

CITY AND COUNTY OF SAN FRANCISCO

Report to Government Audit and Oversight Committee
Year Ended June 30, 2019



Certified
Public
Accountants

CITY AND COUNTY OF SAN FRANCISCO
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Year Ended June 30, 2019

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Government Audit and Oversight Committee
Mr. Ben Rosenfield, Controller
City and County of San Francisco
San Francisco, California

We have audited the governmental activities, the business-type activities, each major fund, and the aggregate discretely presented component unit and remaining fund information of the City and County of San Francisco, California (City) as of and for the year ended June 30, 2019, and have issued our report thereon dated December 30, 2019. Our report includes a reference to other auditors that audited the financial statements of the San Francisco County Transportation Authority, San Francisco International Airport, San Francisco Water Enterprise, Hetch Hetchy Water and Power, Municipal Transportation Agency, San Francisco Wastewater Enterprise, and the Health Service System, as described in our report on the City's financial statements dated December 30, 2019. This communication does not include results of the other audits that are reported on separately by those auditors.

Professional standards require that we advise you of the following matters relating to our audit.

1. Our Responsibility in Relation to the Financial Statement Audit

As communicated in our engagement letter dated July 1, 2019, our responsibility, as described by professional standards, is to form and express an opinion about whether the financial statements that have been prepared by management with your oversight are presented fairly, in all material respects, in accordance with accounting principles generally accepted in the United States of America. Our audit of the financial statements does not relieve you or management of your respective responsibilities.

Our responsibility, as prescribed by professional standards, is to plan and perform our audit to obtain reasonable, rather than absolute, assurance about whether the financial statements are free of material misstatement. An audit of financial statements includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control over financial reporting. Accordingly, as part of our audit, we considered the internal control of the City solely for the purpose of determining our audit procedures and not to provide any assurance concerning such internal control.

We are also responsible for communicating significant matters related to the audit that are, in our professional judgment, relevant to your responsibilities in overseeing the financial reporting process. However, we are not required to design procedures for the purpose of identifying other matters to communicate to you.

2. Planned Scope and Timing of the Audit

We conducted our audit consistent with the planned scope and timing we previously communicated to you.

3. Compliance with All Ethics Requirements Regarding Independence

The engagement team, others in our firm, as appropriate, our firm, and our network firms have complied with all relevant ethical requirements regarding independence.

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4. Qualitative Aspects of the Entity's Significant Accounting Practices

Significant Accounting Policies

Management has the responsibility to select and use appropriate accounting policies. A summary of the significant accounting policies adopted by the City is included in Note 2 to the financial statements. As described in Note 4. to the financial statements, the City adopted the following Governmental Accounting Standards Board (GASB) accounting statements effective for the year ended June 30, 2019.

- GASB Statement No. 83, *Certain Asset Retirement Obligations*

This statement addresses accounting and financial reporting for certain retirement obligations (AROs). An ARO is a legally enforceable liability associated with the retirement of a tangible capital asset. The statement establishes criteria for determining the timing and pattern of recognition of a liability and a corresponding deferred outflow of resources for AROs, and requires disclosures of methods and assumptions used. Application of this statement did not have a significant impact on the City for the year ended June 30, 2019.

- GASB Statement No. 88, *Certain Disclosures Related to Debt, Including Direct Borrowings and Direct Placements*

This statement establishes a definition of debt for purposes of disclosure, requires that information provided for direct borrowings and direct placements of debt be reported separately from other debt, and requires more extensive disclosures about unused lines of credit, assets pledged as collateral, and terms related to default, termination, and acceleration. Application of this statement did not have a significant impact on the City for the year ended June 30, 2019. Required disclosures are included in Note 8.

No matters have come to our attention that would require us, under professional standards, to inform you about (1) the methods used to account for significant unusual transactions and (2) the effect of significant accounting policies in controversial or emerging areas for which there is a lack of authoritative guidance or consensus.

