



CITY OF EVANSTON, ILLINOIS

COMMUNICATION OF DEFICIENCIES
IN INTERNAL CONTROL AND
OTHER COMMENTS TO CITY COUNCIL

For the Year Ended December 31, 2019



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COMMUNICATION OF DEFICIENCIES IN INTERNAL CONTROL AND OTHER COMMENTS TO CITY COUNCIL

Ms. Erika Storlie, Interim City Manager
Mr. Hitesh Desai, City Treasurer/Chief Financial Officer
City of Evanston, Illinois

As part of the annual audit, we are required to communicate internal control matters that we classify as significant deficiencies and material weaknesses to those charged with governance. A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. A material weakness is a deficiency, or a combination of deficiencies in internal control, such that there is a reasonable possibility that a material misstatement of the City's financial statements will not be prevented, or detected and corrected, on a timely basis.

However, during our audit we became aware of several matters that are opportunities for strengthening internal controls and operating efficiency. In addition, we reviewed the status of comments from the December 31, 2018 audit. The status of these comments is included in Appendix A. This letter does not affect our report dated July 14, 2020, on the financial statements of the City.

The City's written responses to these matters identified in our audit has not been subjected to the audit procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

We will review the status of these comments during our next audit engagement. We have already discussed many of these comments and suggestions with Hitesh Desai, City Treasurer/Chief Financial Officer and Andrew Villamin, Accounting Manager and we will be pleased to discuss them in further detail at your convenience, to perform any additional study of these matters, or to assist you in implementing the recommendations.

This memorandum is intended solely for the information and use of management, and is not intended to be, and should not be, used by anyone other than these specified parties.

I encourage you to contact me at (630) 566-8535 should you have any questions.

Sikich LLP

Naperville, Illinois
July 14, 2020

OTHER COMMENTS

1. Deficit Fund Balances

The following deficit balances were reported as of December 31, 2019:

Fund	Deficit
Solid Waste	\$ 298,490
Special Service Area #4	226,193
Internal Service - Insurance	<u>11,593,098</u>
 TOTAL	 <u>\$ 12,117,781</u>

The City should continue to monitor the deficits in the Solid Waste Fund and Insurance Fund and consider adjusting rates to fall in line with expenses in these funds to ensure that they function as the cost-reimbursement accounting tool they are meant to be.

Management Response

The City will continue to monitor these funds to have positive fund balances.

2. Future Accounting Pronouncements

The Governmental Accounting Standards Board (GASB) has issued a number of pronouncements that will impact the City in the future.

GASB Statement No. 87, *Leases*, establishes a single model for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset and aims to enhance comparability of financial statements among governments. This statement also requires additional notes to the financial statements related to the timing, significance, and purpose of a government's leasing arrangements. The requirements of this statement are effective for the fiscal year ending December 31, 2020. Earlier application is encouraged.

GASB Statement No. 91, *Conduit Debt Obligations*, provides a single method of reporting conduit debt obligations by issuers and eliminates diversity in practice associated with (1) commitments extended by issuers, (2) arrangements associated with conduit debt obligations, and (3) related note disclosures. This Statement clarifies the existing definition of conduit debt obligation; establishes that a conduit debt obligation is not a liability of the issuer; establishes standards for accounting and financial reporting of additional commitments and voluntary commitments extended by issuers and arrangements associated with conduit debt obligations; and improves required note disclosures. This statement is effective for fiscal years ending December 31, 2022.

OTHER COMMENTS (Continued)

2. Future Accounting Pronouncements (Continued)

GASB Statement No. 92, *Omnibus 2020*, addresses a variety of topics including: The effective date of Statement No. 87 for interim financial reports; reporting of intra-entity transfers of assets between a primary government employer and a component unit defined benefit pension plan or defined benefit other postemployment benefit (OPEB) plan; the applicability of Statements No. 73 to Certain Provisions of GASB Statement Nos. 67 and 68, as amended, and No. 74, as amended, to reporting assets accumulated for postemployment benefits; the applicability of certain requirements of Statement No. 84, to postemployment benefit arrangements; measurement of liabilities (and assets, if any) related to asset retirement obligations (AROs) in a government acquisition; reporting by public entity risk pools for amounts that are recoverable from reinsurers or excess insurers; reference to nonrecurring fair value measurements of assets or liabilities in authoritative literature and terminology used to refer to derivative instruments. The requirements of this Statement are effective for the fiscal years ending December 30, 2021 and thereafter, except for the requirements related to the effective date of Statement 87 and Implementation Guide 2019-3, reinsurance recoveries, and terminology used to refer to derivative instruments are effective upon issuance.

GASB Statement No. 93, *Replacement of Interbank Offered Rates*. The London Interbank Offered Rate (LIBOR), a result of global reference rate reform, is expected to cease to exist in its current form at the end of 2021, prompting governments to amend or replace financial instruments for the purpose of replacing LIBOR with other reference rates, by either changing the reference rate or adding or changing fallback provisions related to the reference rate. GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*, as amended, requires a government to terminate hedge accounting when it renegotiates or amends a critical term of a hedging derivative instrument, such as the reference rate of a hedging derivative instrument's variable payment. In addition, in accordance with Statement No. 87, *Leases*, as amended, replacement of the rate on which variable payments depend in a lease contract would require a government to apply the provisions for lease modifications, including remeasurement of the lease liability or lease receivable. The objective of this Statement is to address those and other accounting and financial reporting implications that result from the replacement of an IBOR. The removal of LIBOR as an appropriate benchmark interest rate is effective for reporting periods ending after December 31, 2021. All other requirements of this Statement are effective for the fiscal year ending December 31, 2021.

