

LOCAL GOVERNMENT FINANCIAL REPORTING SYSTEM

Performance Audit



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LOCAL GOVERNMENT FINANCIAL REPORTING SYSTEM

EXECUTIVE SUMMARY

Our performance audit disclosed the following:

COMMUNITY REDEVELOPMENT AGENCIES

Finding No. 1: Current law could be enhanced to be more specific as to the types of expenditures that qualify for undertakings of a community redevelopment agency (CRA).

Finding No. 2: Current law could be enhanced to provide county taxing authorities more control over expenditures of CRAs created by municipalities to help ensure that CRA trust fund moneys are used appropriately.

Finding No. 3: Current law could be enhanced to require that all CRAs, including those created before October 1, 1984, are subject to statutory provisions that specify authorized uses of CRA trust fund moneys.

Finding No. 4: Current law could be enhanced to allow CRAs to provide for reserves of unexpended CRA trust fund balances to be used during financial downturns.

Finding No. 5: Current law could be enhanced to promote compliance with the audit requirement in Section 163.387(8), Florida Statutes, and to require such audits to include a determination of compliance with laws pertaining to expenditure of, and disposition of unused, CRA trust fund moneys.

UNRESTRICTED FUND BALANCE IN THE GENERAL FUND

Finding No. 6: Current law could be enhanced to require local governments to establish a minimum fund balance policy or maintain a certain amount of unrestricted fund balance in the General Fund, which would reduce the risk of local governments not having available resources to mitigate revenue shortfalls or unanticipated expenditures.

BUDGET TRANSPARENCY

Finding No. 7: Current law could be enhanced to require the reporting of all local governments that fail to comply with the budget transparency requirements and to specify time periods for the tentative budget, final budget, and budget amendments to remain on a local government's Web site, which would promote more uniform budget transparency.

FLORIDA DEPARTMENT OF MANAGEMENT SERVICES, DIVISION OF RETIREMENT

Finding No. 8: The Florida Department of Management Services needed to enhance its procedures to ensure timely contact of newly created local governmental entities, to timely obtain data on retirement systems or plans, and timely contact of entities that change to the Florida Retirement System from a local plan.

AUDITOR SELECTION PROCESS

Finding No. 9: Current law could be enhanced to specify the composition of the audit committee for local governments other than noncharter counties to help ensure that audit committees function in a prudent manner.

Finding No. 10: Local governments did not always ensure that contracts for audit services include the provisions required by law.

Finding No. 11: Local governments we reviewed did not always perform auditor selection procedures pursuant to Section 218.391, Florida Statutes, and some local governments we reviewed had gone many years without entering into new contracts for audit services. Current law could be enhanced to require that auditor selection procedures be performed at specific intervals and to encourage local governments to comply with Section 218.391, Florida Statutes.

TANGIBLE PERSONAL PROPERTY

Finding No. 12: Based on the results of our audit, which disclosed numerous municipalities and non-taxing special districts that had not implemented adequate controls over tangible personal property, it was not apparent why such entities are not subject to the accountability requirements established by Chapter 274, Florida Statutes.

LOCAL GOVERNMENT BOND ISSUES

Finding No. 13: Local governments we reviewed did not always document the conditions favoring the method of sale selected for bond issues or use an independent financial advisor, which increased the risk of unfavorable issue terms or excessive bond issue costs.

Finding No. 14: Local governments did not always use a competitive selection process when selecting financial advisors, underwriters, and bond counsel for bond issues, potentially increasing costs associated with bond issues.

Finding No. 15: Current law requires the Florida State Board of Administration, Division of Bond Finance (Division) to publish a regular newsletter to the bond community and the general public; however, the Division is no longer publishing a regular newsletter as the type of information formerly included in the newsletter is published by other entities and available on the Internet.

SPECIAL DISTRICT DETERMINATIONS

Finding No. 16: While the Department of Economic Opportunity has the authority to determine whether a special district should be classified as dependent or independent, it does not have the authority to determine whether an entity should be treated as a special district. As a result, some entities that appear to be special districts are not subject to the accountability and oversight provisions in Chapter 189, Florida Statutes.

BACKGROUND

Section 11.45(2)(g), Florida Statutes, requires the Auditor General to conduct a performance audit of the local government¹ financial reporting system (System) at least every three years and to make recommendations to local governments, the Governor, and the Legislature as to how the reporting system can be improved and how program costs can be reduced. The “System” means any statutory provisions related to local government financial reporting and is intended to provide for the timely, accurate, uniform, and cost-effective accumulation of financial and other information that can be used by the members of the Legislature and other appropriate officials to accomplish the following goals:

- Enhance citizen participation in local government;
- Improve the financial condition of local governments;
- Provide essential government services in an efficient and effective manner; and
- Improve decision making on the part of the Legislature, State agencies, and local government officials on matters relating to local government.

FINDINGS AND RECOMMENDATIONS

Community Redevelopment Agencies

Chapter 163, Part III, Florida Statutes, also known as the “Community Redevelopment Act of 1969” (Act) authorizes the creation of redevelopment agencies by counties and municipalities for the purposes of redevelopment of slums

¹ The term “local government” refers to local governmental entities as defined in Section 218.31(1), Florida Statutes (i.e., counties, municipalities, and special districts).

and blighted areas that are injurious to the public health, safety, morals, and welfare of residents and for which there is a shortage of housing affordable to residents of low or moderate income, including the elderly. This Part provides requirements that address the manner in which such an agency may be established, the powers of the agency, the funding of the agency, expenditure restrictions, and reporting and audit requirements.

A community redevelopment agency (CRA) is funded through tax increment financing whereby the CRA generally receives annually 95 percent of the difference between the amount of ad valorem taxes levied by each taxing authority² (exclusive of amounts derived from debt service millages) on taxable properties within the designated community redevelopment area, and the amount of taxes that would have been produced by the millage rates levied by the taxing authorities prior to the effective date of the ordinance providing for the funding.

Finding No. 1: Use of CRA Trust Fund Moneys

Community redevelopment or redevelopment means undertakings, activities, or projects of a CRA in a community redevelopment area for the elimination and prevention of the development or spread of slums and blight, reduction or prevention of crime, provision of affordable housing, slum clearance and redevelopment, or rehabilitation and revitalization of coastal resort and tourist areas that are deteriorating and economically distressed.³

Section 163.387(1), Florida Statutes, establishes a redevelopment trust fund (CRA trust fund) for each CRA created and provides for its annual funding through tax increment revenues. Among the powers granted by the Act to carry out community redevelopment are: to make contracts; to disseminate slum clearance and community redevelopment information; to undertake community redevelopment and related activities; to furnish or repair streets, public utilities, playgrounds, and other public improvements; to hold or dispose of property for redevelopment. Section 163.387(6), Florida Statutes, provides that “Moneys in the redevelopment trust fund may be expended from time to time for undertakings of a community redevelopment agency as described in the community redevelopment plan for the following purposes, including, but not limited to:”

- Administrative and overhead expenses necessary or incidental to the implementation of a CRA plan.
- Expenses of redevelopment planning, surveys, and financial analysis, including the reimbursement of the governing body or the CRA for such expenses incurred before the redevelopment plan was approved and adopted.
- Acquisition of real property in the redevelopment area.
- Clearance and preparation of any redevelopment area for redevelopment and relocation of site occupants within or outside the community redevelopment area as provided in Section 163.370, Florida Statutes.
- Repayment of principal and interest or any redemption premium for any other form of indebtedness.
- Expenses incidental to or connected with the issuance, sale, redemption, retirement, or purchase of any form of indebtedness, including funding of any reserve, redemption, or other fund or account provided for in the ordinance or resolution authorizing such form of indebtedness.
- Development of affordable housing within the community redevelopment area.
- Development of community policing innovations.

A CRA is a special district that may only exercise those powers that have been expressly granted by statute or that are necessarily exercised in order to carry out an express power. The Attorney General has noted in numerous opinions

² Certain taxing authorities are exempted from contributing tax increment revenues pursuant to Section 163.387(2)(c), Florida Statutes.

