

ANNUAL FINANCIAL REPORT

CITY OF PALMDALE, CALIFORNIA

PALMDALE FINANCING AUTHORITY

(A Component Unit of the City of Palmdale)



For the Fiscal Year Ended

June 30, 2014

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CITY OF PALMDALE FINANCING AUTHORITY

**ANNUAL FINANCIAL REPORT
JUNE 30, 2014**

TABLE OF CONTENTS

INDEPENDENT AUDITORS' REPORT.....1

BASIC FINANCIAL STATEMENTS

 Statement of Net Position.....3

 Statement of Revenues, Expenses, and Changes in Fund Net Position4

 Statement of Cash Flows.....5

Notes to the Financial Statements6

**INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER
FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER
MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS
PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING
STANDARDS***14



INDEPENDENT AUDITORS' REPORT

To the Honorable Members of the Board of Directors
Palmdale Financing Authority
City of Palmdale, California

Report on the Financial Statements

We have audited the accompanying financial statements of the Palmdale Financing Authority (Authority), a component unit of the City of Palmdale, California, as of and for the year ended June 30, 2014, and the related notes to the financial statements, as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design 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. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Authority, as of June 30, 2014, and the changes in financial position, and cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As described in Note 1 to the financial statements, the Authority implemented Governmental Accounting Standards Board (GASB) Statement No. 65, *Items Previously Reported as Assets and Liabilities*. Also, as discussed in Note 6 to the financial statements, the Authority reported a prior period adjustment to properly account for lease receivables and related unearned lease revenue. Our opinion is not modified with respect to these matters.

Other Matters

Required Supplementary Information

Management has omitted the Management's Discussion and Analysis that accounting principles generally accepted in the United States of America requires to be presented to supplement the basic financial statements. Such missing information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. Our opinion on the basic financial statements is not affected by this missing information.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated November 25, 2014, on our consideration of the Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Authority's internal control over financial reporting and compliance.

Varrinck, Trine, Day & Co. LLP

Rancho Cucamonga, California
November 25, 2014

CITY OF PALMDALE FINANCING AUTHORITY

STATEMENT OF NET POSITION

JUNE 30, 2014

Assets:

Interest Receivable	\$ 86,837
Leases Receivable	<u>8,695,000</u>
Total Assets	<u>8,781,837</u>

Liabilities:

Accrued Interest Payable	86,837
Noncurrent Liabilities:	
Due in More than One Year	<u>8,695,000</u>
Total Liabilities	<u>8,781,837</u>

Net Position:

Unrestricted	<u>-</u>
Total Net Position	<u><u>\$ -</u></u>

See Accompanying Notes to the Financial Statements

CITY OF PALMDALE FINANCING AUTHORITY

**STATEMENT OF REVENUES, EXPENSES
AND CHANGES IN FUND NET POSITION**

FOR THE YEAR ENDED JUNE 30, 2014

Non-Operating Revenues:	
Payments from the Ctiy	\$ 256,517
Interest Income	<u>86,838</u>
Total Non-Operating Revenues	<u>343,355</u>
Non-Operating Expenses:	
Interest on Debt	<u>260,510</u>
Total Non-Operating Expenses	<u>260,510</u>
Change in Net Positon	82,845
Net Position, Beginning of Year, as restated	<u>(82,845)</u>
Net Position, End of Year	<u><u>\$ -</u></u>

See Accompanying Notes to the Financial Statements

CITY OF PALMDALE FINANCING AUTHORITY

**STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED JUNE 30, 2014**

Cash flows from non-capital financing activities:	
Lease Payments Received from the City of Palmdale	256,517
Interest Paid on Debt	<u>(260,510)</u>
Net cash used for non-capital financing activities	<u>(3,993)</u>
Cash flows from investing activities:	
Interest on Investments	<u>1</u>
Net increase (decrease) in cash and cash equivalents	(3,992)
Cash and cash equivalents - Beginning of Year	<u>3,992</u>
Cash and cash equivalents - End of Year	<u><u>\$ -</u></u>

See Accompanying Notes to the Financial Statements

PALMDALE FINANCING AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS



For the Fiscal Year Ended

June 30, 2014

**CITY OF PALMDALE FINANCING AUTHORITY
TABLE OF CONTENTS TO THE
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2014**

Note No.	Page No.
1. Summary of Significant Accounting Policies.....	7
Description of the Reporting Entity.....	7
Financial Statements Presentation, Basis of Accounting and Measurement Focus.....	7
Cash and Cash Equivalents.....	8
Long-Term Obligations	8
Net Position	8
Use of Estimates	8
Implemented Accounting Pronouncements	8
2. Long-Term Receivables.....	9
Leases Receivables	9
3. Long-Term Debt.....	10
Lease Revenue Bonds.....	10
Changes in Long-Term Liabilities.....	11
4. New Accounting Pronouncements.....	11
5. Subsequent Event.....	12
6. Cumulative Effect of a Change in Accounting Principle and Prior Year Adjustment.....	12

