptions used to develop the estimates in determining that they are reasonable in relation to the financial statements taken as a whole.

Disclosures in the Financial Statements

The disclosures in the financial statements are neutral, consistent, and clear. Certain financial statement disclosures are particularly sensitive because of their significance to financial statement users. The most sensitive disclosure(s) affecting the financial statements was (were):

- The disclosure of cash and investments in Note 2 to the financial statements is sensitive because of the dollar amounts relative to the financial statements as a whole.

TOWN OF LOS GATOS

REPORT TO MANAGEMENT AND TOWN COUNCIL FOR THE FISCAL YEAR ENDED JUNE 30, 2007

REQUIRED COMMUNICATION TO THE COUNCIL (SAS 114)

- The disclosure of capital asset activity in Note 5 informs the reader about the use of Town resources for improvements throughout the year.
- The disclosure of long-term debt in Notes 6 and 7 reports the Town's debt balances and activity.

Significant Difficulties in Performing the Audit

We encountered no significant difficulties in dealing with management in performing our audit.

Corrected and Uncorrected Misstatements

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management. Management has corrected all such misstatements. In addition, none of the misstatements detected as a result of audit procedures and corrected by management were material, either individually or in the aggregate, to the financial statements taken as a whole.

Disagreements with Management

For purposes of this letter, professional standards define a disagreement with management as a matter, whether or not resolved to our satisfaction, concerning a financial accounting, reporting, or auditing matter that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

Management Representations

We have requested certain representations from management that are included in the management representation letter dated December 4, 2008.

Management's Consultations with Other Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the District's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Significant Issues Discussed, or Subject to Correspondence, with Management

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the District's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.