



AGENDA

REGULAR MEETING OF
THE AUDIT COMMITTEE
SEPTEMBER 02, 2020 AT 2:00
PM
ATTEND VIRTUALLY

SPECIAL PROCEDURES FOR AUDIT COMMITTEE MEETING

Attendance: In response to the State's declaration of a Public Health Emergency, the Mayor's Proclamation of Emergency, and the ban on public gatherings of more than five (5) people, the Audit Committee meeting will be conducted virtually.

Viewing: Members of the public may stream the meeting live on the City of Santa Fe's YouTube channel at <https://www.youtube.com/user/cityofsantafe>. The YouTube live stream can be accessed at this address from most smartphones, tablets, or computers.

The video recording of this meeting will also remain available for viewing at any time on the City's YouTube channel at <https://www.youtube.com/user/cityofsantafe>. Staff is available to help members of the public access pre-recorded meetings on-line at any time during normal business hours. Please call 955-6521 for assistance.

Agenda: The agenda for the meeting will be posted at santafe.primegov.com/portal/search.

1. **CALL TO ORDER**
2. **ROLL CALL**
3. **APPROVAL OF AGENDA**
4. **APPROVAL OF MINUTES**
 - a. December 4, 2019
5. **EXECUTIVE SESSION**

In Accordance with the New Mexico Open Meetings Act, Specifically NMSA 1978, Section 10-15-1(H), Subpart (7), Meetings Subject to the Attorney-Client Privilege Pertaining to Threatened or Pending Litigation in Which the City Is or May Become a Participant. (Marcos D. Martinez, Senior Assistant City Attorney; Erin K. McSherry,



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City Attorney, ekmcherry@santafenm.gov, 955-6961). In Accordance with the New Mexico Open Meetings Act, Specifically NMSA 1978, Section 10-15-1(H), Subpart (2).

6. **NEW BUSINESS**
 - a. FY19 CAFR (CLA Staff and Finance Department Staff)
 - b. FY20 Internal Audit (REDW)
 - c. FY21 Internal Audit Resource Allocation
7. **PUBLIC COMMENT**
8. **MATTERS FROM STAFF**
9. **MATTERS FROM THE COMMITTEE**
10. **MATTERS FROM THE CHAIR**
11. **NEXT MEETING:**
12. **ADJOURN**

**Persons with disabilities in need of accommodations,
Contact the City Clerk's Office at (505) 955-6520 five (5) working days prior to the
meeting date**



Agenda

**CITY OF SANTA FE AUDIT COMMITTEE MEETING
CONVENTION CENTER ADMINISTRATIVE CONFERENCE ROOM
WEDNESDAY, DECEMBER 4, 2019
2:00 P.M. – 4:00 P.M.
AGENDA**

- 1. CALL TO ORDER**
- 2. ROLL CALL**
- 3. APPROVAL OF AGENDA**
- 4. APPROVAL OF AUDIT COMMITTEE MINUTES**
 - July 10, 2019 Meeting
 - August 7, 2019 Meeting
 - September 11, 2019 Meeting

5. MATTERS FROM THE CITY ATTORNEY

- **EXECUTIVE SESSION**

In Accordance with the New Mexico Open Meetings Act, Specifically NMSA 1978, Section 10-15-1(H), Subpart (7), Meetings Subject to the Attorney-Client Privilege Pertaining to Threatened or Pending Litigation in Which the City Is or May Become a Participant. (Marcos D. Martinez, Senior Assistant City Attorney; Erin K. McSherry, City Attorney, ekmcsherry@santafenm.gov, 955-6961)

6. NEW BUSINESS

- FY20 Internal Audit Update- Finance Department Staff
- FY20 First Quarter Update- Finance Department Staff

7. PUBLIC COMMENT

8. MATTERS FROM STAFF

9. MATTERS FROM COMMITTEE

10. NEXT MEETING DATE – To be determined

11. ADJOURNMENT

**Persons with disabilities in need of accommodations,
Contact the City Clerk's Office at (505) 955-6520 five (5) working days prior to the meeting date**

RECEIVED AT THE CITY CLERK'S OFFICE	
DATE:	November 26, 2019
TIME:	8:11 AM

VII. ITEMS FROM THE PUBLIC

VIII. ITEMS NEXT MEETING DATE – January 8, 2020

Persons with disabilities in need of accommodation, contact the City Clerk's office at 955-6520, five (5) working days prior to meeting date.

RECEIVED AT THE CITY CLERK'S OFFICE

DATE: November 26, 2019

TIME: 9:21 AM

SUMMARY INDEX
CITY OF SANTA FE AUDIT COMMITTEE
December 4, 2019

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1. CALL TO ORDER	2:05 pm	1
2. ROLL CALL	Quorum Present	1
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4. APPROVAL OF MINUTES September 11, 2019	Approved	2
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• FY 20 First Quarter Update	Discussion Only	3-6
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8. MATTERS FROM STAFF	Discussion Only	6
9. MATTERS FROM THE COMMITTEE	None	7
10. NEXT MEETING DATE:	January 15, 2020	7
12. ADJOURNMENT	Adjourned at 3:40 pm	7

**MINUTES OF THE
CITY OF SANTA FÉ AUDIT COMMITTEE
DECEMBER 4, 2019**

1. CALL TO ORDER

A regular meeting of the City of Santa Fé Audit Committee was called to order by Stephanie Woodruff, Chair, on this date at approximately 2:05 p.m. in the Convention Center Administrative Conference Room, Santa Fé, New Mexico.