CITY OF PALMDALE FINANCING AUTHORITY

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2014

(1) Summary of Significant Accounting Policies

A. Description of the Reporting Entity

The Palmdale Financing Authority of the City of Palmdale, California (Authority) was originally created under a joint powers agreement between the City of Palmdale (City) and the Housing Authority of the City of Palmdale (Agency) on September 26, 2012 for the purpose of financing public improvements in the City. The Authority is financially accountable to the City and, accordingly, is a component unit of the City although it is a separate legal entity. Assets of the Authority, after providing for all debts and obligations, are to be transferred to the City upon final payment of the loans.

The Authority is a component unit of the City of Palmdale, California (as defined by the Governmental Accounting Standards Board) and, as such, is included in the Comprehensive Annual Financial Report of the City. Component units are legally separate organizations for which the elected officials of the primary government are financially accountable. Although a legally separate entity, it is reported on a blended basis as part of the primary government (the City) because a voting majority of the Authority's governing board is appointed by the City Council and they are, in substance part of the City's operations.

B. Financial Statement Presentation, Basis of Accounting and Measurement Focus

The Palmdale Financing Authority's basic financial statements are prepared in conformity with generally accepted accounting principles (GAAP) as applied to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for governmental accounting and financial reporting principles.

The Authority reports its activities as an enterprise fund. The Authority's financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recognized in the period incurred regardless of the timing of related cash flows.

Proprietary funds distinguish operating revenues and expenses from those revenues and expenses that are non-operating. Operating revenues are those revenues that are generated by leasing activities while operating expenses pertain directly to the furnishing of those services. Non-operating revenues and expenses are those revenue and expenses generated that are not directly associated with the normal business of debt activities.

When both restricted and unrestricted resources are available for use, it is the Authority's policy to use restricted resources first, then unrestricted resources as they are needed.

The Annual Financial Statements are intended to reflect the financial position, results of operation and net position of the City of Palmdale Financing Authority. They do not present fairly the financial position and results of operations of the City of Palmdale, California, in conformity with accounting principles generally accepted in the United States of America.

CITY OF PALMDALE FINANCING AUTHORITY

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2014

C. Cash and Cash Equivalents

Investments may include amounts invested in money market funds held by a trustee. Amounts invested in money market funds are reported at fair value, which is the same as the carrying amount as of June 30, 2014.

D. Long-Term Obligations

In the Statement of Net Position, long-term debt is a liability. Bond premium/discounts are deferred and amortized over the life of the bonds using the straight-line method. Bonds payable are reported net of the applicable bond premium or discount.

E. Net Position

Net position is comprised of the cumulative net earnings from non-operating revenues and expenses. Net position is classified in the following categories:

Unrestricted – This component of net position consists of resources that are available to the Authority.

F. Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

G. Implemented Accounting Pronouncements

During fiscal year 2013-14, the Authority adopted GASB Statement No. 65 – *Items Previously Reported as Assets and Liabilities*. This statement establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities. The statement is effective for periods beginning after December 15, 2012, or the 2013-2014 fiscal year. The implementation resulted in a prior period adjustment of \$310,223 to remove unamortized bond costs.

During fiscal year 2013-14, the Authority adopted GASB issued Statement No. 66 *Technical Corrections – 2012 – an amendment of GASB Statements No. 10 and No. 62*. The objective of this statement is to improve accounting and financial reporting for a governmental financial reporting entity by resolving conflicting guidance that resulted from the issuance of two pronouncements, Statements No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions* and No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*. The Statement is effective for periods beginning after December 15, 2012, or the 2013-2014 fiscal year. The implementation did not have any significant impact on the Authority's financial statements.

During fiscal year 2013-14, the Authority adopted GASB Statement No. 67, *Financial Reporting for Pension Plans – an amendment of GASB Statement No. 25*. The objective of this statement is to improve financial reporting by state and local governmental pension plans. This statement results from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for

CITY OF PALMDALE FINANCING AUTHORITY

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2014**

pensions with regard to providing decision-useful information, supporting assessments of accountability and interperiod equity, and creating additional transparency. This statement replaces the requirements of Statement No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans*, and Statement No. 50, *Pension Disclosures*, as they relate to pension plans that are not administered through trust covered by the scope of this statement and to defined contribution plans that provide postemployment benefits other than pension. The statement is effective for periods beginning after June 15, 2013, or the 2013-2014 fiscal year. The implementation did not have any significant impact on the Authority’s financial statements.