³ Section 163.340(9), Florida Statutes.

regarding a special district's authority that any reasonable doubt as to the lawful existence of a particular power sought to be exercised must be resolved against the exercise thereof. In our operational audits of CRAs in recent years, we have noted that CRA trust fund moneys have often been used for purposes not specifically delineated in Section 163.387(6), Florida Statutes, and were not directly related to "redevelopment" as it is defined in law. For example, one CRA we audited expended \$2.1 million during the period October 2011 through March 2013 to fund various nonprofit organizations' operating expenses, promotional activities, or for socially beneficial programs and \$1.1 million to sponsor tennis tournaments for the municipality that created the CRA.⁴ Similar findings relating to promotional activities were noted in other CRA audits we conducted.⁵

In considering the allowability of the types of expenditures discussed above, we found limited guidance to CRAs as to what constitutes authorized expenditures other than the language of the Act. In Opinion No. 2010-40, the Attorney General responded to an inquiry regarding whether a CRA may expend funds for festivals or street parties designed to promote tourism and economic development, make grants to entities that promote tourism and economic development, or make grants to nonprofit entities providing socially beneficial programs. The Attorney General stated in part that "[t]he enumerated uses of community redevelopment trust fund moneys are likewise couched in terms of redevelopment activities involving 'bricks and mortar' in a manner of speaking, rather than promotional campaigns to encourage people to populate the area once the redevelopment has been accomplished. However, to read the statute as precluding the promotion of a redeveloped area once the infrastructure has been completed would be narrowly viewing community redevelopment as a static process. Accordingly, I cannot say that the use of community redevelopment funds would be so limited that the expenditure of funds for the promotion of a redeveloped area would be prohibited. However, grants to entities which promote tourism and economic development, as well as to nonprofits providing socially beneficial programs would appear outside the scope of the community redevelopment act." The Attorney General further stated that "Use of community redevelopment funds to pay entities promoting tourism or providing socially beneficial programs, however, does not have an apparent nexus to carrying out the purposes of the community redevelopment act."

Because some CRA boards have broadly interpreted the phrase in Section 163.387(6), Florida Statutes, "including, but not limited to" to authorize expenditure of moneys for anything perceived as a CRA undertaking, CRA trust fund moneys may be expended in a manner inconsistent with legislative intent of the Act. Providing clear direction to CRAs as to the express authority for expending CRA trust fund moneys, particularly with respect to promotional activities, would ensure that legislative intent is accomplished.

Recommendation: The Legislature should consider amending Section 163.387(6), Florida Statutes, to be more specific as to the types of expenditures that qualify as undertakings of a CRA, particularly with respect to promotional activities.

Finding No. 2: CRA Governance

Pursuant to law⁶, a county or municipality may not create a CRA unless they establish (1) the existence of one or more slum or blighted areas, or the existence of one or more areas in which there is a shortage of housing affordable to residents of low or moderate income, including the elderly, and (2) the rehabilitation, conservation, or redevelopment,

⁴ Report No. 2014-013, finding No. 1.

⁵ Report No. 2013-093, finding No. 11, and report No. 2008-036, finding No. 1.

⁶ Section 163.355, Florida Statutes.

or a combination thereof, of such area or areas, including, if appropriate, the development of housing that residents of low or moderate income, including the elderly, can afford, and is necessary in the interest of the public health, safety, morals, or welfare of the residents of such county or municipality. The clear legislative purpose of establishing a CRA is to eliminate slum or blighted conditions or establish affordable housing within a specified area. All CRA activity is to be accomplished pursuant to a CRA plan approved by the CRA's governing body.⁷ Further, the CRA plan may be amended, including expansion of the boundaries of the CRA.⁸

The governing body of a county or municipality may declare itself to be a CRA.⁹ Although one or more members of the CRA's governing body may be representatives of a taxing authority,¹⁰ the governing bodies of the majority of the CRAs as of September 30, 2014, were the same as the governing body of the entity that created the CRA. For 144 (67 percent) of the 214 active CRAs as of September 30, 2014, the members of the CRA's governing body were the same as the members of the governing body of the entity that created the CRA.¹¹

When the governing body of the entity that created the CRA is functioning as the CRA board, there is an increased risk that CRA trust fund moneys may be used to supplant those used for general operating expenses of the entity that created the CRA. CRAs are prohibited from paying for general government operating expenses unrelated to carrying out the CRA plan.¹² In some of our audits of CRAs, we noted instances in which the CRA paid moneys to the municipality that created the CRA for services purportedly provided to the CRA, but for which there was no evidence to document the services provided and, as a result, it appeared these moneys were used to pay for general operating costs of the municipality. For example, we noted that two CRAs we audited paid moneys to the municipalities that created the CRAs for all or a portion of municipal employees' salary expenses with no documentation to evidence the time the applicable individuals expended on CRA activities.¹³ Additionally, another CRA we audited appeared to have subsidized the operations of the municipality that created the CRA through property rental arrangements between the CRA and the municipality.¹⁴

A total of 186 (87 percent) of the 214 active CRAs as of September 30, 2014, were created by municipalities.¹⁵ For a CRA created by a municipality, there are at least two potential taxing authorities contributing to the CRA, the county and the municipality.¹⁶ Some CRAs have multiple taxing authorities that contribute to the CRA. For example, for the 2012-13 fiscal year, the Daytona Beach CRA received tax increment revenues totaling \$4.4 million, of which \$2 million (45 percent) was contributed by the City of Daytona Beach, \$1.8 million (41 percent) was contributed by Volusia County, and \$0.6 million (14 percent) was contributed by six other taxing authorities.

Taxing authorities, other than the entities that created the CRAs, are required to remit tax increment revenues to the CRAs but likely have no say in how their contributions are spent. As noted above, CRA activity is to be accomplished pursuant to a CRA plan approved by the CRA's governing body and such plan may be subsequently amended. Although charter counties may retain much of the control over municipal CRAs by not delegating authority to the municipal governing authority when the CRA is created, noncharter counties and charter counties that were chartered

⁷ Sections 163.360 and 163.387(6), Florida Statutes.

⁸ Section 163.361, Florida Statutes.

⁹ Section 163.357(1)(a), Florida Statutes.

¹⁰ Section 163.356(2), Florida Statutes.

¹¹ Florida Department of Economic Opportunity Special District Accountability Program's Official List of Special Districts.

¹² Section 163.370(3), Florida Statutes.

¹³ Report No. 2008-036, finding No. 11, and report No. 2013-093, finding No. 12.

¹⁴ Report No. 2014-013, finding No. 2.

¹⁵ Florida Department of Economic Opportunity, Special District Accountability Program's Official List of Special Districts. Excludes the City of Jacksonville.

¹⁶ Likewise, some county CRAs' boundaries include property within municipalities.

after creation of the CRA do not have this option.¹⁷ Of the 186 active municipal CRAs at September 30, 2014, 104 (56 percent) were located in charter counties and 82 (44 percent) were located in noncharter counties; however, 23 of the 104 municipal CRAs located in charter counties were created prior to the chartering of the county. Thus, at a minimum, 105 (82 + 23, or 56 percent) of the municipal CRAs are not required by law to obtain county approval for adoption of, or amendment to, their CRA plans.¹⁸

Most CRA governing bodies are the same as the entity that created the CRA, the vast majority of CRAs are created by municipalities,¹⁹ and the taxing authorities other than the entities that created the CRAs may be required to remit tax increment revenues for up to 60 years.²⁰ Requiring county approval of municipal CRA plans and amendments thereto would strengthen oversight of CRA activities and help ensure that CRA funds are expended only for authorized CRA activities.

Recommendation: The Legislature should consider revising Chapter 163, Florida Statutes, to require county approval for the adoption and amendment of all municipal CRA plans.

Finding No. 3: CRA Exemptions

Pursuant to Section 163.362(11), Florida Statutes, some CRAs are exempted from certain requirements based on when the CRA approved and adopted a CRA plan or authorized the issuance of debt. Section 163.362, Florida Statutes, establishes the requirements for the contents of the CRA plan and the following elements are not required to be included in the CRA plan for the 31 CRAs that adopted a CRA plan or were authorized to issue debt prior to October 1, 1984:

- A legal description of the boundaries of the community redevelopment area and the reasons for establishing such boundaries.
- If the redevelopment area contains low or moderate income housing, a neighborhood impact element that describes in detail the impact of the redevelopment upon the residents of the redevelopment area and the surrounding areas in terms of relocation, traffic circulation, environmental quality, availability of community facilities and services, effect on school population, and other matters affecting the physical and social quality of the neighborhood.
- Identification specifically of any publicly funded capital projects to be undertaken within the community redevelopment area.
- Provision of an element of residential use in the redevelopment area if such use exists in the area prior to the adoption of the plan or if the plan is intended to remedy a shortage of housing affordable to residents of low or moderate income, including the elderly, or if the plan is not intended to remedy such shortage, the reasons therefor.
- A detailed statement of the projected costs of the redevelopment, including the amount to be expended on publicly funded capital projects in the community redevelopment area and any indebtedness of the CRA, the county, or the municipality proposed to be incurred for such redevelopment if such indebtedness is to be repaid with increment revenues.