2. ROLL CALL

Roll call indicated the presence of a quorum as follows:

Members Present:

Stephanie Woodruff, Chair
Al Castillo
Paul Margetson
Cristina Mulcahy

Members Absent:

Mary Ellen Erpelding-Chacon, Excused

Staff Attending

Mary McCoy, Finance Director
Debra Harris Garmandia, Controller

Others Attending:

Melissa Byers, Stenographer
Marcos Martinez

Ms. McCoy introduced new members of her staff and some veteran staff who will be presenting later in the meeting. The staff introduced were as follows: Clayton Pelletier, Interim Treasury Officer; Alexis Lotero, Budget Officer; Andy Hopkins, Primary Budget Analysts; Patrick Lucero, Interim Controller and Munis Project Manager; Deborah Harris Garmandia, Accounting Officer; Brad Fluetsch, Planning and Investment Officer and Marcos Martinez, Assistant City Attorney.

Ms. McCoy said, through the Munis, staff will be implementing the Human Capital Management System on January 1, 2020 and will follow that with the Budget and Inventory Systems.

3. APPROVAL OF AGENDA

MOTION: Member Mulcahy moved, seconded by Member Castillo, to approve the agenda as presented.

VOTE: The motion was unanimously approved by voice vote.

4. APPROVAL OF MINUTES:

- July 10, 2019, August 7, 2019 and September 11, 2019

It was noted that the July and August minutes had been previously approved.

MOTION: Member Castillo moved, seconded by Member Mulcahy, to approve the minutes of September 11, 2019, as presented.

VOTE: The motion was unanimously approved by voice vote.

5. MATTERS FROM THE CITY ATTORNEY

EXECUTIVE SESSION (IF NECESSARY)

In Accordance with the New Mexico Open Meetings Act, Specifically NMSA 1978, Section 1015-1(H), Subpart (7), Meetings Subject to the Attorney-Client Privilege Pertaining to Threatened or Pending Litigation in Which the City Is or May Become a Participant.

MOTION: Member Castillo moved to enter into executive session pursuant to the Open Meetings Act, §10-15-1(H)(7) for discussion regarding threatened or pending litigation in which the City is or may become a participant. The motion was seconded by Member Mulcahy.

VOTE: The motion was unanimously approved by roll call vote as follows:
Member Castillo, yes; Member Margetson, yes; Member Mulcahy, yes and Chair Woodruff, yes.

The Audit Committee entered into executive session at 2:16 p.m.

The Audit Committee concluded the executive session and returned to open session at 2:35 p.m.

MOTION: Member Castillo, pursuant to the Open Meetings Act, §10-15-1(J)(6), moved that the Audit Committee reconvene in open session and state for the record the matters discussed in the closed session were limited to those specified in the motion for closure. The motion was seconded by Member Mulcahy.

VOTE: The motion was unanimously approved by roll call vote as follows:

Member Castillo, yes; Member Margetson, yes; Member Mulcahy, yes and Chair Woodruff, yes.

6. NEW BUSINESS

- **FY20 Internal Audit Update- Finance Department Staff**

Ms. McCoy said the firm selected is REDW. She and the Chair had a kickoff meeting with the Internal Audit Team. Now in December there will be a kickoff meeting with City staff. The first internal audit will be for vendor and contract management. In preparation for the new accounting standards around leases where the City is the Leasee and Lessor our second internal audit will be around that process. The contract has been approved by Council and has been signed. REDW will be on the ground in the next few weeks. We have already started to pass on documents for the two internal audits to REDW.

- **FY20 First Quarter Update- Finance Department Staff**

Ms. McCoy informed the Committee that the Finance Department would be presenting the City's financial performance report on a quarterly basis to this Committee and the Finance Committee. The performance focuses on the revenues and expenditures.

Mr. Hopkins referred to pages 3 to 6 of the report, which gives a general overview of where the City is in terms of all operating funds, excluding CIP projects, and transitions over to the general fund. Staff is seeing both revenue and expenditures trending within our budget estimates. Our revenues are led by gross receipts taxes and lodgers' tax. Both are slightly above budget. On the expenditure side, the expenses are trending slightly below budget levels. A lot of it involves discretionary accounts. Where we have control, we are staying within the budget. General Fund revenues are trending slightly above budget.

Mr. Pelletier presented actual results for first quarter of FY 20. The gross receipts tax generated is \$1.58 billion in sales. Compared to gross receipts from sales in the first quarter of 2019, which was \$1.3 billion, it is up 16%. That generated the taxes the City received from the state. In FY 20, the City received \$3.9 million as compared to \$3.4 million in 2019 creating an 8% increase. We have started to receive internet sales tax from the legislation passed at last year's session. The City's portion of that is \$62,400 for the first quarter of FY 20, as indicated on page 8.

Member Castillo asked about the details on the Lodger's Tax.

Mr. Pelletier said the details are shown on pages 9 and 10.

Member Castillo asked about the operating budget.

Ms. McCoy said on page 4 is the all funds operating budget.