During fiscal year 2013-14, the Authority adopted GASB Statement No. 70 –*Accounting and Financial Reporting for Nonexchange Financial Guarantees*. The objective of this statement is to improve the recognition, measurement, and disclosure for state and local governments that have extended or received financial guarantees that are nonexchange transactions. The statement is effective for periods beginning after June 15, 2013, or the 2013-2014 fiscal year. The implementation did not have any significant impact on the Authority’s financial statements.

(2) Long-Term Receivables

A. Leases Receivable

The Authority and the City of Palmdale have entered into a lease agreement that obligates the City to pay lease payments to the Authority in consideration of the City’s use and enjoyment of certain property and improvements. The lease payment schedule, as well as the facilities subject to the lease, are more fully described on pages 10-11, Note 4 A – Lease Revenue Bonds. Lease receivable activity for the year ended June 30, 2014, was as follows:

	<u>Balance at</u> <u>July 1, 2013</u>	<u>Additions</u>	<u>Payments</u>	<u>Balance at</u> <u>June 30, 2014</u>
Lease Receivable Related to:				
2012 Lease Revenue Bonds	\$ 8,695,000	\$ -	\$ -	\$ 8,695,000
 Total Lease Receivables	<u>\$ 8,695,000</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 8,695,000</u>

CITY OF PALMDALE FINANCING AUTHORITY

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2014**

As of June 30, 2014, future lease payments are as follows:

Fiscal Year Ended	2012 Lease Receivable	
	Principal	Interest
2015	\$ -	\$ 260,510
2016	490,000	255,610
2017	500,000	243,210
2018	515,000	227,985
2019	530,000	212,310
2020-2024	2,890,000	809,387
2025-2029	3,185,000	353,176
2030	585,000	9,872
	<u>\$ 8,695,000</u>	<u>\$ 2,372,060</u>

(3) Long-Term Debt

A. Lease Revenue Bonds

2012 Lease Revenue Bond Payable - On December 19, 2012, the Authority issued \$8,695,000 of Lease Refunding Revenue Bonds (2012 Bonds). Interest on the 2012 Bonds is payable semi-annually on March 1 and September 1 at rates ranging from 2.00% to 4.00% per annum. Principal installments are payable September 1 of each year from 2015 to 2029.

The 2012 Bonds maturing on or after September 1, 2015, are subject to extraordinary mandatory redemption from net proceeds of an insurance, title insurance, condemnation or eminent domain award on any interest payment date, in the amount of principal and accrued interest, to the extent that the City credits these proceeds towards the prepayment of lease payments. The 2012 Bonds maturing on or after September 1, 2023, may be redeemed on or after September 1, 2022, from proceeds of optional lease prepayments made by the City, without premium.

The proceeds of the 2012 Bonds were used to refinance an existing lease and refund the related certificates of participation, to satisfy the reserve requirement of the bonds, and pay the costs incurred in connection with the issuance of the bonds.

The 2012 Bonds represent direct, undivided fractional interests in a lease of the City's Development Services Building and the South Valley WorkSource Center. The City has the right, subject to certain conditions, to substitute alternate property for the above properties, as the property subject to the lease.

The lease agreement requires the City to pay a semi-annual base rental on August 15 and February 15 to the Authority for the use of the facilities through September 2029. The rentals will be used by the Authority to pay principal and interest with respect to the 2012 Bonds as they become due. Title to the land and facilities covered by the lease and the 2012 Bonds is vested in the Authority, for the benefit of the 2012 Bond holders, during the lease term.

Upon completion of the term of the lease and payment in full to the 2012 Bond holders, title to the property shall vest in the City. The City may, on any date, deposit sufficient funds into an irrevocable

CITY OF PALMDALE FINANCING AUTHORITY

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2014**

trust to pay all remaining lease payments, at which time the lease agreement shall cease and terminate and title to the property shall vest in the City.