¹⁷ Sections 163.410 and 163.415, Florida Statutes.

¹⁸ It was not practicable for us to determine the extent to which charter counties had delegated authority under the Act to municipalities.

¹⁹ Of the 214 CRAs, 186 were created by municipalities, 26 were created by counties, 1 was created by the consolidated city/county government of Jacksonville, and 1 was created by a municipality and county.

²⁰ Section 163.387(2)(a), Florida Statutes.

A CRA is authorized to expend moneys only as described in its CRA plan. One CRA we audited, which was created in 1981, disclosed that the CRA plan contained some general objectives that were vague regarding the method of accomplishment and very few specific projects with long range accomplishment dates (e.g., within 10 years).²¹ As a result, we found it difficult to link its expenditures to the CRA plan. In response to our requests for the reference in the CRA plan to support expenditures, the CRA indicated that it was not required to be specific in its CRA plans as to the projects it will undertake or how CRA moneys will be spent.

Since CRAs are not authorized to expend moneys except as described in their CRA plans, it is not apparent why some CRAs would be exempt from requirements that provide specificity. Providing the elements described in Section 163.362, Florida Statutes, affords transparency in planned CRA projects and a means to hold CRAs accountable.

Recommendation: **The Legislature should consider repealing Section 163.362(11), Florida Statutes, to impose the same requirements as to the contents of CRA plans on all CRAs.**

Finding No. 4: CRA Trust Fund Unexpended Balances

Section 163.387(7), Florida Statutes, provides that on the last day of a CRA's fiscal year, any money remaining in the CRA trust fund after the payment of allowable expenses for such fiscal year must be:

- Returned to each taxing authority that paid the increment in the proportion that the amount of the payment of such taxing authority bears to the total amount paid into the trust fund by all taxing authorities for that year; or
- Used to reduce the amount of any indebtedness to which increment revenues are pledged; or
- Deposited into an escrow account for the purpose of later reducing any indebtedness to which increment revenues are pledged; or
- Appropriated to a specific redevelopment project pursuant to an approved CRA plan, which project will be completed within three years from the date of such appropriation.

While the law provides various options for CRAs to dispose of ending balances in the CRA trust fund, it does not provide a mechanism for CRAs to establish reserves to mitigate current and future risks, such as revenue shortfalls and unanticipated expenditures. For example, in the economic downturn in recent years, CRAs experienced significant reductions in tax increment revenues due to the decline in property values and limitations placed on the ad valorem revenue-raising capability of counties and municipalities. As discussed further under the heading, **Unrestricted Fund Balance in the General Fund**, the Government Finance Officers Association (GFOA) recommends that all local governments, regardless of size, maintain unrestricted fund balance in the General Fund of no less than two months of regular General Fund operating revenues or regular General Fund operating expenditures. Allowing for the establishment of reserves would provide additional assurance that CRA operations, including debt repayments, may continue without interruption.

Recommendation: **The Legislature should consider amending Section 163.387(7), Florida Statutes, to provide CRAs with the ability to establish reserves for mitigating current and future risks and to exempt the reserves from the ending balance disposition requirements.**

²¹ Report No. 2008-036, finding No. 2.

Finding No. 5: CRA Audits

Section 163.387(8), Florida Statutes, requires CRAs to provide for an audit of the CRA trust fund each fiscal year and a report of such audit to be prepared by an independent certified public accountant or firm. Such report must describe the amount and source of deposits into, and the amount and purpose of withdrawals from, the trust fund during the fiscal year; the amount of principal and interest paid during the fiscal year on any indebtedness to which increment revenues are pledged; and the remaining amount of such indebtedness.

We selected 60 CRA's to determine how they met this requirement. We noted that all 60 CRA's were included within the local governing authority's financial statements in the local governing authority's 2012-13 fiscal year audit report prepared pursuant to Section 218.39, Florida Statutes. Of the 60 audit reports, 8 (13 percent) did not provide for an auditor's opinion on the CRA trust fund, and 4 (7 percent) did not provide the amount and sources of deposits into, and the amount and purpose of withdrawals from, the redevelopment trust fund during the fiscal year. These instances of noncompliance with Section 163.387(8), Florida Statutes, may have occurred because the CRAs and their auditors were not aware of these requirements or may have misunderstood the requirements.

If CRAs wish to satisfy the audit requirement in Section 163.387(8), Florida Statutes, through inclusion in the local governing authority's audit, the CRA trust fund must be reported as a major fund,²² or the auditor must separately provide an opinion on the CRA trust fund and the information required by the law. Because the CRA trust fund may not meet the major fund reporting criteria established by the Governmental Accounting Standards Board (GASB), it is often aggregated and displayed in a single column along with the local government's other nonmajor funds; consequently, the financial statement presentation would not be at the level of detail required to demonstrate compliance with Section 163.387(8), Florida Statutes. GASB provides that governmental funds that do not meet the major fund reporting criteria, but for which the government's officials believe is particularly important to financial statement users, may be reported as major funds. However, some CRAs may not be aware of this reporting option for demonstrating compliance with Section 163.387(8), Florida Statutes.

In addition to the questionable or unsupported uses of CRA trust funds moneys disclosed by our audits of three CRAs referred to in finding No. 2, our audits of two of those CRAs disclosed uses of CRA trust fund moneys that did not appear to be in accordance with the approved CRA plans contrary to Section 163.387(6), Florida Statutes.²³ In addition, our audits of two CRAs disclosed that the CRAs did not document compliance with Section 163.387(7), Florida Statutes, regarding the disposition of unexpended CRA trust fund moneys.²⁴

Although Section 163.387(8), Florida Statutes, provides for a separate audit of the each CRA trust fund, this requirement is normally accomplished through the annual financial audit pursuant to Section 218.39, Florida Statutes, the scope of which typically would not disclose questionable uses of CRA trust fund moneys or failure to document the lawful disposition of unexpended CRA trust fund moneys disclosed by our audits. Requiring that the audit pursuant to Section 163.387(8), Florida Statutes, include a determination of compliance with Sections 163.387(6) and 163.387(7), Florida Statutes, would improve accountability for CRA resources and provide additional transparency for those taxing authorities required to remit tax increment revenues to a CRA.

²² The GASB established criteria for a fund to be reported as a major fund in an entity's governmental financial statements and provides that nonmajor funds should be aggregated and displayed in a single column. In addition to funds that meet the major fund criteria, any other governmental or enterprise fund that the government's officials believe is particularly important to financial statement users (for example, because of public interest or consistency) may be reported as a major fund. See GASB Statement No. 34, paragraph 76, as amended by GASB Statement No. 65, paragraph 33, and GASB Statement No. 37, paragraph 15, as amended by GASB Statement No. 65, paragraph 33.

²³ Report No. 2008-036, finding No. 1, and report No. 2013-093, finding No. 11.

²⁴ Report No. 2013-093, finding No. 13, and report No. 2014-013, finding No. 4.

Recommendation: CRAs should ensure that annual audits are obtained of the CRA trust fund, and the audit reports include all information required by Section 163.387(8), Florida Statutes. The Legislature should consider amending Section 163.387(8), Florida Statutes, to require that the audit of the CRA trust fund include a determination of compliance with Sections 163.387(6) and 163.387(7), Florida Statutes.

Unrestricted Fund Balance in the General Fund

Finding No. 6: General Fund Unrestricted Fund Balance and Minimum Fund Balance Policy

The General Fund serves as a local government's chief operating fund and accounts for all financial resources of the general government, except those required to be accounted for in another fund. General government administration, such as the general counsel's office, budget and procurement services, financial services, human resources, and growth management, as well as public safety (police and fire), community development, and public works, are typically funded from the General Fund. Revenues supporting general government operations may include property, utilities service, and franchise taxes; licenses and permits; and various service charges.

Fund balance in a governmental fund represents the net financial resources available in the fund. The GASB, through issuance of GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, established classifications of fund balance based on the extent to which the funds are bound by external and internal constraints. Fund balance classified as nonspendable and restricted represent funds that cannot be spent or must be spent for specific purposes based on external or legal constraints. Fund balance classified as committed is restricted for specified purposes based on formal action of the governing body using its highest level of decision-making authority (i.e., by ordinance for counties and municipalities and by resolution for special districts), and fund balance classified as assigned or unassigned is essentially available to the local government for any lawful governmental purpose.