Mr. Pelletier said as the City Treasurer, it is his intention to develop a comparison for all revenues for future reports. GRT is the big one.

Chair Woodruff asked if the City is on track to exceed the budget in revenue.

Mr. Pelletier said yes, comparing actuals to actuals.

Mr. Hopkins said we are trending above budget for now.

Ms. McCoy said part of the reason for that is due to amended taxpayer returns and one-time additional revenue received from that. Two taxpayers amended their returns. One of Mr. Pelletier's tasks is to continue to build on those relationships. The reports from the Taxation and Revenue Department do not delve into much detail. Staff was able to confirm it was a one-time bump.

Member Castillo asked if the City is being aggressive in collections.

Ms. McCoy said the City has joined a lawsuit to sue Taxation and Revenue because we do not know that we have received everything we are owed.

Member Margetson asked if the wastewater fees are down.

Ms. McCoy said that is a major category that includes many different things.

Mr. Fluetsch said on the internal service fees, they are collected on the last day of the fiscal year. Staff distributes expenses such as IT, Risk Management, Finance and HR to other City Departments at the end of the year as well.

Mr. Pelletier said the detail on property tax is on page 9 and indicates where property taxes are coming from; 80% is residential and 20% is commercial.

Member Margetson asked what the percentage of property tax is, that the City receives.

Mr. Fluetsch said the City gets 9% of the property tax. Property tax is the most stable revenue source. The County benefits from having property taxes as well.

Member Castillo asked how property tax is calculated and shown.

Ms. Harris Garmandia said for property tax historically, the City is using a hybrid accrual cash processing method. In the current year, they are recording a cash receipt accrual using a cash basis date. Looking forward, we need to reach out to DFA to ask about changing accounting methods. She referred to page 4, for property tax, for FY 2019, year to date is \$145,000. The revenue is pushed further along calendar dates. Cash dates are aligned to when they are received. The actual first quarter revenue is \$17,653 more in the variance to the prior year. Currently, for property tax, we are \$21,000 above the prior year. Hopefully we will have a resolution on what can be presented and can go back and fix the prior year and current year.

Member Castillo said this is interesting and a big leap.

Ms. McCoy said according to City ordinance, staff has to present twice a year. The goal would be to present this in a user-friendly format. We are informing you about new additions, on page 8, on the City's GRT distribution. At the Finance Committee meeting, they asked about adding Lodgers Tax.

Member Margetson asked about transit/quality of life.

Mr. Fluetsch said within that increment of GRT – 75% goes to transit per the City ordinance. Also, in the City ordinance, it includes quality of life for seniors and youth, community services and parks and recreation.

Member Margetson asked about auditing the Lodgers Tax

Ms. McCoy said it was audited for FY 16 and 17. The universe they audited was the universe of the folks that are paying. The audit is for those who have paid.

Mr. Pelletier referred to page 9 and explained franchise fees. It is substantial.

Mr. Fluetsch said one of the biggest changes in that category is that the City increased the fee for PNM.

Mr. Pelletier referred to Lodgers Tax. He said he met with the Director of Tourism. A lot comes from AIRBNB. They are negotiating with VRBO. If negotiated it will give more stability to the collection. Entities renting facilities are going to get more exposure and we will be able to project better.

Mr. Fluetsch went over the investment portfolio. On the first page is the yield curve. You can draw a line at the five-year point. The policy does not allow us to invest beyond five years. We are allowed to use prime money market funds. There was a change in state statute last year. We need to update our policy per statute. The curve substantially

9. MATTERS FROM THE COMMITTEE

There were none.

10. NEXT MEETING DATE

The next meeting date will be on January 15, 2020.

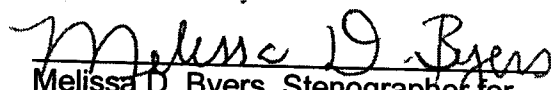
11. ADJOURNMENT

Upon motion by Member Castillo, and second by Member Margetson, the meeting was adjourned at approximately 3:40 p.m.

Approved by:

Stephanie Woodruff, Chair

Submitted by:


Melissa D. Byers, Stenographer for
Byers Organizational Support Services

City of Santa Fe FY19 CAFR



August 2020



Agenda

1. Timeline
2. FY19 CAFR Challenges
3. Finance Department/Accounting Division Staffing
4. Highlight Reconciliations
5. CLA FY19 CAFR Presentation



Timeline

- September 2017 – McHard Report Published identifying several weaknesses and deficiencies in City's Finances
- January 2018 – Council Adopted State Procurement Code
- Summer 2018 – Weekly Updates provided to Council on Corrective Action
- Summer 2018- FY17 CAFR completed, qualified opinion; single audit, unmodified
- Summer 2018- FY18 Year End Close process
- Fall 2018- GRT Bond Issued, City AA+ Ratings
- December 2018- FY18 CAFR completed on time, unmodified opinion; single audit, unmodified
- Spring 2019- Green Bond Issued, Waste Water AA+ Ratings
- Summer 2020 – Finance Department reorganization created structure to separate duties
- Summer 2019- FY19 Year End Close process started
- January 2020 – Council Adopted City Procurement Manual
- Fall 2019- Council notified FY19 CAFR would be late due to detailed review
- Summer 2020-
 - FY19 CAFR completed as projected, unmodified opinion; single audit, qualified
 - 5 Findings cleared up from FY18 to FY19 CAFR



