Identifying Local Fiscal Distress

August 21, 2017
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Auditor of Public Accounts
Locality Audit Requirements (new)

• Locality contracts for audit by April 1
• Locality submits audited CAFR and Comparative Report Transmittal form by November 30
• CPA firm presents audit to local governing body by December 31 and sends notarized statement to APA that this was done
• All matters communicated to the governing body by the CPA must be in writing
Locality Audit Requirements, cont. (new)

• APA to establish a prioritized early warning system
• APA to notify localities where we make a preliminary determination of potential fiscal distress
  – Based upon request of local governing body or CEO, APA may conduct a review and request additional information
  – Based on results of review, APA shall notify the Governor and chairs of the money committees if APA is of the opinion that state assistance, oversight or targeted intervention is needed
APA Work Group

• Established a work group to develop the criteria
  – Secretary of Finance
  – Staff Directors for HAC and SFC
  – Commission on Local Government
  – Virginia Association of Counties
  – Virginia Municipal League
  – Governor’s Deputy Chief of Staff
APA New Process

• APA calculates 10 ratios using information in the CAFR
• APA ranks each locality’s performance by ratio and converts into percentile rankings
• APA uses average of the percentile rankings to determine a Financial Assessment Model (FAM) score
• APA use the FAM score to determine need for follow-up
Scoring

- Ratios are accumulated for each locality and FAM score calculated.
- Will build a database over time that will have several years worth of data - 2014, 2015, 2016 for now.
- Will set a cutoff point to perform follow up procedures - for 2016, cutoff is overall score of less than 16%.
- APA will also select localities qualitatively based on significant trends or other information available.
City of Petersburg Graph

Petersburg- FAM Scores

<table>
<thead>
<tr>
<th>Year</th>
<th>FAM Score</th>
<th>Needs Follow-up</th>
</tr>
</thead>
<tbody>
<tr>
<td>2014</td>
<td>13.93%</td>
<td>16%</td>
</tr>
<tr>
<td>2015</td>
<td>7.31%</td>
<td>16%</td>
</tr>
<tr>
<td>2016</td>
<td>4.48%</td>
<td>16%</td>
</tr>
</tbody>
</table>
Graphs for Localities Selected for Review

City A - FAM Scores

<table>
<thead>
<tr>
<th>Year</th>
<th>FAM Score</th>
<th>Needs Follow-up</th>
</tr>
</thead>
<tbody>
<tr>
<td>2014</td>
<td>9.38%</td>
<td>16%</td>
</tr>
<tr>
<td>2015</td>
<td>10.87%</td>
<td>16%</td>
</tr>
<tr>
<td>2016</td>
<td>4.25%</td>
<td>16%</td>
</tr>
</tbody>
</table>

FAM Score vs Needs Follow-up
# Graphs for Localities Selected for Review

## City B - FAM Scores

<table>
<thead>
<tr>
<th></th>
<th>2014</th>
<th>2015</th>
<th>2016</th>
</tr>
</thead>
<tbody>
<tr>
<td>FAM Score</td>
<td>49.30%</td>
<td>13.06%</td>
<td>13.73%</td>
</tr>
<tr>
<td>Needs Follow-up</td>
<td>16%</td>
<td>16%</td>
<td>16%</td>
</tr>
</tbody>
</table>

![Graph showing FAM Scores over years](image)

- **FAM Score**
- **Needs Follow-up**
Graphs for Localities Selected for Review

County A - FAM Scores

<table>
<thead>
<tr>
<th></th>
<th>2014</th>
<th>2015</th>
<th>2016</th>
</tr>
</thead>
<tbody>
<tr>
<td>FAM Score</td>
<td>5.90%</td>
<td>8.23%</td>
<td>7.31%</td>
</tr>
<tr>
<td>Needs Follow-up</td>
<td>16%</td>
<td>16%</td>
<td>16%</td>
</tr>
</tbody>
</table>
Graphs for Localities Selected for Review

County B - FAM Scores

<table>
<thead>
<tr>
<th>Year</th>
<th>FAM Score</th>
<th>Needs Follow-up</th>
</tr>
</thead>
<tbody>
<tr>
<td>2014</td>
<td>21.00%</td>
<td>16%</td>
</tr>
<tr>
<td>2015</td>
<td>15.47%</td>
<td>16%</td>
</tr>
<tr>
<td>2016</td>
<td>11.12%</td>
<td>16%</td>
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</tbody>
</table>

FAM Score

Needs Follow-up
Graphs for Localities Selected for Review

County C- FAM Scores

<table>
<thead>
<tr>
<th></th>
<th>2014</th>
<th>2015</th>
<th>2016</th>
</tr>
</thead>
<tbody>
<tr>
<td>FAM Score</td>
<td>43.11%</td>
<td>29.03%</td>
<td>16.49%</td>
</tr>
<tr>
<td>Needs Follow-up</td>
<td>16%</td>
<td>16%</td>
<td>16%</td>
</tr>
</tbody>
</table>
Notification to Locality

• For localities that have a FAM score that causes concern, notification letter sent to
  – Governing body
  – Management

• Explain the analytical process and the cause for concern

• Explain the follow up process that will be followed

• Explain potential assistance available
Follow up Questions to Localities – Budget Process

- Structurally balanced budget?
- Use of transfers between funds to balance budget?
- Frequent amendments to budget?
- Budget monitoring process
  - Periodic discussions by the governing body
- Any external factors that have impacted your budget for the current fiscal year?
Follow up Questions to Localities – Debt and Borrowing

- Delinquent with any debt service payments to Authorities?
- Compliance with debt covenants?
- Recent change in bond ratings?
- Significant interfund borrowings between General fund and other funds?
  - If so, plans for repayment
- Any Tax or Revenue Anticipation Notes?
  - If so, sufficiency of revenues to repay
Follow up Questions to Localities – Debt and Borrowing, cont.

- Other short-term financing during the year?
  - If so, used for operating expenses?
- Any unusual factors during the year, including external factors, that impacted debt/borrowings?
Follow up Questions to Localities – Expenses and Payables

• Any payments in arrears to vendors or Authorities?

• Age of payables – prompt pay being met?
  – Discussion of age of payables with governing body?

• Delinquent in paying wages or payroll taxes?

• Delinquent in paying VRS, worker’s compensation or health care premiums?
Follow up Questions to Localities – Revenue and Receivables

• Major one-time revenue items
• Any difficulties in collecting receivables?
• Age of accounts receivable, monitoring process
  – Discussion of delinquencies with governing body?
  – Significant increase in delinquencies?
• Any significant revenue shortfalls?
  – Plans by governing body to address
Follow up Questions to Localities – Other Areas

- Vacancies in key positions?
- New systems or technology issues?
- Timely annual audit? If not, why?
- Audit results
  - Unmodified opinion?
  - Material weaknesses or significant deficiencies or other matters in a management letter?
    - Plans for corrective action
  - Emphasis of a matter paragraph/ Going Concern related to potential fiscal stress?
Planned APA Actions

- Follow up with 4 localities based on current FAM
- Follow up with 2 localities based on significant downward trend of FAM over past three years
- Follow up with 2 localities that have not yet submitted their 2016 financial statements
- Letter to other localities to say no follow up planned and offer the tool for self assessment
Possible Future APA actions

- Consider building in external factors to the model
- Dashboard on website with fiscal stress scoring
- Summary report of localities experiencing fiscal stress
QUESTIONS