According to the GFOA Best Practice, *Appropriate Level of Unrestricted Fund Balance in the General Fund* (October 2009) (*Best Practice*), it is essential that governments maintain adequate levels of fund balance to mitigate current and future risks (e.g., revenue shortfalls and unanticipated expenditures) and to ensure stable tax rates. The *Best Practice* recommends, at a minimum, that a local government, regardless of size, maintain unrestricted²⁵ fund balance in the General Fund of no less than two months (17 percent) of regular General Fund operating revenues or regular General Fund operating expenditures. The choice of revenues or expenditures as a basis of comparison may be dictated by what is more predictable in a government's particular circumstances.

In its *Best Practice*, the GFOA also recommends that governments establish a formal policy on the level of unrestricted fund balance that should be maintained in the General Fund. The formal policy should include specific plans for replenishing the unrestricted fund balance, should it fall below the target level.

Minimum Fund Balance Policy. We surveyed 35 local governments (5 counties, 15 municipalities, and 15 special districts) to determine if the entities' governing bodies had adopted a minimum unrestricted fund balance policy for the General Fund. Of the 33 responses we received, 24 (73 percent) of the entities (3 counties, 7 municipalities, and 14 special districts) had not adopted a minimum fund balance policy. Of the 9 entities that had adopted a minimum unrestricted fund balance policy for the General Fund, 2 municipalities' policies did not address a method for replenishing unrestricted fund balance, should it fall below the target level.

²⁵ In the *Best Practice*, the term "unrestricted" refers to those amounts classified as committed, assigned, and unassigned.

Levels of General Fund Unrestricted Fund Balance Reported. We reviewed General Fund unrestricted fund balance reported in 266 local governments' 2012-13 fiscal year audited financial statements and noted that 45 (17 percent) local governments reported General Fund unrestricted fund balance that was less than the GFOA-recommended amount of 17 percent of operating revenues or expenditures, as follows:

- For the 66 counties we reviewed, 6 (9 percent) reported General Fund unrestricted fund balance of less than 17 percent of operating revenues and operating expenditures.
- For the 100 municipalities of varying sizes we reviewed, 13 (13 percent) reported General Fund unrestricted fund balance of less than 17 percent of operating revenues and operating expenditures.
- For the 100 special districts of varying sizes and functions we reviewed, 26 (26 percent) reported General Fund unrestricted fund balance of less than 17 percent of operating revenues and operating expenditures.

Although there are Florida laws that govern the level of unrestricted funds maintained by district schools boards, colleges, and universities,²⁶ there are no similar requirements for local governments. For example, Section 1011.051, Florida Statutes, requires each district school board to maintain a General Fund ending fund balance that is sufficient to address normal contingencies. The law provides that if at any time the portion of the district school board's General Fund's ending fund balance not classified as restricted, committed, or nonspendable in the approved operating budget is projected to fall below three percent of projected General Fund revenues during the current fiscal year, the superintendent must provide written notification to the district school board and the Commissioner of Education. If the level is projected to fall below two percent, and the district school board does not have a plan that is reasonably anticipated to avoid a financial emergency, the Commissioner of Education must appoint a financial emergency board.

Without an adequate General Fund unrestricted fund balance there is an increased risk that a local government will not have the available resources to mitigate current and future risks (e.g., revenue shortfalls and unanticipated expenditures).

Recommendation: The Legislature should consider enacting a law that requires local governments to adopt a minimum General Fund unrestricted fund balance policy or to maintain a certain level of General Fund unrestricted fund balance.

Budget Transparency

Finding No. 7: Budget Transparency

Pursuant to Florida budget transparency laws,²⁷ local governments must adopt budgets at the level of detail required for the annual financial report under Section 218.32, Florida Statutes, and post on their Web sites tentative budgets, final budgets, and certain budget amendments. If a municipality or special district does not have an official Web site, it may post on the county or counties in which the municipality is located, or the local general purpose government or governments in which the special district is located.

In August 2014, we reviewed compliance with the budget transparency requirements for 35 local governments (15 municipalities, 15 special districts, and 5 counties). In doing so, we determined whether the local governments posted tentative and final budgets for the 2013-14 fiscal year, and whether budget amendments for the 2012-13 fiscal

²⁶ Sections 1011.051, 1011.40(2), and 1011.84(3)(e), Florida Statutes.

²⁷ Sections 129.03(3)(c), 129.06(2)(f)(2), 166.241(3), 166.241(5), 189.016(4), 189.016(7), 373.536(5)(d), and 373.536(6)(d), Florida Statutes (2014).

year were posted when required. We noted that as of the date of our review, 26 (74 percent) of the 35 local governments had not complied with the budget transparency requirements, as follows:

- Two special districts did not post the 2013-14 fiscal year tentative or final budgets on their Web sites.
- Twenty local governments (1 county, 8 municipalities, and 11 special districts) had the 2013-14 fiscal year final budgets posted on their Web site but not the 2013-14 fiscal year tentative budgets.
- One county had posted its 2013-14 fiscal year tentative budget but not its 2013-14 fiscal year final budget on its Web site.
- Fifteen local governments (2 counties, 11 municipalities, and 2 special districts) did not post required amendments for their 2012-13 fiscal year budgets on their Web sites, although their 2012-13 fiscal year audit reports indicated that such amendments were adopted.
- For one municipality without a Web site, no budgetary information was posted on the Web site of the county where the municipality is located.

Providing the required budgetary information enhances citizen involvement and the ability to analyze, monitor, and evaluate budget outcomes. However, we noted that the budget transparency laws do not specify how many years or months that the tentative budget, final budget, and budget amendments must be posted on a local government's Web site. Additionally, while Section 11.45(7)(i), Florida Statutes, requires us to annually transmit by July 15, to the President of the Senate, the Speaker of the House of Representatives, and the Department of Financial Services, a list of all school districts, charter schools, charter technical career centers, Florida College System institutions, State universities, and water management districts that have failed to comply with transparency requirements, no such notification is required regarding noncompliant counties, municipalities, and special districts other than water management districts. Establishing uniform time periods for local governments to post these items on their Web sites and requiring notification of all noncompliant local governments would promote more uniform budget transparency.

Recommendation: Local governments should ensure that tentative and final budgets, as well as certain budget amendments, are posted to their Web sites as required by law. The Legislature should consider revising the budget transparency laws to specify time periods for the tentative budget, final budget, and budget amendments to remain on a local government's Web site. The Legislature should also consider revising Section 11.45(7)(i), Florida Statutes, to require notification of all local governments that fail to comply with transparency requirements.

Florida Department of Management Services, Division of Retirement
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Finding No. 8:	Database of Municipalities and Special Districts
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Part VII of Chapter 112, Florida Statutes, provides for the operation and funding of public employee retirement systems and plans, and requires each system and plan to have regularly scheduled actuarial reports prepared and certified by an enrolled actuary (Section 112.63(1), Florida Statutes). The frequency of the actuarial reports is to be at least every three years commencing from the last actuarial report of the plan or system, and the actuarial report is to be furnished to the Florida Department of Management Services, Division of Retirement (DMS), within 60 days after receipt from the actuary (Section 112.63(2), Florida Statutes). Additionally, actuarial impact statements of proposed changes to local retirement systems are to be furnished to the DMS (Section 112.63(3), Florida Statutes). Upon receipt of the actuarial report or actuarial impact statement, the DMS is to acknowledge such receipt, but must review and comment on each retirement system's or plan's actuarial valuations at least on a triennial basis (Section 112.63(4), Florida Statutes). The DMS maintains a database to track local retirement systems plans and its review activities related to those plans.

Section 112.665(1)(a), Florida Statutes, requires the DMS to gather, catalog, and maintain complete, computerized data information on all public employee retirement systems or plans in the State. The DMS e-mailed surveys, requesting information regarding employee retirement systems or plans, to all municipalities listed in the Florida League of Cities' directory and to all special districts listed on the Department of Economic Opportunity (DEO) Web site, for which an email address was known, on August 8, 2014. According to DMS staff, this was the first time the DMS surveyed local governments requesting information regarding employee retirement systems or plans since 2010.

According to DMS and DEO records, there were 47 entities that were newly created and 6 that had switched from an existing local pension plan to the Florida Retirement System (FRS) during the period July 1, 2011, through August 12, 2014. Our review disclosed that 49 of the 53 entities were contacted from 94 days to 1,123 days after their creation or their change from a local pension plan to the FRS, with an average of 612 days. The DMS was unable to send e-mails to the remaining 4 entities because the entities did not have e-mail addresses on file with the DMS; however, the DMS indicated that it would send hard copies of the survey to these entities after completing its e-mail surveys. Without timely information, the DMS cannot effectively monitor local governments' compliance with the actuarial report and impact statement submission requirements.