Significant Accounting Estimates

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

The most sensitive accounting estimates affecting the City's financial statements are:

- a) Fair value of investments (including investment derivatives) and related net appreciation in the fair value of investments in the City Treasurer's investment pool and the pension trust fund;
- b) Accrual of claims liabilities;
- c) Estimated contractual adjustments and bad debt allowances for patient accounts receivable;
- d) Cost report settlement receivables and payables;
- e) Estimated bad debt allowance for accounts and loans receivable;
- f) Accrual of compensated absences;

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4. Qualitative Aspects of the Entity's Significant Accounting Practices (Continued)

- g) Depreciation estimates for capital assets, including depreciation methods and useful lives assigned to depreciable properties;
- h) Pension plans' employer and employee contribution requirements, the net pension liability of the pension plans and related deferred outflows and inflows of resources; and
- i) Other postemployment benefits (OPEB) plans contribution requirements, the net OPEB liability of the OPEB plans and related deferred outflows and inflows of resources.

Management's estimates were based on the following:

- a) Management's estimate of the fair value of investments in the City Treasurer's investment pool and the pension trust fund is discussed in Note 2(c) to the financial statements.
- b) Liabilities for workers' compensation and general liability claims were based on actuarial evaluations using historical loss and other data. Other claims liabilities were estimated based on the City Attorney's judgment about the ultimate outcome of the claim.
- c) Estimated bad debt allowances for patient accounts receivable were based on historical experience. See d) below for basis for contractual adjustments.
- d) Estimated contractual adjustments for patient accounts receivable and cost report receivables and payables were based on prior cost report adjustments, previous regulatory settlements, and potential future retrospective adjustments.
- e) Estimated bad debt allowance for accounts receivable was based on historical experience and loans receivable was based on the type of loan (e.g., forgivable, deferred, grant or amortizing) and management's estimate regarding the likelihood of collectability based on loan provisions and collateral.
- f) Accrual of compensated absences is based on unused employee sick leave and vacation and the employees' pay rates at year-end and includes the City's share of social security and Medicare payments made on behalf of employees.
- g) Useful lives for depreciable property were determined by management based on the nature of the capital asset. The City uses the straight line method of depreciation and three different conventions for the amount of first-year depreciation based on the departments that purchased the capital assets.
- h) Pension plans' employer and employee contribution requirements, the net pension liability of the pension plans and related deferred outflows and inflows of resources are based on actuarial calculations performed by the City's and California Public Employees' Retirement System's independent actuaries.
- i) OPEB plans' employer and employee contribution requirements, the net OPEB liability of the OPEB plans and related deferred outflows and inflows of resources are based on actuarial calculations performed by the City's independent actuaries.

We evaluated the key factors and assumptions used to develop these accounting estimates and determined that they are reasonable in relation to the basic financial statements taken as a whole and in relation to the applicable opinion units.

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4. Qualitative Aspects of the Entity's Significant Accounting Practices (Continued)

Financial Statement Disclosures

Certain financial statement disclosures involve significant judgment and are particularly sensitive because of their significance to financial statement users. The most sensitive disclosures affecting the City's financial statements relate to pension and other postemployment benefits. The disclosures about pension and other postemployment benefits in Note 9 to the financial statements are based on actuarial valuations.

5. Significant Difficulties Encountered during the Audit

We encountered no significant difficulties in dealing with management relating to the performance of the audit.

6. Uncorrected and Corrected Misstatements

For purposes of this communication, professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that we believe are trivial, and communicate them to the appropriate level of management. Further, professional standards require us to also communicate the effect of uncorrected misstatements related to prior periods on the relevant classes of transactions, account balances or disclosures, and the financial statements as a whole and each applicable opinion unit. The attached schedule summarizes uncorrected financial statement misstatements whose effects in the current and prior periods, as determined by management, are immaterial, both individually and in the aggregate, to the financial statements taken as a whole and each applicable opinion unit.

7. Disagreements with Management

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

8. Representations Requested from Management

We have requested certain written representations from management, which are included in the management representation letter dated December 30, 2019.

9. Management's Consultations with Other Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters. Management informed us that, and to our knowledge, there were no consultations with other accountants regarding auditing and accounting matters.

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10. Other Significant Matters, Findings, or Issues

In the normal course of our professional association with the City, we generally discuss a variety of matters, including the application of accounting principles and auditing standards, operating and regulatory conditions affecting the entity, and operational plans and strategies that may affect the risks of material misstatement. None of the matters discussed resulted in a condition to our retention as the City's auditors.

As described in Note 2(t) to the financial statements, the San Francisco Wastewater Enterprise recorded corrections to previously issued financial statements as of and for the year ended June 30, 2018 to eliminate recognition of certain capital assets. The net position of the enterprise fund as of July 1, 2017 was reduced by \$6.8 million. Additionally, nondepreciable capital assets were reduced and related expenses were increased by \$28.3 million as of and for the year ended June 30, 2018. As a result, the net position of Business-Type Activities on the Statement of Net Position as of July 1, 2018 has been decreased by \$35.1 million from previously reported results.

