Audit Committee
Meeting Minutes
July 13, 2012

The Bethany Beach Audit Committee held a meeting on Friday, July 13, 2012 at 10:00 a.m. in the Town Meeting Room, 214 Garfield Parkway, Bethany Beach, DE 19930.

Members present: Patrick Sheplee, Chairman, who presided; Monte Wisbrock, and Thomas Defibaugh.

Also present: Finance Director, Janet Connery; Internal Auditor, Philip Rossi; TGM Group LLC representatives, Herb Geary and Roy Geiser; Council members, Mayor Tony McClenny, Vice-Mayor Jack Gordon, Secretary Treasurer, Jerry Dorfman, Joseph Healy, and Lew Killmer; Administrative Secretary, Lindsey Good; and interested members of the public.

Mr. Sheplee called the meeting to order at 10:00 a.m.

Approval of Agenda
Mr. Wisbrock made a motion to approve the agenda. The motion was seconded by Mr. Defibaugh and unanimously approved.

Approval of Minutes from the May 04, 2012 Meeting
Mr. Defibaugh made a motion to approve the minutes dated May 04, 2012. Seconded by Mr. Wisbrock, the motion was unanimously approved.

Report by Accounting Firm TGM Group, LLC on this Year's Audit and Financial Statements
Mr. Geiser of the TGM Group LLC, gave the following report:

The audit went very well, and the management was prepared and submitted all the needed information. He then reported the highlights of the Financial Statements for the year ended March 31, 2012.

The Independent Auditors' Report on pages three (3) and four (4) illustrate an unqualified opinion, which is the highest assurance that can be obtained, that the statements are free of material misstatements.

He acknowledged that Ms. Connery did a great job on the Town of Bethany Beach's Management's Discussion and Analysis, on pages five (5) through sixteen (16).

Pages seventeen (17) and eighteen (18) contains the Statement of Net Assets and Statement of Activities, which are most similar to the financials prepared by private companies and show the town-wide combination of the General and Enterprise funds. He explained that total Net Assets increased by more than one million dollars ($1,000,000) since the prior year.

Page 19 is the Governmental Balance Sheet, which in a modified basis of accounting. The Town implemented GASB 54 last year, which was a year earlier than is required. This effects how the

Town's reserves are presented as non-spendable, restricted, committed or unassigned. The Government Finance Officers Association (GFOA) recommends that governments hold a minimum of two (2) months' worth of operating expenses in reserve. The Town holds $4.2 million in total reserves, almost twelve (12) months of operating costs, which means that the Town is in good financial shape, which is not common for most other towns.

On page 35 and 36, there is an explanation of the capital assets. The Town reinvested $1.8 million in itself through capital assets, such as the boardwalk, street work, and the purchase of equipment and trucks. However, the Town has very little debt. The only debt added this year was the three-year payment plan for the second half of the parking pay stations.

Mr. Sheplee questioned if any of the capital assets that were reinvested were obtained by borrowing funds.

Ms. Connery stated that there were no funds that were borrowed.

Mr. Geiser noted that it is very impressive that the Town holds very little debt.

Mr. Geiser reviewed pages 39 and 40, which addressed post-employment healthcare benefits, also known as other post-employment benefits (OPEB). The Town's total actuarial accrued liability is $545,000. The Town chose to amortize this liability over a ten-year period, and there are seven years remaining. The Town's net OPEB obligation to date is $130,000. The Town holds $130,000 in assets specific to this liability and so has fully funded the current liability. He emphasized that many governments are not funding the liability at all.

Mr. Sheplee asked how the Town holds the $130,000 in assets. Ms. Connery replied the assets are kept in a separate bank account and each quarter she books a portion of the year's liability and transfer the cash. She added that she had intended to hold these funds in treasury bills, but interest rates have not been favorable.

Mr. Pat Neary, property owner, questioned why the Town is responsible for covering this expense. Councilman, Mr. Killmer explained that it is a promised responsibility that took place in the past. Ms. Connery added that this was common benefit in the 1980's and 1990's, however, recently government accounting standards were changed so that governments must show the projected cost of this liability.