FY19 CAFR Challenges

Antiquated Accounting System environment

- E1 Accounting System
 - manual processes, manual Journal Entries and file document searches
 - paper source files and paper Journal Entries, paper file chasing
- Finance Department required all city-wide journal entries scanned to share drive and duplicated in paper and FY19 electronic reconciliations

FY19 Year End Close restarted under COVID stay-home order, and Furloughs

- City-wide staff working remotely or working at department sites to perform and assist in FY19 Close
Accounting Staff working onsite at City Hall with contracted CPA's to perform FY19 Close and Audit Prep

FY19 Staffing Changes

- Finance Department staffing changes after the McHard Report.
- 7 of 8 existing employees left the Accounting division during FY19.
- Accounting division retained 1 employee and gained 5 new employees in FY19 & FY20.
- Hiring Freeze began in April 2020 when the Accounting Division had 2 vacant positions.



Accounting Division staffing levels for a budget of over \$300M

- Prior to McHard
 - 8 accountants
 - 5 staff working on Grants with 2 of those FTE dedicated solely to Grants
 - 40 hrs/wk for staff
- Currently
 - 5 accountants including Accounting Officer, with 2 vacant positions
 - 1 staff only dedicated to grant accounting
 - Staff is furloughed to 36 hours per week



Reconciliations- Definitions & what the reconciliation process entails

Definitions

- General Ledger (GL) – Accounting System of Record, shows the total summarized amount for accounts, Ex: \$500K
- Sub ledger – Detailed Customer Accounting, shows detail for accounts which is summarized in the GL, Ex: 5 transactions of \$100K
- Journal Entries (JEs) and Adjusting Journal Entries (AJEs) – Accounting method for reporting transactions or correcting JEs
- Reconciliation – process of ensuring two sets of records (General Ledger and sub ledger) are balanced

Reconciliation Process

1. Consistently update and maintain sub ledger with detailed activity
 - Billings, Customer Payments, Review Customer Accounts
2. Consistently and frequently compare sub ledger to general ledger totals which must be equal
 - Organize and file/maintain all activity, information and documentation to support both sub ledger and GL
 - Analyze side by side the sub ledger and GL for any activity differences
3. Research all differences, and perform the proper corrective action such as a AJE to bring both systems to equal
4. Create complete reconciliation packet for files- complete reconciliation packet consists of Pg. 1: Summary Reconciliation; Pg. 2: Detailed Reconciliation; Pg. 3: Excel spreadsheets to support, Pg. 1 & 2; Pg. 4: Outside source documents to support Pg. 3; Pg. 5: Munis GL/Trial Balance to support and proof out reconciliation



Reconciliations-

Finance Department introduced reconciliation analysis to staff for the FY18 & FY19 Year End Close. Training continues for the FY20 Year End Close.

Reconciliation Summary Example

Cash Common Reconciliation

Trial Balance Account: 7000.100900

Per Trial Balance	\$ 19,047,246.04
Per Bank Statement	\$ 20,780,967.92
Outstanding Checks	(2,118,184.26)
Deposits in Transit	384,462.38
Adjusted Balance	<u>\$ 19,047,246.04</u>
Variance from Trial Balance	<u><u>\$ -</u></u>

Summary AR Aging with Known Collectability Analysis

	YE Balance at 6/30/20	Known collected 7/1/20 - 7/15/20	Known uncollected Balance at 7/15/20	Uncollected percentage makeup
Current	250,000.00	50,000.00	200,000.00	98%
31-60 days	100,000.00	100,000.00	-	0%
61-90 days	50,000.00	50,000.00	-	0%
Over 90 days	25,000.00	20,000.00	5,000.00	2%
	<u>425,000.00</u>	<u>220,000.00</u>	<u>205,000.00</u>	<u>100%</u>



Reconciliations- Challenges with Reconciliations

- Time

- Reconciliations are combination of electronic and manual processes which are extremely tedious and very time consuming. Some can take weeks to do, based on volume of data, ease of research and locating source documents, whether reconciliations have been performed on a consistent basis so there's no learning curve which slows the process down, and date of last reconciliation.

- Staffing

- City must have adequate number of staff to perform reconciliations and research, city must have staff trained in reconciliations and research and staff must understanding importance of submitting timely reconciliations.

- Documentation

- City must have existence of and complete historical and current source information and documents, source information and documents mostly in paper files. Finance Staff and External Auditors must have access to source information and document files (paper or electronic), many not available or provided.



FY19 CAFR Presentation

CliftonLarsonAllen LLP

Raul J. Anaya, Principal, CLA

Ryan Jones, Director, Assurance, CLA

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City of Santa Fe

Audit Exit Presentation for June 30, 2019

Audit Opinions

Independent Auditors' Report – Clean Opinion (Unmodified)

- Limited procedures were performed, and no opinion was rendered on management's discussion and analysis, official roster, required supplementary information, and the Introductory and Statistical sections.
- Limited procedures were performed, and an "in-relation to" opinion is given on the additional information in the CAFR.