11. Other Information in Documents Containing Audited Financial Statements

Pursuant to professional standards, our responsibility as auditors for other information in documents containing the City's audited financial statements does not extend beyond the financial information identified in the audit report, and we are not required to perform any procedures to corroborate such other information. However, in accordance with such standards, we applied certain limited procedures to management's discussion and analysis, the pension plans schedules of the City's proportionate share of the net pension liability, changes in net pension liability and related ratios, changes in total pension liability and related ratios, and employer contributions, the postemployment healthcare benefits plans schedules of changes in net OPEB liability and related ratios and employer contributions and budgetary comparison schedule – General Fund, which are required supplementary information (RSI) that supplements the basic financial statements. Our procedures consisted of inquiries of management regarding the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We did not audit the RSI and do not express an opinion or provide any assurance on the RSI.

We were engaged to report on the combining and individual fund financial statements and schedules and the schedule of expenditures of federal awards, which accompany the financial statements but are not RSI. With respect to this supplementary information, we made certain inquiries of management and evaluated the form, content, and methods of preparing the information to determine that the information complies with accounting principles generally accepted in the United States of America, the method of preparing it has not changed from the prior period, and the information is appropriate and complete in relation to our audit of the basic financial statements. We compared and reconciled the supplementary information to the underlying accounting records used to prepare the financial statements or to the basic financial statements themselves.

We were not engaged to report on the introductory and statistical sections, which accompany the basic financial statements but are not RSI. Such information has not been subjected to the auditing procedures applied in the audit of the basic financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

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11. Other Information in Documents Containing Audited Financial Statements (Continued)

Our responsibility also includes communicating to you any information which we believe is a material misstatement of fact. Nothing came to our attention that caused us to believe that such information, or its manner of presentation, is materially inconsistent with the information, or manner of its presentation, appearing in the financial statements.

This report is intended solely for the information and use of the Government Audit and Oversight Committee, Board of Supervisors, City management, and others within the organization, and is not intended to be, and should not be, used by anyone other than these specified parties.

Macias Gini É O'Connell LAP

San Francisco, California
December 30, 2019

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CURRENT YEAR RECOMMENDATIONS

None Reported.

STATUS OF PRIOR YEAR RECOMMENDATION

Reference Number:	2018-001 Reliability of System-Generated Reports Used for Financial Reporting <i>Significant Deficiency in Internal Controls over Financial Reporting</i>
Audit Finding:	<p>An effective information system should allow management to obtain and process quality information to make informed decisions in achieving key objectives and addressing risks. It defines quality information as information that is appropriate, current, complete, accurate, accessible, and provided on a timely basis.</p> <p>On July 3, 2017, the City implemented a new enterprise financial and procurement system, PeopleSoft Financial System, which impacted many facets of the City’s financial management processes, and resulted in the creation of new spreadsheets and alternative solutions to address unexpected system-generated outputs and workflow bottlenecks. A number of system-generated reports did not produce expected results and required substantial time and effort in validating the system outputs. To overcome the additional efforts required in validating system outputs, various spreadsheets and reconciliations were created to ensure the City’s financial statements were prepared in accordance with generally accepted accounting principles. These reconciliations and review processes resulted in significant delays in compiling the City’s financial statements and performing the audits for the year ended June 30, 2018.</p>
Status of Corrective Action:	Corrective action was implemented.