Recommendation: The DMS should enhance its procedures to ensure that it timely contacts entities that change to the FRS to determine if local plans are still in effect and any newly created entity to obtain data on all public employee retirement systems or plans as soon as possible after the creation of the entity.

Auditor Selection Process

Local government audits provide independent assessments as to the accuracy and completeness of the financial statements and are usually considered to be vital to the development of local government bond ratings by the bond rating services, which can significantly impact the entity's bond issuance costs. In addition, audits provide a means for evaluating the effectiveness of a local government's internal controls and determining the extent to which the entity has complied with applicable laws, rules, regulations, contracts, grant agreements, and other guidelines.

Recognizing the importance of audits, the Legislature has established general provisions for audits of local governments. Section 218.39(1), Florida Statutes, requires each county, and each municipality and special district with certain revenue or expenditure totals, that have not been notified as of July 1 in any fiscal year that a financial audit will be performed by the Auditor General, to obtain an annual financial audit of its accounts and records. The audit is to be performed by an independent certified public accountant retained by the local government and paid from public funds.

Section 218.391, Florida Statutes, establishes required procedures for the selection of auditors to perform the annual financial audits required by Section 218.39, Florida Statutes. We reviewed the auditor selection process at 30 local governments, consisting of 15 municipalities and 15 special districts, to determine whether local governments were complying with the requirements of Section 218.391, Florida Statutes, and the extent to which they followed guidance published by the GFOA. Finding Nos. 9 through 11 below described the results of our review for the 30 local governments.

Finding No. 9: Audit Committee Membership

Section 218.391(2), Florida Statutes, requires the local government's governing body to establish an audit committee. The composition of the audit committee is not specified in law, except that the composition of a noncharter county, at a minimum, must include each of the county officers elected pursuant to Article VIII, Section 1(d) of the State

Constitution, or a designee, and one member of the board of county commissioners or its designee. The primary purpose of the audit committee is to assist the governing body in selecting an auditor to conduct the annual financial audit; however, the audit committee may serve other audit oversight purposes, as determined by the entity's governing body.

Legal Compliance. Of the 30 entities we reviewed, 2 (6 percent) entities (1 municipality and 1 special district) did not establish an audit committee, contrary to law.

Non-mandatory Guidance. According to the GFOA's publication, *An Elected Official's Guide to Audit Committees (Guide)*, no member of the governing body or delegate who exercises financial management responsibilities should serve as a member of the audit committee. Of the 30 entities reviewed, the audit committees for 11 (37 percent) of the entities (6 municipalities and 5 special districts) included at least one member who exercised financial management responsibilities.

The GFOA's *Guide* also recommends that the audit committee membership be composed of the governing body or a subset of the governing body. We noted that the audit committees for 4 entities (3 municipalities and 1 special district) did not include any member of the governing body.

As indicated in the *Guide*, an audit committee helps to preserve and enhance the objectivity and independence of the financial statement audit by furnishing a forum in which the independent auditors can candidly discuss audit-related matters with members of the governing board apart from management. Based upon the membership deficiencies noted above, some local government audit committees may not be functioning in a prudent manner.

Recommendation: The Legislature should consider revising Section 218.391(2), Florida Statutes, to specify the composition of the audit committee for local governments other than noncharter counties. Local governments should ensure that an audit committee is established as required by law.

Finding No. 10: Audit Services Contracts

Section 218.391(7), Florida Statutes, requires that every procurement of audit services be evidenced by a written contract embodying all provisions and conditions of the procurement of such services. An engagement letter signed and executed by both parties shall constitute a written contract. The written contract must, at a minimum, include the following:

- A provision specifying the services to be provided and fees or other compensation to be paid for such services;
- A provision requiring that invoices for fees or other compensation be submitted in sufficient detail to demonstrate compliance with the terms of the contract; and
- A provision specifying the contract period, including renewals, and conditions under which the contract may be terminated or renewed.

Legal Compliance. Our review of the 30 contracts for audit services disclosed that the contracts specified the services to be provided and the fees or other compensation for such services. However, we noted the following:

- Six (20 percent) did not include a provision requiring that invoices for fees or other compensation (e.g., travel reimbursements, copy charges, telephone calls, etc.) be submitted in sufficient detail to demonstrate compliance with the terms of the contract.
- Four (13 percent) did not specify a finite contract period.
- Four (13 percent) did not specify the conditions under which the contract may be terminated or renewed.

Our review of the invoices submitted for the 30 contracts discussed above disclosed the following:

- Invoices submitted for 15 (50 percent) of the 30 contracts did not provide sufficient detail to determine whether the fees charged were consistent with the fees specified in the contract. In addition, 14 of these contracts were on a “not to exceed” basis, but the invoices were only for progress billing with no detail as to the staff level and hours. The other contract stated that payment would be based on the pay rates of audit firm staff positions working on the audit; however, the local government was only billed the maximum fee.
- Invoices submitted for 2 (7 percent) of the 30 contracts did not include documentation supporting the actual cost incurred for reimbursable costs.

Absent comprehensive written contracts for auditing services and detailed billings, local governments cannot be assured that invoices for services are in accordance with the contract. Additionally, failure to monitor contract invoices and payments increases the risk of over payments.

Recommendation: Local governments should ensure that contracts for audit services include the provisions required by law and that invoices comply with terms of the contract prior to payment.

Finding No. 11: Auditor Selection Procedures

Local governments, prior to entering into a written contract for audit services, must use the auditor selection procedures prescribed in Section 218.391, Florida Statutes, when selecting an auditor to conduct the annual financial audit. The law requires local governments to select an audit committee, assigns certain responsibilities to the audit committee in evaluating and recommending an auditor for the annual financial audit, and specifies certain provisions that must be included in the written contract for audit services.

Of the 30 local governments reviewed, 9 (30 percent) of the entities (4 municipalities and 5 special districts) did not use the auditor selection procedures prescribed in Section 218.391, Florida Statutes, to select an auditor for the 2012-13 fiscal year annual financial audit, as follows:

- As noted in finding No. 10, contracts for 4 (13 percent) entities did not specify a finite contract period. For these 4 entities, an auditor selection process had not been conducted since 1998, 2003, 2006, and 2010, respectively.
- Five (17 percent) of the entities (3 municipalities and 2 special districts) improperly extended the original contract as the original contract did not contain renewal provisions.

Properly performed audits play a vital role in the public sector by helping to preserve the integrity of the public finance functions and, thereby, maintaining citizens’ confidence in their elected leaders. The use of an objective auditor selection process ensures selection of a qualified auditor and satisfactory audit effort.

Recommendation: The Legislature should consider amending Section 218.391, Florida Statutes, to require local governments to perform auditor selection procedures at specified intervals. The Legislature should also consider establishing provisions in law to encourage local governments to comply with the auditor selection procedures in Section 218.391, Florida Statutes.

Tangible Personal Property

Finding No. 12: Tangible Personal Property

Recognizing the importance of accountability over tangible personal property, the Legislature has established general provisions for tangible personal property owned by local governments in Section 274, Florida Statutes. Although “local governmental entity” is generally defined in Section 218.31, Florida Statutes, as a county agency, a municipality,

or a special district for purposes of many financial reporting requirements, Section 274.01(1), Florida Statutes, defines “governmental unit” as the governing board, commission, or authority of a county or taxing district of the State or the sheriff of the county.

Section 274.02(2), Florida Statutes, gives the State of Florida’s Chief Financial Officer (CFO) the authority to establish requirements for the recording of tangible personal property and for the periodic review of property for inventory purposes. The CFO established these requirements in Department of Financial Services (DFS) Rules, Chapter 69I-73, Florida Administrative Code (FAC), which provides:

- All property with a value or cost of \$1,000 or more and a projected useful life of one year or more must be recorded in the local government’s financial system as property for inventory purposes.
- Each property item must be permanently marked with the identification number assigned to that item to establish its identity and ownership by the local governmental unit holding title to the item. The property records must contain sufficient descriptive data to permit positive identification of the property items including an identification number; date acquired; cost or value; physical location of the item; and year, model, and manufacturer, if applicable.
- The authority for disposition of capital assets must be recorded on the individual property record (resolution of the governing body properly recorded in the minutes as required by Section 274.07, Florida Statutes).
- There must be a complete physical inventory of all property annually and whenever there is a change of custodian or change of custodian’s delegate.