Report on Internal Control and Compliance for Each Major Federal Program (Uniform Guidance) – Modified Opinion

- CDBG – Entitlement Grants Cluster (CFDA 14.CDBG) – Modified for material noncompliance over reporting, program income, and special tests and provisions
- Airport Improvement Program (CFDA 20.106) – Modified for material noncompliance over reporting requirements



Audit Results

- **Audit Adjustments**

- 25 adjusting journal entries posted to the trial balance, with most of them resulting from audit procedures.

- **Findings Summary**

- 8 material weaknesses (3 federal)
- 8 significant deficiencies (3 federal)
- 5 compliance or other matters that don't rise to the level of a significant deficiency



Material Weaknesses

2019-001 – Internal Controls over Financial Reporting

- The City lacks an effective internal control structure over the financial close and reporting process to allow for timely and accurate financial reporting. The City is not adhering to a monthly or quarterly accounting close schedule



Material Weaknesses

2019-002 – Utility Billings Receivable and Liabilities

- The City did not perform a year-end reconciliation on accounts related to utility billings receivable and the associated allowances for doubtful accounts, resulting in misstatements of approximately \$1,000,000. Utility liabilities, including balances of \$588,586 in amounts owed to customers and deposits in the amount of \$876,018, were also not reconciled as of June 30, 2019. The City does not have support for these balances.



Material Weaknesses

2019-003 – Billing/Recognition of Federal Revenue

- The federal share of expenditures was more than revenues recognized in the financial statements by approximately \$3.5 million. Reimbursements were not claimed within the availability period of 60 days.

2019-004 – Construction in Process

- The City was unable to produce detailed supporting schedules for construction-in-process balances at June 30, 2019.



Material Weaknesses

2019-005 – Accrued Liabilities – Guarantees and Customer Deposits

- Deposits totaling approximately \$350,000 were indicated as received prior to 2010. These amounts have not been subject to a formal reconciliation.
- Additionally, customer advances in the amount of \$2,102,263 had not been subject to a formal reconciliation, resulting in an adjustment of \$712,461.



Material Weaknesses

2019-012 – Reporting (Federal Compliance)

- For both the Airport Improvement Program and the CDBG Program, we were unable to obtain evidence that federal financial reports and other grant-specific reports had been submitted as required.

2019-015 Program Income (Federal Compliance)

- For the CDBG program, the City was unable to produce evidence that program income requirements for subrecipients were being monitored by the City, as required under Uniform Guidance.



Material Weaknesses

2019-016 Special Tests and Provisions (Federal Compliance)

- For the CDBG program, the City was found to be lacking a Citizen Participation Plan.
- The City was found to be lacking approval from HUD for the release of funds for three out of the four projects tested.
- The City was found to be lacking environmental reviews for five subrecipients tested.





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City of Santa Fe
Leases Internal Audit

April 2020

City of Santa Fe Leases Internal Audit

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City of Santa Fe

Lease Administration Internal Audit

Report

City of Santa Fe
Audit Committee and Management

INTRODUCTION

We performed the internal audit consulting services described below to assist City of Santa Fe in evaluating lease administration. Our internal audit focused on evaluating City of Santa Fe's processes and controls over lease administration to determine if the City was utilizing best practices and sound internal controls. In addition, we evaluated the current processes in place to ensure compliance with the upcoming changes to the lease implementation standard. To gain an understanding of the processes and controls in place we interviewed key personnel. These interviews indicated significant opportunities for improvement in the existing control structure so detailed testing was not considered beneficial at this time.

Our services were performed in accordance with the terms of our Professional Services Agreement and engagement letter for internal audit services and the applicable Standards for Consulting Services prescribed by the American Institute of Certified Public Accountants. Although we have included management's responses in our report, we do not take responsibility for the sufficiency of these responses or the effective implementation of any corrective action.

PURPOSE AND OBJECTIVES

In June 2017, the Governmental Accounting Standards Board (GASB) published a single model for lease accounting in order to assist with improving the comparability and decision-making information provided on a government's financial statements. This change fundamentally alters the way leases were previously accounted for on a government's books by shifting the way leases are recognized, measured and disclosed. Major changes include:

- Lease classifications into "short-term", "contracts that transfer ownership" and "all other";
- Leases longer than 12 months will have balance sheet impact on both the lessee and lessor; and
- Financial statement disclosures and schedules will be required for contracts that transfer ownership and non-short-term leases.

The City of Santa Fe is required to implement GASB 87 by July 1, 2021, for its fiscal year 2022. The City of Santa Fe currently has a lease portfolio consisting of primarily real estate and equipment leases in which the City serves as both the lessee and lessor. Many leases in the portfolio will be subject to the GASB 87 rules therefore, it is critical for the City of Santa Fe to develop an implementation plan and work towards ensuring compliance with the new standard prior to the deadline.

Our internal audit focused on evaluating the City of Santa Fe's controls and processes around lease administration and oversight with an emphasis on measures taken to achieve compliance with GASB 87 by the required implementation date. The primary objectives were to assist management in determining whether processes surrounding the initiation, recording and tracking of leases provided adequate safeguards and reflected best practices to ensure leases were accounted for.