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UNCORRECTED FINANCIAL STATEMENT MISSTATEMENTS

Index	Fund Type	Description	STATEMENT OF NET POSITION				STATEMENT OF CHANGES IN NET POSITION		
			Assets DR (CR)	Deferred Outflows DR (CR)	Liabilities DR (CR)	Deferred Inflows DR (CR)	Net Position DR (CR)	Revenue DR (CR)	Expenses DR (CR)
GOVERNMENTAL ACTIVITIES									
GA1	Governmental Activities	Other Revenues	\$ -	\$ -	\$ -	\$ -	\$ -	\$ (7,696,263)	\$ -
	Governmental Activities	Net Position - Beginning	-	-	-	-	14,109,815	-	-
	Governmental Activities	Deferred Inflows – Unamortized Gain on Leaseback Transaction <i>(To recognize the net impact of two sale-leaseback transactions from the fiscal year ended June 30, 2017.)</i>	-	-	-	(6,413,552)	-	-	-
GA2	Governmental Activities (including Internal Service)	OPEB Expense	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ (15,913,783)
	Governmental Activities (including Internal Service)	Deferred Outflows Related to OPEB Changes in Proportionate Share	-	16,195,865	-	-	-	-	-
	Governmental Activities (including Internal Service)	Deferred Inflows Related to OPEB Changes in Proportionate Share <i>(To record deferred outflows/inflows of resources for OPEB due to changes in proportions.)</i>	-	-	-	(282,082)	-	-	-
GA3	Governmental Activities (including Internal Service)	Deferred Outflows Related to Pension Changes in Proportionate Share	\$ -	\$ 12,772,068	\$ -	\$ -	\$ -	\$ -	\$ -
	Governmental Activities (including Internal Service)	Deferred Inflows Related to Pension Changes in Proportionate Share	-	-	-	(50,037,031)	-	-	-
	Governmental Activities (including Internal Service)	Pension Expense <i>(To record deferred outflows/inflows of resources for pensions due to changes in proportions.)</i>	-	-	-	-	-	-	37,264,963
GA4	Governmental Activities	Loans Receivable Net - Current	\$ 13,817,574	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
	Governmental Activities	Loans Receivable Net - Noncurrent <i>(To record the current portion of net loans receivable.)</i>	(13,817,574)	-	-	-	-	-	-
		TOTAL GOVERNMENTAL ACTIVITIES	\$ -	\$ 28,967,933	\$ -	\$ (56,732,665)	\$ 14,109,815	\$ (7,696,263)	\$ 21,351,180
BUSINESS-TYPE ACTIVITIES									
BA1	Business-Type Activities	Effect of net adjustments from SF General Hospital (see below)	\$ 2,777,826	\$ 8,662,041	\$ -	\$ (3,984,000)	\$ (3,404,165)	\$ 626,339	\$ (4,678,041)
BA2	Business-Type Activities	Effect of net adjustments from Laguna Honda Hospital (see below)	2,793,139	6,918,568	-	(4,507,402)	(906,849)	(1,886,290)	(2,411,166)
BA3	Business-Type Activities	Effect of net adjustments from Port of San Francisco (see below)	-	650,357	-	(1,063,900)	-	-	413,543
		TOTAL BUSINESS-TYPE ACTIVITIES	\$ 5,570,965	\$ 16,230,966	\$ -	\$ (9,555,302)	\$ (4,311,014)	\$ (1,259,951)	\$ (6,675,664)
SAN FRANCISCO GENERAL HOSPITAL									
SFGH1	SF General Hospital	Accounts Receivable	\$ 2,777,826	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
	SF General Hospital	Medical Inpatient Revenue	-	-	-	-	-	626,339	-
	SF General Hospital	Net Position – Beginning <i>(To record patient services revenues and receivables in the proper fiscal year.)</i>	-	-	-	-	(3,404,165)	-	-
SFGH2	SF General Hospital	OPEB Expense	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 866,023
	SF General Hospital	Deferred Inflows Related to OPEB Changes in Proportionate Share <i>(To record deferred inflows of resources for OPEB due to changes in proportions.)</i>	-	-	-	(866,023)	-	-	-
SFGH3	SF General Hospital	Deferred Outflows Related to Pension Changes in Proportionate Share	\$ -	\$ 8,662,041	\$ -	\$ -	\$ -	\$ -	\$ -
	SF General Hospital	Deferred Inflows Related to Pension Changes in Proportionate Share	-	-	-	(3,117,977)	-	-	-
	SF General Hospital	Pension Expense <i>(To record deferred outflows/inflows of resources for pensions due to changes in proportions.)</i>	-	-	-	-	-	-	(5,544,064)
		TOTAL SAN FRANCISCO GENERAL HOSPITAL	\$ 2,777,826	\$ 8,662,041	\$ -	\$ (3,984,000)	\$ (3,404,165)	\$ 626,339	\$ (4,678,041)

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UNCORRECTED FINANCIAL STATEMENT MISSTATEMENTS (CONTINUED)