Although not subject to the requirements of Chapter 274, Florida Statutes, or the DFS Rules stated above, we reviewed the tangible personal property procedures at 30 local governments, consisting of 15 municipalities and 15 special districts (all non-taxing districts), to determine the extent to which these local governments’ procedures provided for accountability and safeguarding of tangible personal property. Our review, disclosed the following:

- Ten (33 percent) entities (6 municipalities and 4 special districts), did not have any written policies and procedures covering tangible personal property. To ensure proper accountability over tangible personal property, each local government should develop written policies and procedures providing for accountability over tangible personal property.
- We selected 464 property items recorded in the property records of the 30 entities. Of the 464 items, 41 (9 percent) were not sufficiently described in the property records to permit positive identification of the property items. For example, for 13 property items, the property records did not indicate an identification number or serial number. Also, 127 (31 percent) of the 464 items were not appropriately marked as local government property with an assigned identification number. Providing sufficient detail in the property records and appropriately marking property with an identification number provides additional assurance that all property items have been recorded and accounted for, and helps in reconciling the physical inventory with the property records.
- Twenty-eight entities (15 municipalities and 13 special districts) had procedures that required approval prior to the disposition of property. However, 11 (39 percent) of those entities (8 municipalities and 3 special districts) had procedures that allowed someone other than the governing board or commission the authority to authorize the disposal of property. For proper control and accountability over property, the governing body should have the final approval of any property disposals.
- Fifteen (50 percent) entities (8 municipalities and 7 special districts) did not perform a complete physical inventory of all property during the 2012-13 fiscal year, including one entity that had not performed a complete physical inventory since 2005. For 2 of the 15 entities, the physical inventory counts were not reconciled to the local governments’ property records. We also noted that of the 20 entities that had written policies and procedures for tangible personal property, the policies and procedures for 4 (25 percent) entities (1 municipality and 3 special districts) did not require an annual inventory. Effective controls over property

include comparisons of detailed property records with existing assets at reasonable intervals, and appropriate action with respect to any differences.

Chapter 274, Florida Statutes, and DFS Rules, Chapter 69I-73, FAC, provide requirements for good stewardship for tangible personal property owned by counties and taxing districts. It is not apparent why these requirements are not also applicable to municipalities and special districts that do not levy taxes. Given the above-noted issues disclosed by our audit, making these requirements applicable to all local governments may ensure better accountability for tangible personal property owned by municipalities and non-taxing districts.

Recommendation: Local governments should establish written policies and procedures providing for accountability over tangible personal property and addressing the above-noted control deficiencies. The Legislature should consider revising the definition of “governmental unit” in Section 274.01, Florida Statutes, to include all “local governmental entities” as that term is defined in Section 218.31, Florida Statutes.

Local Government Bond Issues

Section 218.38, Florida Statutes, requires local governments to furnish the Florida State Board of Administration’s Division of Bond Finance (Division) a complete description of new general obligation and revenue bonds, including advance notice of the impending sale of any new issues, and a copy of the final official statement, if any. The law also provides that certain information be provided to the Division within 120 days after delivery of the bonds.

Based on information obtained from the Division, we identified bonds issued during the 2012-13 fiscal year and selected 25 of these bond issues for our review of the bond issue process. The 25 bond issues totaled approximately \$1.3 billion, as shown in the following tabulation:

Entity Type	Number of Bond Issues Selected	Amount of Bonds Selected
Municipalities	11	\$257,762,807
Special Districts	14	1,018,535,000
Total	25	\$1,276,297,807

Source: Division of Bond Finance

Finding No. 13: Method of Sale for Local Government Bond Issues

There are essentially three methods by which bonds are sold: competitive bids, negotiated sale, and private placement. In a competitive bid sale, the issuer solicits bids from underwriting firms and sells the bonds to the firm offering the lowest true interest cost bid. In a negotiated sale, an underwriting firm is selected early in the process and the underwriter assists the issuer in all steps. At the time the bonds are sold, the issuer negotiates a purchase price for the bonds with the underwriter. In a private placement (a type of negotiated sale), the issuer sells the bonds directly to investors without a public offering, although underwriting firms may be actively involved in placing the bonds on behalf of the issuer.

The GFOA recommends that state and local government bond issuers sell their debt using the method of sale that is most likely to achieve the lowest cost of borrowing while taking into account both short-range and long-range implications for taxpayers and ratepayers. Issuers should select a method of sale based on a thorough analysis of the relevant rating, security, structure, and other factors pertaining to the proposed bond issue. If the entity has in-house

expertise, defined as dedicated debt management staff whose responsibilities include daily management of a debt portfolio, this analysis and selection could be made by the entity's staff. However, in the more common situation where an entity does not have sufficient in-house expertise, this analysis and selection should be undertaken in partnership with a financial advisor. Due to the inherent conflict of interest, the GFOA recommends that issuers not use a broker/dealer or potential underwriter to assist in the method of sale selection unless that firm has agreed not to underwrite that transaction.²⁸ Failure to use an independent financial advisor can reduce public confidence in the bond sale process, and may result in the governing body making decisions with respect to the debt issuance that are not in the best interest of the local government.²⁹

The following tabulation provides a breakdown of the total amount issued by method of sale for the 25 bonds issues reviewed:

Method of Sale	Number of Issues	Amount Issued	Percentage
Negotiated (Including Private Placements)	23	\$1,186,647,807	92
Competitive	<u>2</u>	<u>89,650,000</u>	<u>8</u>
Totals	<u>25</u>	<u>\$1,276,297,807</u>	<u>100</u>

Source: Local Government Records

Our review of the 25 bond issuances disclosed the following:

- For 5 (22 percent) of the 23 issues sold by negotiated sale, the local government's records did not evidence the conditions favoring a negotiated sale.
- For 5 (20 percent) of the 25 issues, the local government did not use the services of an outside financial advisor. For 2 of the 20 issues for which the local government employed the services of an outside financial advisor, the financial advisor was not independent of the underwriter (i.e., the financial advisor was involved in underwriting the bond issue).

Section 218.38, Florida Statutes, requires local governments to furnish a complete description of all of its new general obligation bonds and revenue bonds to the Division, and Section 218.385(1), Florida Statutes, requires all local government general obligation bonds and revenue bonds to be sold at public sale by competitive bids unless the governing body determines that a negotiated sale of such bonds is in the best interest of the issuer. However, these laws do not require the local government governing body to document the conditions favoring the selected method of sale and to provide this information to the Division. Further, despite the importance of using an independent financial advisor as discussed above, current law does not require local governments to use a financial advisor, nor does it prohibit the use of the underwriter of a bond issue in determining the method of sale for that bond issue. Failure to use the most appropriate sale method, or an independent financial advisor, may result in unfavorable issue terms or excessive bond issue costs.

Section 218.385(7), Florida Statutes, provides that the failure of a local government to comply with one or more provisions of Sections 218.385 or 218.38, Florida Statutes, shall subject the local government to the sanctions provided in Section 218.38(3), Florida Statutes. Section 218.38(3), Florida Statutes, requires the Division to report to the Legislative Auditing Committee (LAC) local governments that fail to provide information, and the LAC can take action pursuant to Section 11.40, Florida Statutes, to compel the local government to provide such information.

²⁸ GFOA Best Practice: *Selecting and Managing the Method of Sale of Bonds* (2014)

²⁹ GFOA Best Practice: *Selecting and Managing Municipal Advisors* (2014)

Recommendation: To promote public confidence in the bond sale process, and to ensure that an independent and adequate determination is made as to the best bond sale method, the Legislature should consider amending Section 218.385(1), Florida Statutes, to require local governments to use a financial advisor that is independent of the underwriter, or to otherwise demonstrate that the local governments have staff with sufficient expertise to act in a financial advisor capacity. In addition, to ensure that local governments adequately document and justify that a negotiated or private placement sale is the most appropriate type of sale, the Legislature should consider amending Sections 218.38 and 218.385, Florida Statutes, to require local governments to document the conditions favoring this type of sale and provide such documentation to the Division.

Finding No. 14: Selection of Bond Professionals

Various Florida laws establish provisions that local governments are required to follow in the procurement of professional services. For example, Section 218.391, Florida Statutes, provides for the selection of financial auditors, while Section 287.055, Florida Statutes, addresses the acquisition of professional architectural, engineering, landscape architectural, surveying and mapping services. However, Florida law generally does not provide similar guidance regarding the procurement of financial and professional services for local government general obligation and revenue bond issues.