SCOPE AND PROCEDURES PERFORMED

In order to gain an understanding of the processes and operations, we interviewed the following personnel:

- Mary McCoy, Finance Director
- Debra Harris-Garmendia, Accounting Officer
- Clayton Pelletier, Interim Treasury Officer
- Patrick Lucero, Finance Project Manager
- Fran Dunaway, Chief Purchasing Officer
- Jarel LaPan Hill, City Manager
- Brad Fluetch, CFA, Investment and Planning Officer
- Kevin Kellog, Asset Development Manager
- Rich Brown, Economic Development Director
- Lauren Lucero, Economic Development Associate
- Erin McSherry, City Attorney
- Marcos Martinez, Assistant City Attorney
- Irene Romero, Office Manager
- Andrea Salazar, Assistant City Attorney

We inquired whether there are any documented policies and procedures related to lease initiation and management; however, it was communicated that any written documentation was either unavailable or outdated and inconsistent with current practices.

Based on the results of these conversations, significant issues were identified in the existing control structure that the City was already aware of. REDW determined testing the current processes would provide no additional benefit, as it is clear what the issues were and testing

would likely not identify any new insights. REDW worked closely with City of Santa Fe staff to assess which areas should be addressed first and provided recommendations for key considerations as suggested by GASB and the Government Finance Officers Association (GFOA).

OBSERVATIONS, RECOMMENDATIONS AND MANAGEMENT RESPONSE

We identified the following weaknesses in lessee/lessor internal controls:

1) LEASE MANAGEMENT

The new rules surrounding GASB 87 will require significant recordkeeping for all leases in place with City of Santa Fe. GASB 87 defines a lease as “a contract that conveys control of the right to use another entity’s nonfinancial asset as specified in the contract for a period of time in an exchange or exchange like transaction”. The new standard must be applied retroactively by restating financial statements for all prior periods presented.

The City of Santa Fe has no centralized repository for executed leases, nor any written policies and procedures regarding lease management for when the City is either the lessee or lessor. The Clerk’s Office files all executed contracts, including leases; however, there is no process in place to easily identify lease contracts and/or monitor key dates or other relevant compliance aspects. Further, it was unclear whether the information maintained at the Clerk’s Office was complete and/or accurate. Many lease contracts are old and may lack necessary details that will be necessary to comply with GASB 87.

The existing control structure only provides some oversight for leases in which the City is the Lessee. Lessor type leases are typically older, the contracts lack detail and there is no individual/department responsible for ensuring revenues earned are being collected timely.

Potential Risk: High – The City of Santa Fe has no mechanism in place to 1) easily identify its portfolio of leases as both the lessee and lessor 2) track and monitor key dates, payments, or other compliance aspects of each individual lease; and, 3) ensure compliance with financial reporting guidelines and upcoming GASB 87 implementation thus elevating this risk to high.

Recommendations

GASB 87 Implementation Plan

In accordance with key considerations provided by the GFOA, the City of Santa Fe should consider developing an implementation plan for GASB 87. While the City of Santa Fe has taken some proactive steps to get prepared, such as beginning work on developing a complete lease database and upgrading the MUNIS Financials system, there are several other steps that must be performed to ensure compliance with implementation rules. Below are several recommendations listed in order of suggested implementation that synchronize GASB and GFOA key considerations with the current structure at City of Santa Fe.

Lease Aggregation and Portfolio Development

City of Santa Fe should work closely with the Clerk’s Office, departments, and the Assessor’s Office to develop a lease portfolio as well as establish who maintains the information on each lease. City management must first determine how far back accounting and other recordkeeping documents should be examined to maximize the completeness of the portfolio population while

also being mindful of time and resources available. Consideration should be placed on any potentially substantial real estate leases that may have been executed long ago but still represent a significant revenue/expense to the City. In these instances, it may be practical to define different timeframes for each type of lease population. This time frames should be well documented and communicated to all participants working on the project. The portfolio should comprise all leases (both lessee and lessor) and provide a standardized method for differentiation. The City's lease population should be assessed at a) a lower-volume/higher-dollar value arrangement for real estate and property and b) a higher-volume/lower-dollar value arrangements for equipment. The City should then allocate time and resources based on the differing needs and risks of these populations. Also, the City needs to consider maintaining the following for each lease at a minimum:

- The tracking numbers used by various departments (i.e. Clerk's Office and Finance). Each lease should contain all these unique identifiers to more easily communicate with the various departments.
- Department Lease is assigned.
- Contact details of department employee assigned to oversee.
- Lease Terms
 - Lease commencement date; and
 - Lease end date (including end-of-lease options that are reasonably assured/certain).
- Payment Terms
 - Lease incentives;
 - Contractual minimum lease payments;
 - Residual value guarantee, including the amount of guarantee;
 - Bargain purchase options likely to be exercised, including the amount of the option; and
 - Any payments made prior to the start of the lease term.
- Lease Classifications
 - Economic lives of related assets;
 - Fair values of underlying assets; and
 - Interest rate (or incremental borrowing rate).

If existing lease agreements do not contain necessary information and/or are ambiguous, the City should work to revise or amend these contracts and explore whether a standard lease contract template could be used, where practicable. The City's Legal department should work in tandem with the employees tasked with lease aggregation to help facilitate any lease amendments or revisions that are necessary such that each agreement contains enough detail to comply with GASB 87.

Identify GASB 87 Leases

Once a complete portfolio of leases has been developed with key details, all leases should be assessed to determine what components must be disclosed under the GASB 87 rules. Per the GFOA, the following steps should be taken during the review of each lease contract:

- If the contract has both lease and non-lease components (i.e. maintenance agreements), separate the lease components from the non-lease components, and treat as separate contracts.