Mr. Geiser reviewed page 18 with the Committee. He reported that governmental revenue decreased by $200,000 from the prior year, which mainly resulted from the reduction in transfer tax revenue. He emphasized that there were two major cost increases in the Sanitation Fund, the purchase of a new trash truck and the purchase of recycling dumpsters and carts. He added that the revenue of business-type activities is comparable to the prior year.

Mr. Geiser addressed that he is aware that the Town is applying to borrow $2.6 million for twenty (20) years at a rate of 2.5% from the State Revolving Fund for the construction of a new water tower. Additional audit procedures are required when the spending of Federal money exceeds $500,000 in a year, even if that money goes through a state agency. This is called a

Single Audit, and the Town will be subjected to this type of audit in 2014. During a Single Audit, information is reviewed more thoroughly, internal controls are examined closer, and compliance with grant conditions is investigated more thoroughly. He noted that the fee to complete this audit will be slightly higher as well. The Town will be required to have a Single Audit completed at the time when the cash is paid out, and this will most likely occur during fiscal years 2014 and 2015.

Mr. Killmer questioned if their auditing firm performs Single Audits. Mr. Geary replied that their auditing firm is capable of performing a Single Audit.

Mr. Dorfman noted that there is an agenda item on funding options for the proposed water tower to be discussed at the upcoming Budget and Finance meeting on July 19th, and questioned if this is entered into the auditing firm's estimates. Mr. Geary replied that it does not modify the auditing firm's estimate.

Mr. Sheplee questioned if the Town is expecting to expend money in 2014 for the water tower construction. Ms. Connery explained that some funds will be expended during 2014 but that much of the engineering costs have already been paid this year. It was noted that there will be a Special Election to vote on borrowing funds for the water tower.

Mr. Killmer questioned if there is a limit to the amount of money that the Town can borrow. Ms. Connery replied that there is a limit based on a percentage of property assessments, but the limit is very high, much more than the borrowing proposed.

Hearing no further questions at this time, Mr. Geiser stated that he has no further information to provide and states that overall the audit went very well. Mr. Geary added that there were minor modifications made to the Audit Report, but there were no major changes. Ms. Connery acknowledged that the Committee thoroughly reviews the Audit Report and considers any recommendations that are provided.

Mr. Geary advised the Committee to thoroughly review the Management's Discussion and Analysis (MD&A) audit to verify that there are no errors, since it is a very concise report.

Ms. Connery reviewed the Management's Discussion and Analysis (MD&A) report that she prepared. She emphasized that her priority is to guide the reader to understand the financial status of the Town and the reason for major changes from the prior year.
In the report, she made a point to stress that when cash is paid out for capital purchases, assets are also increasing.

Ms. Connery stated that she is open to any suggestions on what information to include in the MD&A. She noted as an example that a property owner mentioned that he did not see the Town's total property assessment in the financial statements, so she will be adding a sentence to Page 10 in the current draft that will state, "The assessed value of taxable properties as of May 2011 was $978,484,505 and the tax rate was $0.165 per $100 of assessed value."

Ms. Connery referenced Page 8 of the MD&A and explained that the Town invested a significant amount in capital projects this year, especially for the removal of the utility poles on Garfield Parkway. Since the poles have been removed, the State has indicated that they will fund the Streetscape Project in coming years, which will enhance the beautification of the Town.

Mr. Sheplee questioned if the capital reserves are guidelines established by the Town Council. Ms. Connery explained that there are guidelines that were developed by the Budget and Finance Committee, and that Committee is responsible for closely monitoring expended costs. The Budget and Finance Committee will be meeting next week.

Ms. Connery reviewed Page 10 of the MD&A. She explained that one of the Town's main goals is to have summer season revenue fully cover the cost of the summer season. Each year, she estimates how much of the Town's costs are related to being a summer season tourist attraction. This year it was estimated that this cost was $2.6 million which is more than covered by the $2.7 million in revenue generated by the summer season. This shows that property taxes are not used to cover the costs for lifeguards or bandstand performances.

Page 11 was referenced in the MD&A report, which includes two (2) charts that show the Town's sources of revenue. Ms. Connery stated that currently property taxes are the Town's main source of revenue, but in 2006 the largest source of revenue was real estate transfer taxes, and the amount exceeded all other sources. In 2006, Council significantly decreased the Town's dependence on transfer taxes because it was not a reliable source of income, which is why property taxes needed to increase. The graph at the bottom of Page 11 shows how transfer tax revenue fell from almost $1.6 million to just over $400,000 last year.