Governments typically employ a number of professionals to assist them in the bond process, primarily a financial advisor, an underwriter, and bond counsel. As discussed above, financial advisors can be used in determining the bond sale method and may have various other roles depending on which sale method is selected.³⁰ The primary role of the underwriter in a negotiated sale is to market the issuer's bonds to investors. Assuming that the issuer and underwriter reach agreement on the pricing of the bonds at the time of sale, the underwriter purchases the entire bond issue from the issuer and resells the bonds to investors.³¹ Bond counsel renders an opinion on the validity of the bond offering, the security for the offering, and whether and to what extent interest on the bonds is exempt from income and other taxation. The opinion of bond counsel provides assurance both to issuers and to investors who purchase the bonds that all legal and tax requirements relevant to the matters covered by the opinion are met.³²

GFOA recommends that issuers select financial advisors, underwriters, and bond counsel using a competitive process using a Request for Proposal (RFP) or Request for Qualifications (RFQ). Using a competitive process allows the issuer to compare the qualifications of proposers and to select the most qualified firm based on the scope of services and evaluation criteria outlined in the RFP or RFQ. A competitive process also provides objective assurance that the best services and interest rates are obtained at the lowest cost possible and demonstrates that marketing and procurement decisions are free of self-interest and personal or political influences. Furthermore, a competitive process reduces the opportunity for fraud and abuse and is fair to competing finance professionals.³³

Our review of the 25 bond issues disclosed the following:

- For 13 (65 percent) of the 20 issues for which local governments employed the services of an outside financial advisor, the local government did not use a formal RFP or RFQ to select the financial advisor. The 20 financial advisors were paid up to \$91,000 for their services.

³⁰ GFOA Best Practice: *Selecting and Managing Municipal Advisors* (2014)

³¹ GFOA Best Practice: *Selecting and Managing Underwriters for Negotiated Bond Sales* (2014)

³² GFOA Best Practice: *Selecting Bond Counsel* (1998 and 2008)

³³ GFOA Best Practice: *Selecting and Managing Municipal Advisors* (2014); GFOA Best Practice: *Selecting and Managing Underwriters for Negotiated Bond Sales* (2014); GFOA Best Practice: *Selecting Bond Counsel* (1998 and 2008)

- For 12 (55 percent) of the 22 issues sold by negotiated sale or private placement and involving the use of an underwriter, the local government did not use a formal RFP or RFQ to select the underwriter. The 22 underwriters were paid up to \$2,267,000 for their services. Of the remaining 10 issues for which an underwriter was selected by RFP or RFQ, 6 contracts lacked provisions prohibiting the underwriting firm from engaging in activities on behalf of the issuer that would produce a direct or indirect financial gain for the firm, other than agreed-upon compensation, without the issuer's informed consent.
- For 18 (72 percent) of the 25 issues, the local government did not use a formal RFP or RFQ to select the bond-related counsel. The 25 bond counsels were paid up to \$220,000 for their services. Of the remaining 7 issues for which bond-related counsel was selected by RFP or RFQ, 2 contracts did not require disclosure of relationships or activities that might present a conflict of interest.

The majority of local governments that did not use a formal RFP or RFQ to select bond counsel, financial advisors, or underwriters stated that they selected the same professionals as used in the past based on their qualifications or familiarity with the entity or entity staff, or the bond professionals were selected by the entity's governing body or legal staff.

Recommendation: Local governments employing the services of underwriters should include contract provisions that prohibit the firm from engaging in activities on their behalf that produces financial gain for the firm other than agreed-upon compensation. Local governments employing the services of bond-related counsel should include contract provisions that require the firm to disclose relationships or activities that might present a conflict of interest. To ensure that qualified financial and professional services are acquired at the lowest possible cost consistent with the size, nature, and complexity of the bond issue, the Legislature should consider amending Section 218.385, Florida Statutes, to require local governments to select financial advisors and bond counsels using a competitive selection process whereby RFPs or RFQs are solicited from a reasonable number of professionals and, for negotiated bond issues, to use RFPs to solicit qualified underwriting firms to serve as the underwriter.

Finding No. 15: Florida State Board of Administration's Division of Bond Finance Newsletter

Section 218.37(1)(f), Florida Statutes, requires the Florida State Board of Administration's Division of Bond Finance (Division) to issue a regular newsletter to issuers, underwriters, attorneys, investors, and other parties within the bond community and the general public containing information of interest relating to local and State bonds and authorizes the Division to charge fees for subscriptions to the newsletter. Through inquiry with Division management, we determined that the Division is no longer publishing the newsletter due to a lack of resources and availability of the same information at no cost on the Internet. For example, the Municipal Securities Rulemaking Board's Electronic Municipal Market Access Web site provides extensive information relating to bond issues, including an educational section and an extensive glossary of terms relating to bonds.

Recommendation: The Legislature should consider repealing Section 218.37(1)(f), Florida Statutes, to no longer require the Division to issue a newsletter.

Special District Determinations
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Finding No. 16: Determination of Special Districts

Pursuant to Section 189.012(6), Florida Statutes, the term "special district" means "a unit of local government created for a special purpose, as opposed to a general purpose, which has jurisdiction to operate within a limited geographic boundary and is created by general law, special act, local ordinance, or rule of the Governor and Cabinet. The term

does not include a school district, a community college district, a special improvement district created pursuant to Section 285.17, Florida Statutes, a municipal service taxing or benefit unit as specified in Section 125.01, Florida Statutes, or a board which provides electrical service and which is a political subdivision of a municipality or is part of a municipality.”

Entities determined to be special districts must comply with the creation, dissolution, and reporting requirements set forth in Chapter 189, Florida Statutes. For example, special districts are required to:

- Provide information to the DEO such as creation documents, maps and boundaries, and a written statement that includes a reference to the status as dependent or independent and the basis for such classification.
- Designate a registered office and a registered agent and file such information with the local governing authority and the DEO.
- Adopt a budget for each fiscal year by resolution in a prescribed format.
- Post the tentative and final budgets and budget amendments to the special district’s Web site or the Web site of the local governing authority.
- Comply with various financial reporting requirements, such as requirements to submit an annual financial report to DFS and, if required, a financial audit report to the Auditor General. Additionally, special districts are subject to consequences if they fail to comply with the financial reporting requirements.

While Section 189.016, Florida Statutes, provides the DEO the authority to determine whether a special district’s status should be classified as dependent or independent, the DEO has not been granted the authority to determine whether an entity is a special district. The DEO has occasionally requested information from entities that appear to meet the definition of a special district and has been advised by the creators of the entities that they are not special districts. In these cases, the DEO has no authority to require these entities to file required information or add them to the list of special districts.³⁴ For example, the Pinellas County Construction Licensing Board and the Palm Beach County Construction Industry Licensing Board both appear to be special purpose entities that operate within a limited geographical boundary and were created by special act. Although the Pinellas County Construction Licensing Board is considered a special district, the Palm Beach County Construction Industry Licensing Board is not. The determinations as to whether they were special districts were made by the entities rather than the DEO.

Providing the DEO with the authority to determine whether an entity is a special district will ensure that entities that should be so classified comply with the accountability and oversight provisions in Chapter 189, Florida Statutes.

Recommendation: **The Legislature should consider revising Chapter 189, Florida Statutes, to provide the DEO authority to determine whether an entity is a special district.**

OBJECTIVES, SCOPE, AND METHODOLOGY

The Auditor General conducts audits of governmental entities to provide the Legislature, Florida’s citizens, public entity management, and other stakeholders unbiased, timely, and relevant information for use in promoting government accountability and stewardship and improving government operations.

We conducted this performance audit from March through September 2014 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives.

³⁴ Pursuant to Section 189.064(2), Florida Statutes, the Special District Accountability Program within the DEO is required to maintain an official list of special districts. This list is used by other State agencies to which special districts are required to report.

We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

This performance audit's overall objective was to determine the accuracy, efficiency, and effectiveness of the System in achieving its goals. This included:

- Documenting our understanding of managements controls relevant to the operations of selected local government financial reporting system administrative responsibilities. Our purpose in obtaining an understanding of management controls and making judgments with regard thereto was to determine the nature, timing, and extent of substantive audit tests and procedures to be performed.
- Evaluating selected managements' performance in administering assigned local government financial reporting system responsibilities in accordance with applicable laws, rules, and other guidelines.
- Determining the extent to which selected management controls promoted and encouraged the achievement of management's control objectives in the categories of compliance with applicable laws, rules, and other guidelines; the economic and efficient administration of the assigned functions; and the safeguarding of assets.
- Evaluating the adequacy and appropriateness of local government financial reporting system laws related to the scope of this audit.

This audit was designed to identify, for those programs, activities, or functions included within the scope of the audit, deficiencies in management's internal controls, instances of noncompliance with applicable laws, rules, policies, and other guidelines, and instances of inefficient or ineffective operational policies, procedures, or practices. The focus of this audit was to identify problems so that they may be corrected in such a way as to improve government accountability and efficiency and the stewardship of management. Professional judgment has been used in determining significance and audit risk and in selecting the particular transactions, legal compliance matters, records, and controls considered.