- If the contract has multiple underlying assets with different lease terms:
 - Treat each underlying asset as a separate component (lessor and lessee) and allocate the contract price to each component based on professional judgment and reasonableness.
 - Use the price for each component in the contract, or
 - Stand-alone prices for similar assets.
 - If unable to determine an allocation, treat as a single-lease unit.
- Determine the interest rate charged by the lessor in the agreement, if known (it may be implicit in the lease). Otherwise, an estimate of the interest rate the lessee would be charged to finance the lease is acceptable.

Lease Tracking Software

The City of Santa Fe will upgrade the MUNIS Financial system which will enable lease tracking. The City should ensure this software will meet the needs for GASB 87 compliance, prior to entering leases into the system. After all relevant GASB 87 leases have been identified, the City of Santa Fe must then perform calculations to determine what must be reported on the financial statements under the new standard. Under GASB 87, the City will be responsible for expanded financial reporting disclosures, both as lessee and lessor. The City should work to input all GASB 87 leases into the MUNIS Financials system and ensure appropriate review controls are in place over the calculations to ensure their accuracy.

Monitoring

The City needs to define how leases, from the lessee and lessor perspective, will be monitored. Once a portfolio of leases is developed, each lease should be assigned to a designated employee and/or department who will be responsible for ensuring compliance with lease terms.

Policy and Procedures

Once a lease repository has been developed and a lease tracking software implemented, management should develop policies and procedures around the newly developed processes. Policies are critical documents used to reinforce and clarify the standards expected of employees and will help the City manage staff more effectively as it defines what is acceptable, and creates consistency throughout all departments. Documented procedures are just as important to provide guidance on how activities should be performed and provides safeguards for maintaining institutional knowledge, in the event of employee departures. These new policies and procedures should document both the tracking and reporting components of a lease from both the lessee and lessor side. Items to consider adding are:

- Policies surrounding adequate documentation of lease terms, options, payment provisions;
- Controls to ensure Accounting is aware of new leases and changes to existing leases to ensure proper financial reporting; and
- Capitalization policies on intangible assets.

The City of Santa Fe should consider implementing standardized forms to assist in tracking this information. Policies and procedures should be developed and implemented prior to the effective implementation date of GASB 87.

Other Considerations

As discussed previously, the GASB 87 standard will significantly change the way governments report leases. As the City of Santa Fe works to implement the changes, other items of consideration include:

- Perform a review of state and local laws and agreements to determine impact with compliance on debit limitations and bond covenants; and
- Utilize the City's auditors (either external or internal) to work with staff who will be part of the lease process to provide training on implementation and monitoring on leases.

Management Response: Management agrees with this observation.

As GASB 87 establishes a single model for lease accounting based on the principle that leases are financings of the right to use an asset, the City will begin training and preparing in FY21 to be in compliance with GASB 87, effective for fiscal year 2022.

City staff has already started the process to create an inventory of existing leases and contracts. This is a time consuming process, as lease contracts are spread across the organization in different departments, divisions, and locations. As part of developing a complete portfolio, staff is gathering and maintaining information specific to GASB 87 compliance, (ex: lease term, extensions, termination options, and payment provisions) for leases, including buildings, land, and equipment as well as subscription-based information technology arrangements.

Staff is reviewing all agreements as agreements may meet the definition of a lease under GASB 87 even if the word "lease" is not in the agreement. As the City creates the inventory of existing leases and contracts, staff is also determining which agreements meet the GASB 87 definition of a lease and which can be excluded as not all leases will meet the definition of a lease under GASB 87. Although only leases that exceed the capitalization threshold of \$500,000 in total lease payments (or \$500,000 in remaining lease payments if the lease has already begun) must be recorded under GASB 87 accounting rules. However, the City is requiring that all leases be tracked and departments will be able to use MUNIS Financials to track all leases, regardless of dollar value.

Currently, policies and procedures along with a business process are being developed that will take into consideration internal controls and compliance with GASB 87 standards so that lessees will recognize a lease liability and an intangible right-to-use asset, and lessors will recognize a lease receivable and a deferred inflow of resources.

Within its MUNIS Financial System upgrade, beginning in FY21 the City has taken steps to ensure the system will be in compliance with GASB 87.

The system will have the following functionality: a central repository of leases, the ability to track City-owned and leased land and leases of other assets such as equipment and vehicles, and software subscriptions; billing for payments, track receivable leases (City is lessor) for land and other assets, and for facilities leased to a non-City entity; record lease accounting transactions, including lease payments, produce reports for reconciliation and financial statement disclosures. By using a single system for multiple business purposes, the City will reduce data entry and increase data accuracy.

As part of future trainings, a list of the data fields that will be required in MUNIS for each type of lease will be provided to Department staff. MUNIS system fields and reports are currently scheduled to be completed in the Spring of 2021 so that staff can start using the new system to maintain additional lease information in preparation for the FY22 effective date of GASB 87.

If existing lease agreements do not contain necessary information and/or are ambiguous, the City should work to revise or amend these contracts and explore whether a standard lease contract template could be used, where practicable.