Index	Fund Type	Description	STATEMENT OF NET POSITION					STATEMENT OF CHANGES IN NET POSITION	
			Assets DR (CR)	Deferred Outflows DR (CR)	Liabilities DR (CR)	Deferred Inflows DR (CR)	Net Position DR (CR)	Revenue DR (CR)	Expenses DR (CR)
LAGUNA HONDA HOSPITAL									
LHH1	Laguna Honda Hospital	Accounts Receivable	\$ 2,793,139	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
	Laguna Honda Hospital	Medical Inpatient Revenue	-	-	-	-	-	(1,886,290)	-
	Laguna Honda Hospital	Net Position – Beginning	-	-	-	-	(906,849)	-	-
		<i>(To record patient services revenues and receivables in the proper fiscal year.)</i>							
LHH2	Laguna Honda Hospital	OPEB Expense	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 3,863,810
	Laguna Honda Hospital	Deferred Inflows Related to OPEB Changes in Proportionate Share	-	-	-	(3,863,810)	-	-	-
		<i>(To record deferred inflows of resources for OPEB due to changes in proportions.)</i>							
LHH3	Laguna Honda Hospital	Deferred Outflows Related to Pension Changes in Proportionate Share	\$ -	\$ 6,918,568	\$ -	\$ -	\$ -	\$ -	\$ -
	Laguna Honda Hospital	Deferred Inflows Related to Pension Changes in Proportionate Share	-	-	-	(643,592)	-	-	-
	Laguna Honda Hospital	Pension Expense	-	-	-	-	-	-	(6,274,976)
		<i>(To record deferred outflows/inflows of resources for pensions due to changes in proportions.)</i>							
		TOTAL LAGUNA HONDA HOSPITAL	\$ 2,793,139	\$ 6,918,568	\$ -	\$ (4,507,402)	\$ (906,849)	\$ (1,886,290)	\$ (2,411,166)
PORT OF SAN FRANCISCO									
PORT1	Port of San Francisco	OPEB Expense	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 697,862
	Port of San Francisco	Deferred Inflows Related to OPEB Changes in Proportionate Share	-	-	-	(697,862)	-	-	-
		<i>(To record deferred inflows of resources for OPEB due to changes in proportions.)</i>							
PORT2	Port of San Francisco	Deferred Outflows Related to Pension Changes in Proportionate Share	\$ -	\$ 650,357	\$ -	\$ -	\$ -	\$ -	\$ -
	Port of San Francisco	Deferred Inflows Related to Pension Changes in Proportionate Share	-	-	-	(366,038)	-	-	-
	Port of San Francisco	Pension Expense	-	-	-	-	-	-	(284,319)
		<i>(To record deferred outflows/inflows of resources for pensions due to changes in proportions.)</i>							
		TOTAL PORT OF SAN FRANCISCO	\$ -	\$ 650,357	\$ -	\$ (1,063,900)	\$ -	\$ -	\$ 413,543
AGGREGATE REMAINING FUNDS									
AGG1	Aggregate Remaining Funds (Internal Service)	OPEB Expense	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ (1,267,287)
	Aggregate Remaining Funds (Internal Service)	Deferred Outflows Related to OPEB Changes in Proportionate Share	-	1,549,369	-	-	-	-	-
	Aggregate Remaining Funds (Internal Service)	Deferred Inflows Related to OPEB Changes in Proportionate Share	-	-	-	(282,082)	-	-	-
	Aggregate Remaining Funds (Retirement System)	OPEB Expense	-	382,123	-	-	-	-	-
	Aggregate Remaining Funds (Retirement System)	Deferred Outflows Related to OPEB Changes in Proportionate Share	-	-	-	-	-	-	(382,123)
		<i>(To record deferred outflows/inflows of resources for OPEB due to changes in proportions.)</i>							
AGG2	Aggregate Remaining Funds (Internal Service)	Deferred Outflows Related to Pension Changes in Proportionate Share	\$ -	\$ 1,300,066	\$ -	\$ -	\$ -	\$ -	\$ -
	Aggregate Remaining Funds (Internal Service)	Deferred Inflows Related to Pension Changes in Proportionate Share	-	-	-	(2,709,180)	-	-	-
	Aggregate Remaining Funds (Internal Service)	Pension Expense	-	-	-	-	-	-	1,409,114
		<i>(To record deferred outflows/inflows of resources for pensions due to changes in proportions.)</i>							
		TOTAL AGGREGATE REMAINING FUNDS	\$ -	\$ 3,231,558	\$ -	\$ (2,991,262)	\$ -	\$ -	\$ (240,296)

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