OTHER COMMENTS (Continued)

2. Future Accounting Pronouncements (Continued)

GASB Statement No. 94, *Public-Private and Public-Public Partnerships and Availability Payment Arrangements*, issued to address tissues related to accounting and reporting for public-private and public-public partnership arrangements (PPPs). A PPP is an arrangement in which a government (the transferor) contracts with an operator (a governmental or nongovernmental entity) to provide public services by conveying control of the right to operate or use a nonfinancial asset, such as infrastructure or other capital asset (the underlying PPP asset), for a period of time in an exchange or exchange-like transaction. Some PPPs meet the definition of a service concession arrangement (SCA), which is defined in this Statement as a PPP in which (1) the operator collects and is compensated by fees from third parties; (2) the transferor determines or has the ability to modify or approve which services the operator is required to provide, to whom the operator is required to provide the services, and the prices or rates that can be charged for the services; and (3) the transferor is entitled to significant residual interest in the service utility of the underlying PPP asset at the end of the arrangement. This Statement also provides guidance for accounting and financial reporting for availability payment arrangements (APAs). As defined in this Statement, an APA is an arrangement in which a government compensates an operator for services that may include designing, constructing, financing, maintaining, or operating an underlying nonfinancial asset for a period of time in an exchange or exchange-like transaction. This Statement is effective for fiscal year ending December 31, 2023.

GASB Statement No. 95, *Postponement of the Effective Dates of Certain Authoritative Guidance*. This pronouncement, which is effective upon issuance, allows, but does not require, governments to defer implementing the following pronouncements by one year from their original effective date as follows:

GASB Statement No. 83 - reporting periods beginning after June 15, 2019.

GASB Statement No. 84 and Implementation Guide 2019-2 - reporting periods beginning after December 15, 2019.

GASB Statement No. 87 and Implementation Guide 2019-3 - fiscal years beginning after June 15, 2021, and all reporting periods thereafter.

GASB Statement No. 88 - reporting periods beginning after June 15, 2019.

GASB Statement No. 89 - reporting periods beginning after December 15, 2020.

GASB Statement No. 90 - reporting periods beginning after December 15, 2019.

GASB Statement No. 91 - reporting periods beginning after December 15, 2021.

GASB Statement No. 92, paragraphs 6 and 7 - fiscal years beginning after June 15, 2021.

GASB Statement No. 92, paragraphs 8, 9, and 12 - reporting periods beginning after June 15, 2021.

GASB Statement No. 92, paragraph 10 - government acquisitions occurring in reporting periods beginning after June 15, 2021.

GASB Statement No. 93, paragraphs 13 and 14 - fiscal years beginning after June 15, 2021, and all reporting periods thereafter.

OTHER COMMENTS (Continued)

2. Future Accounting Pronouncements (Continued)

Implementation Guide 2017-3, Questions 4.484 and 4.491 - the first reporting period in which the measurement date of the (collective) net OPEB liability is on or after June 15, 2019.

Implementation Guide 2017-3, Questions 4.85, 4.103, 4.108, 4.109, 4.225, 4.239, 4.244, 4.245, and 5.1–5.4 - actuarial valuations as of December 15, 2018, or later.

Implementation Guide 2018-1 - reporting periods beginning after June 15, 2019.

Implementation Guide 2019-1 - reporting periods beginning after June 15, 2020.

GASB Statement No. 96, *Solution-Based Information Technology Arrangements*, provides guidance on the accounting and financial reporting for subscription-based information technology arrangements (SBITAs) for government end users. A SBITA is defined as a contract that conveys control of the right to use another party's (a SBITA vendor's) information technology (IT) software, alone or in combination with tangible capital assets (the underlying IT assets), as specified in the contract for a period of time in an exchange or exchange-like transaction. This Statement establishes that a SBITA results in a right-to-use subscription asset—an intangible asset—and a corresponding subscription liability, provides the capitalization criteria for outlays other than subscription payments, including implementation costs of a SBITA; and requires note disclosures regarding a SBITA. To the extent relevant, the standards for SBITAs are based on the standards established in Statement No. 87, *Leases*, as amended. The requirements of this Statement are effective for fiscal years beginning after June 15, 2022, and all reporting periods thereafter (i.e., June 30, 2023 and thereafter). Earlier application is encouraged.

We will advise the City of any progress made by GASB in developing this and other future pronouncements that may have an impact on the financial position and changes in financial position of the City.

APPENDIX A
STATUS OF COMMENTS FROM DECEMBER 31, 2018

OTHER COMMENTS

1. Compensated Absences

Compensated absences balances recorded by the City related to accrued vacation, sick hours, and comp hours balances at January 1, 2019, rather than at December 31, 2018. Additionally, it was noted that the City does not maintain records of the accrued sick hours that would need to be paid out if an employee were to leave. Instead, the total accrued sick hours are tracked and then adjusted based on the terms of each employee's contract when preparing the compensated absences schedule. Sikich recommends the City ensures its compensated absences schedules is maintained and balances recorded at fiscal year end agree to the City's calculated liability as of December 31.

Status - Comment considered implemented at December 31, 2019.

2. Insurance Expense

During our testing of insurance expense and related balances, Sikich noted certain prepaid expenses and terminal reserve balances were not properly adjusted at December 31, 2018. Sikich recommended AJE 01 and AJE03 to adjust balance to actual at year end. Sikich recommends the City review accrual accounts at year end to ensure expenses are properly recognized for the fiscal year which they relate to.

Status - Comment implemented as of December 31, 2019.