<u>Year Ending</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2015	\$ -	\$ 260,510	\$ 260,510
2016	490,000	255,610	745,610
2017	500,000	243,210	743,210
2018	515,000	227,985	742,985
2019	530,000	212,310	742,310
2020-2024	2,890,000	809,387	3,699,387
2025-2029	3,185,000	353,176	3,538,176
2030	585,000	9,872	594,872
Totals	<u>\$ 8,695,000</u>	<u>\$ 2,372,060</u>	<u>\$ 11,067,060</u>

B. Changes in Long-Term Liabilities

Long-term liability activity for the year ended June 30, 2014, was as follows:

	<u>Principal Balance at July 1, 2013</u>	<u>Additions</u>	<u>Retirements</u>	<u>Principal Balance at June 30, 2014</u>	<u>Amounts Due Within One Year</u>
2012 Lease Revenue Bonds	\$ 8,695,000	\$ -	\$ -	\$ 8,695,000	\$ -
Total	<u>\$ 8,695,000</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 8,695,000</u>	<u>\$ -</u>

(4) New Accounting Pronouncements

GASB Statement No. 68 – In June 2012, GASB issued Statement No. 68, *Accounting and Financial Reporting for Pensions – an amendment of GASB Statement No. 27*. The primary objective of this Statement is to improve accounting and financial reporting by state and local governments for pensions. It also improves information provided by state and local governmental employers about financial support for pensions that is provided by other entities. This Statement results from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for pensions with regard to providing decision-useful information, supporting assessments of accountability and interperiod equity, and creating additional transparency. The Statement is effective for periods beginning after June 15, 2014, or the 2014-2015 fiscal year. The Authority has not determined the effect on the financial statements.

GASB Statement No. 69 – In January 2013, GASB issued Statement No. 69, *Government Combinations and Disposals of Government Operations*. The objective of this Statement is to establish reporting standards related to government combinations and disposals of government operations. The Statement is effective for periods beginning after December 15, 2013, or the 2014-2015 fiscal year. The Authority has not determined the effect on the financial statements.

CITY OF PALMDALE FINANCING AUTHORITY

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2014**

GASB Statement No. 71 - In November 2013, GASB issued Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date – an amendment to GASB Statement No. 68*. This Statement amends paragraph 137 of Statement 68 to require that, at transition, a government recognize a beginning deferred outflow of resources for its pension contributions, if any, made subsequent to the measurement date of the beginning net pension liability. Statement 68, as amended, continues to require that beginning balances for other deferred outflows of resources and deferred inflows of resources related to pensions be reported at transition only if it is practical to determine all such amounts. The provisions of this Statement are required to be applied simultaneously with the provisions of Statement 68. The Authority has not determined the effect on the financial statements.

(5) Subsequent Event

On October 16, 2014, the Palmdale Financing Authority issued \$25,920,000 2014 Lease Agreement and Certificates of Participation in a partial refunding. The net proceeds will be used to refinance an existing lease and refund \$25,445,000 of Palmdale Civic Authority’s 2002 Certificates of Participation (2002 Park Improvement and Avenue S Construction Project) on November 15, 2014. The principal and interest on the 2014 Certificates of Participation are payable from pledged Park Assessment Funding revenues.

(6) Cumulative Effect of a Change in Accounting Principle and Prior Year Adjustment

Effective July 1, 2013, the Authority implemented GASB 65, *Items Previously Reported as Assets and Liabilities*. It was determined that debt issuance costs do not meet the definition of an asset or a deferred outflow and should be recognized as an outflow of resources in the reporting period in which they are incurred.

The Authority also corrected an error regarding the deferral of the lease receivable on the Statement of Net Position. The Authority incorrectly deferred future lease revenues due from the City of Palmdale.

The following is the summary of the effect of these adjustments on net position:

Beginnng Net Position, as Previously Reported	\$ (8,467,622)
Deferred Revenue/Unearned	8,695,000
Cost of Issuance	<u>(310,223)</u>
Beginning Net position, as restated	<u>\$ (82,845)</u>

CITY OF PALMDALE FINANCING AUTHORITY

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2014**

Following is the Pro forma effect of the retroactive application of GASB 65:

	As Previously <u>Stated</u>	<u>Restatement</u>	<u>Restated</u>
Deferred Charges-Cost of Issuance	\$ 310,223	\$ (310,223)	-
General Government	8,520,789	(35,543)	8,485,246



INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

To the Honorable Members of the Board of Directors
Palmdale Financing Authority
City of Palmdale, California

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Palmdale Financing Authority (Authority), a component unit of the City of Palmdale, as of and for the year ended June 30, 2014, and the related notes to the financial statements, which collectively comprise the Authority's basic financial statements, and have issued our report thereon dated November 25, 2014. Our report contained an emphasis of matter regarding the adoption of Governmental Accounting Standards Board (GASB) Statement No. 65, *Items Previously Reported as Assets and Liabilities*, effective July 1, 2013.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Authority's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control. Accordingly, we do not express an opinion on the effectiveness of the Authority's internal control.

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 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 entity's financial statements will not be prevented, or detected and corrected 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.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or, significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Authority's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Vavrinik, Trine, Day & Co. LLP

Rancho Cucamonga, California
November 25, 2014