Ms. Connery reviewed Page 13 of the MD&A document and explained the reasons for the changes in the Sanitation Fund. Operating expenses increased $209,000, but $147,000 of this were expenses from new State yard waste and recycling regulations, and an additional $38,000 was a result of increases in disposal fees charged by the Delaware Solid Waste Authority. This year, the Sanitation Fund shows an operating loss of $77,266, while last year had a gain of $74,401. The main reason for this is the result of modified government standards on how grant revenue is presented. She added that the Budget and Finance Committee will discuss this in further detail at its meeting this week.

Mr. Healy expressed that he feels the governmental accounting standards resulted in accounting language that could be misinterpreted, especially on Pages 24 and 51 as an example. He stated the issue is that while the purchase of recycling carts and dumpsters is an operating cost, the grant revenue that is used to pay for those purchases is "below the line" as a non-operating revenue. He emphasized that the statements should be accurate as possible, and not misleading. He said that the Town is in excellent financial condition, however, it is not portrayed as such. He acknowledged that the Budget and Finance Committee has addressed these issues, but many other governments have not.

Mr. Geary and Mr. Geiser replied that they understand Mr. Healy's concern, but explained that they must abide by the standards on governmental accounting. Mr. Geary commented that the policy on operating costs is explained on Page 32.

Mr. Killmer questioned what the rationale is for the standards of governmental accounting. Mr. Geary explained that grant funds are separate from operating funds.

Mr. Sheplee agreed that the language is not as clear it could be, but that it is required that it is completed this way and the reasons are explained in the MD&A.

The Committee agreed with the suggestion to add text to Page 51 referring to Page 14 of the MD&A, where the grant and operating loss are explained.

Mr. Patrick Neary, property owner, asked why the Water Department Debt shown on Page 37 states an interest rate range of 2.75% to 9.75%. He expressed concern as to why the interest rate is not explained, and why the Town tolerates it to be so high.

Ms. Connery explained that the bond terms had an interest rate of 9.75% for a few years, but there has been an interest rate of 5.3% for the past few years on this debt. One of the modifications she is proposing is to state only this 5.3% rate on Page 37. Based on Mr. Neary's concern, she will add the following text to Page 16: "Refinancing of the 1994 bond issue was considered several times and found that it would not result in significant savings".

Mr. Sheplee questioned if there is any guidance on what should be included in the MD&A. The auditors replied that there are seven (7) to nine (9) specific requirements, which the Town meets, but no guidance beyond those minimum standards.

Mr. Neary inquired about the Town's collection rate for property taxes. Ms. Connery explained that the Town collects more than 99% of property taxes as well as Sanitation and Water fees. There has been no significant increase in the amount owed to the Town in the past year. Every year there are a few properties that owe $1,000 or more but the Town will collect that in full plus the 2% per month late penalty once the house is sold.

Mr. Neary asked how many employees are covered on Page 25, *Cash Flows from Operating Activities*, "Payments to employees" for the Water Funds. Ms. Connery answered that this amount includes three (3) employees plus an allocated percentage of administrative employees.

Mr. Neary asked for the reason for the increase in *Employer's Payroll and Contributions Under the Plan* on Page 42. Ms. Connery replied that an I.T. position was added.

Hearing no further questions or concerns, Ms. Connery noted that a copy of the draft financials had also been sent to the members of the Budget and Finance Committee, which meets next week. At that meeting, she will ask the Committee members if they have any changes, questions or suggestions for the statements. After the meeting, she will send the Audit Committee members a list of changes and the report will be finalized before the end of the month, within the 120-day Charter requirement.

Mr. Sheplee expressed his appreciation to Ms. Connery for doing an excellent job on the MD&A report. He also thanked Mr. Geary and Mr. Geiser for all of their work on the report.

Adjourn

Mr. Wisbrock made a motion to adjourn the meting. Seconded by Mr. Defibaugh, the motion was unanimously approved.

The meeting was adjourned at 11:20 a.m.