2) LESSOR PAYMENTS

The City of Santa Fe currently is the lessee and lessor for various types of leases with differing payment requirements (i.e. annual, semi-annual, monthly, etc.). The City of Santa Fe uses an antiquated in-person payment method for lessor payments and there is no mechanism in place to ensure all lessors have been paying the correct amounts on a timely basis. City management communicated to REDW that given the antiquated payment method many lessor payments could have been uncollected for decades. In addition, there is minimal information requested when payments are made therefore, there is no process in place to ensure lease payments are appropriately applied to the correct receivable and revenue accounts. Lastly, there is no database to track lease payments and evaluate delinquencies thus the City is unable to accurately quantify current receivables and pursue collections if necessary. Due to the lack of controls, REDW was unable to quantify a range of potential uncollected revenues. The City of Santa Fe provided an analysis for one department (Economic Development) that attempted to quantify lessor revenues over the period of July 2015 through June 2019. This analysis resulted in total revenues of approximately \$803,000. REDW did not audit this schedule, nor is aware of its completeness, but it may provide some insight into the total magnitude of dollars related to lessor activity. This information was provided only for illustrative purposes as other departments may have fewer, or no, lessor type agreements.

Potential Risk: *High* – Failure for the City to adequately account for and monitor lease payments could result in lost revenue. In addition, failure for the City to adequately track lease payments and ensure lease revenues are posted to appropriate accounts could result in skewed financial data which ultimately could affect the decision making process when it comes to lease operations.

Recommendations

We recognize the City has already taken proactive steps towards addressing some of the issues discussed above such as hiring an individual to build a module in the MUNIS system that will allow the City to send invoices to lessees in accordance with lease provisions and also allow payments to be made electronically. In addition, steps are being taken to build a complete lease database in MUNIS Financials to ensure all leases can be tracked and lease receivables are being assessed on each lease to determine where issues may be. As progress continues in this area, we recommend the following items (in order of suggested implementation) be considered:

Cash Window Payments

Since not all payments will be electronic, it is critical for controls to be implemented at the City Hall payment window to ensure lease payments received are able to be recorded timely and accurately. The City should consider developing a form with all necessary information such as lessee number, lessee name, property address etc. for the lessee to fill out when making a

payment to assist the City in identifying which payments belong to which leases when they are submitted. In addition, as the City moves towards a paperless environment, it would be beneficial to add all relevant information to the individual invoice so when a customer brings in payment, the Cashier can reference the invoice for assistance in applying the payment to the correct account.

Cashiers who will be processing lease payments should be required to attend trainings regarding how lease payments should be accounted for to ensure the process is consistent. In addition, policies and procedures should be developed over the process for Cashiers to reference when processing payments.

Lease Receivables Tracking

Once a database of leases has been developed, the City should implement procedures to review outstanding receivables on a monthly basis to determine if collection efforts need to begin. The City Legal department should be involved in the process and made aware when a lessee becomes delinquent so they can process the collections in accordance with relevant laws and regulations.

Management Response: Management agrees with this observation.

In order to maximize revenue collection especially during the budget shortfalls resulting from COVID19, the City has already taken steps to address the issues identified by REDW such as creating an inventory and reviewing terms and collections monthly, ensuring lease revenues are posted to appropriate accounts, starting to upgrade the MUNIS Financial System that will allow the City to send invoices to lessees in accordance with lease provisions and also allow payments to be made electronically.

Within its MUNIS Financial System upgrade, the City of Santa Fe will implement an electronic payment system consisting of the modules General Billing and Vendor Self-Service. This will allow the City's lessees to submit electronic payments that are monitored and tracked in the Project Accounting and Accounts Receivable modules. Regarding the terms and compensation of each individual City lease, policies and procedures, along with a business process are currently being developed that will take into consideration internal controls and compliance with GASB 87 Standards.

City staff has already started the process to create an inventory of existing leases and contracts to ensure all leases can be tracked and lease receivables are being assessed. This is a time consuming process, as lease contracts are spread across the organization in different departments, divisions, and locations. Staff is gathering and maintaining information specific to GASB 87 compliance, (ex: lease term, extensions, termination options, and payment provisions) for leases, including buildings, land, and equipment as well as subscription-based information technology arrangements.

The City has developed a form with all necessary information such as lessee number, lessee name, property address etc. for the lessee to fill out when making a payment to assist the City in identifying which payments belong to which leases when they are submitted. This will create controls at the City's Cashier's Office to ensure lease payments received are able to be recorded timely and accurately. Cashiers processing lease payments have been trained on how lease payments should be accounted for to ensure the process is consistent and the Treasury Officer is developing policies and procedures for Cashiers to reference when processing payments.

Finally, in FY21 the Treasury Officer will implement procedures to review outstanding receivables on a monthly basis to determine if collection efforts need to begin and work with the City Attorney's Office when a lessee becomes delinquent so they can process the collections.

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This report is intended solely for the information and use of City of Santa Fe's management, Audit Committee and City Council members. If additional procedures had been performed, other matters might have come to our attention that would have been reported to you.

We received excellent cooperation and assistance from City of Santa Fe personnel during the course of our testing. We very much appreciate the courtesy and cooperation extended to our personnel. We would be pleased to meet with you to discuss our findings and answer any questions.

REDW LLC

Albuquerque, New Mexico
August 26, 2020