For those programs, activities, and functions included within the scope of our audit, our audit work included, but was not limited to, communicating to management and those charged with governance the scope, objectives, timing, overall methodology, and reporting of our audit; obtaining an understanding of the program, activity, or function; exercising professional judgment in considering significance and audit risk in the design and execution of research, interviews, tests, analyses, and other procedures included in the audit methodology; obtaining reasonable assurance of the overall sufficiency and appropriateness of the evidence gathered in support of our audit's findings and conclusions; and reporting on the results of the audit as required by governing laws and auditing standards.

This scope of this audit focused on certain activities performed by the Florida Department of Management Services and local governments, and a review and evaluation of certain laws relating to local governments.

Specific scope and audit procedures applied relative to this audit were:

Community Redevelopment Agencies

Determined whether laws pertaining to CRAs adequately provided guidance regarding the operation of, and accountability for, CRAs. In conducting the audit, we:

- Reviewed results of special audits of CRAs for possible recommended law changes.
- Interviewed appropriate stakeholders for input on recommended law changes governing CRAs.
- Tested 60 CRAs' compliance with Section 163.387(8), Florida Statutes.

Unrestricted Fund Balance in the General Fund

Determined whether local governments were maintaining adequate levels of unrestricted fund balance for the General Fund. In conducting the audit, we:

- Determined whether local governments had established policies that are consistent with the GFOA's best practice recommendations regarding minimum level of unrestricted fund balance in the General Fund.
- Calculated the percentage of reported General Fund unrestricted fund balance to total revenues and total expenditures to determine whether local governments reported the minimum level (unassigned and assigned) recommended by GFOA as of September 30, 2013.

Budgetary Compliance

Determined whether local governments complied with the budgetary requirements in law. In conducting the audit, we determined whether local governments adopted their 2012-13 fiscal year budgets at the required level of detail and whether they posted certain 2012-13 and 2013-14 fiscal year budget-related documents on their Web sites.

Florida Department of Management Services, Division of Retirement

Determined whether the DMS took adequate corrective actions for finding Nos. 11 and 12 in report No. 2011-196. In conducting the audit, we:

- Reviewed the responsibilities of the Division as they relate to contacting newly created entities or entities that changed to the Florida Retirement System from a local plan.
- Determined whether DMS properly withheld insurance premium tax money from police and firefighter retirement plans when the actuarial reports had not been State accepted.

Financial Disclosure Forms

Determined whether local governments notify the Commission on Ethics of individuals required to file statements of financial interests. In conducting the audit, we selected 35 local governments (5 counties, 15 municipalities, and 15 special districts) and determined whether the names of individuals required to file statements of financial interests were communicated to the Commission on Ethics.

Auditor Selection Process

Determined whether local governments had adequate controls and procedures regarding the selection of auditors to conduct financial audits pursuant to Section 218.39, Florida Statutes. In conducting the audit, we selected 30 local governments (15 municipalities and 15 special districts) and:

- Reviewed the local governments' auditor selection process.
- Determined whether the local governments complied with Section 218.391, Florida Statutes, and GFOA best practices in selecting their financial auditors.

Tangible Personal Property

Determined whether municipalities and special districts had adequate controls and procedures over tangible personal property. In conducting the audit, we selected 30 local governments (15 municipalities and 15 special districts) and:

- Reviewed the local governments' controls over tangible personal property and compared their policies and procedures to Department of Financial Services' Rules Chapter 69I-73, Florida Administrative Code, requirements for counties and taxing districts.

- Determined whether tangible personal property was recorded in the property records and inventoried, results of the inventory compared to the property records, and differences appropriately investigated and resolved.

Local Government Bond Issues

Determined whether local governments had adequate controls and procedures over issuance of bonds. In conducting the audit, we selected 25 local governments (11 municipalities and 14 special districts) that issued long-term debt during the 2012-13 fiscal year and:

- Obtained bond issuance information from the Division of Bond Finance to quantify debt issued and related costs.
- Determined whether the local governments followed GFOA best practices when issuing long-term debt.

Travel Policies

Determined whether local government travel policies were reasonable. In conducting the audit, we selected 30 local governments (15 municipalities and 15 special districts) and reviewed the local government's travel policies for reasonableness.

Special District Governing Body and Management Benefits

Determined whether benefits paid to special district governing body members and management were reasonable. In conducting the audit, we selected 50 special districts and evaluated the benefits paid to both governing body members and management staff for reasonableness.

Determination of Special Districts

Evaluated the determination of special districts. In conducting the audit, we:

- Reviewed laws applicable to special districts.
- Obtained listings of non-districts and special districts and analyzed.
- Discussed special district determinations with Department of Economic Opportunity staff.

Unless otherwise indicated in this report, records and transactions were not selected with the intent of projecting the results, although we have presented for perspective, where practicable, information concerning the relevant population value or size and quantifications relative to the items selected for examination.

AUTHORITY

Pursuant to the provisions of Section 11.45(2)(g), Florida Statutes, I have directed that this report be prepared to present the results of our performance audit of the local government financial reporting system.



David W. Martin, CPA
Auditor General

MANAGEMENT'S RESPONSE

The Florida Department of Management Services' response to finding No. 8 is included as Exhibit A.

EXHIBIT A
MANAGEMENT'S RESPONSE



4050 Esplanade Way
Tallahassee, FL 32399-0950
Tel: 850-488-2786 | Fax: 850-922-6149

Rick Scott, Governor

Craig J. Nichols, Agency Secretary

October 27, 2014

Mr. David W. Martin, CPA
Auditor General
G74 Claude Pepper Building
111 West Madison Street
Tallahassee, Florida 32399-1450

Dear Mr. Martin:

Pursuant to subsection 11.45(4)(d), Florida Statutes, this is our response to your report, ***Audit of Local Government Financial Reporting Systems***. Our response corresponds with the finding and recommendation related to the Department of Management Services contained in the draft report.

If further information is needed concerning our response, please contact Walter Sachs, Inspector General, at 488-5285.

Sincerely,

A handwritten signature in black ink, appearing to read 'Craig J. Nichols', is written over a faint, larger version of the same signature.

Craig J. Nichols
Agency Secretary

Attachment

cc: Darren Brooks, Deputy Secretary, Workforce Operations
Dan Drake, Director of State Retirement Division
Elizabeth Stevens, Assistant Director of Statement Retirement Division
Walter Sachs, Inspector General
Yolanda Lockett, Audit Director

EXHIBIT A (CONTINUED)
MANAGEMENT'S RESPONSE



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Rick Scott, Governor

Craig J. Nichols, Agency Secretary

Department of Management Services' Response
 To the Auditor General's Local Government Financial Reporting Systems Audit

Finding No. 8: Database of Municipalities and Special Districts

The Florida Department of Management Services needed to enhance its procedures to ensure timely contact of newly created local government entities, to timely obtain data on retirement systems or plans, and timely contact of entities that change to the Florida Retirement System from a local plan.

Recommendation:

The DMS should enhance its procedures to ensure that it timely contacts entities that change to the FRS to determine if local plans are still in effect and any newly created entity to obtain data on all public employee retirement systems or plans as soon as possible after the creation of the entity.

Response:

☒ **Concur**

☐ **Non-Concur**

While DMS agrees that more frequent surveys would further mitigate the risk of missing pension plans in the database, based on the 2014 survey responses, none of the identified new districts had created a pension plan for their employees, and currently only 47 out of more than 1,600 total special districts sponsor such a plan (less than 3%). In recent years, the definite trend has been away from establishing new pension plans. Although the risk of missing a new pension plan is low, DMS will establish a procedure to perform local government surveys at least on a triennial basis going forward. Also, DMS will implement a procedure to contact new local government entities within one year of creation.

It should also be noted that when a city or special district initiates participation in the Florida Retirement System (FRS), all future hires are mandatory FRS members. Existing local plan members are given an option to remain in the local plan or join FRS for future service. Depending on individual ballots, the local plan may be terminated, closed or transferred to a substituted trust fund. The Bureau of Enrollment and Contributions in DMS regularly communicates with the Bureau of Local Retirement Systems during the FRS enrollment process. Depending on the disposition of the local plan, which is communicated to DMS during the enrollment process, the Bureau of Local Retirement Systems amends the database to reflect the plan's current status. Consequently, there is low risk that a local plan will be improperly identified in the database following a switch to FRS.