

CITY OF WEST COVINA, CALIFORNIA
WEST COVINA HOUSING AUTHORITY FUND

(A COMPONENT UNIT OF
THE CITY OF WEST COVINA)

**FINANCIAL STATEMENTS AND
INDEPENDENT AUDITOR'S REPORT**

JUNE 30, 2017

City of West Covina, California
West Covina Housing Authority Fund
Table of Contents
June 30, 2017

	<u>PAGE</u>
Independent Auditor's Report	1
Basic Financial Statements	
Balance Sheet	4
Statement of Revenues, Expenditures, and Changes in Fund Balance	5
Notes to the Financial Statements	6
Required Supplementary Information	
Budgetary Comparison Schedule	11
Note to Required Supplementary Information	12
Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>	13



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INDEPENDENT AUDITOR'S REPORT

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West Covina, California

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Report on the Financial Statements

We have audited the accompanying financial statements of the West Covina Housing Authority Fund (the Housing Authority), (a component unit of the City of West Covina, California (the City)), as of and for the year ended June 30, 2017, 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.

Auditor's 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 auditor's 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.

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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 Housing Authority, as of June 30, 2017, and the changes in financial position thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 1, the financial statements present only the Housing Authority and do not purport to, and do not present fairly the financial position of the City as of June 30, 2017, the changes in its financial position, or, where applicable, its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the budgetary comparison schedule, identified as Required Supplementary Information (RSI) in the accompanying table of contents, be presented to supplement the basic financial statements. Such Information, although not a part of the basic financial statement, 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. We have applied certain limited procedures to the RSI in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about 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 the audit of the basic financial statements. We do not express an opinion or provide any assurance on the RSI because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Management has omitted management's discussion and analysis that accounting principles generally accepted in the United States of America require to be presented to supplement the basic financial statements. Such missing information, although not a part of that basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of the 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 issued our report dated December 12, 2017, on our consideration of the Housing Authority's internal control over financial reporting and 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 the 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 Housing Authority's internal control over financial reporting and compliance.

Rogers, Anderson, Malody & Scott, LLP.

San Bernardino, California
December 12, 2017

City of West Covina, California
West Covina Housing Authority Fund
Balance Sheet
June 30, 2017

Assets

Cash and investments	\$ 5,620,355
Interest receivable	1,078
Notes and loans receivable	14,266,152
Advances to Successor Agency	4,857,950
Prepays	<u>122,500</u>
 Total assets	 <u><u>\$ 24,868,035</u></u>

Liabilities and fund balance

Liabilities:

Accounts payable	\$ 4,279
Other accrued liabilities	<u>3,360</u>
 Total liabilities	 <u>7,639</u>

Fund balance:

Nonspendable:

Prepays	122,500
Advances to Successor Agency	4,857,950

Restricted for:

Affordable housing	<u>19,879,946</u>
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Total fund balance	<u>24,860,396</u>
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Total liabilities and fund balance	<u><u>\$ 24,868,035</u></u>
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The accompanying notes are an integral part of these financial statements.

City of West Covina, California
West Covina Housing Authority Fund
Statement of Revenues, Expenditures, and Changes in Fund Balance
For the year ended June 30, 2017

Revenues

Investment income	\$ 819,924
Other revenues	<u>2,398</u>
Total revenues	<u>822,322</u>

Expenditures

Current:	
Affordable housing	<u>408,140</u>
Total expenditures	<u>408,140</u>

Net change in fund balance 414,182

Fund balance, beginning of year 24,446,214

Fund balance, end of year \$ 24,860,396

The accompanying notes are an integral part of these financial statements.

City of West Covina, California
West Covina Housing Authority Fund
Notes to the Financial Statements
For the year ended June 30, 2017

Note 1 – Organization and Summary of Significant Accounting Policies

The City of West Covina (the City) was incorporated on February 23, 1923, under the laws of the State of California and enjoys all the rights and privileges applicable to a general law city. It is governed by an elected five-member City Council.

The following is a summary of the significant accounting policies of the City as they pertain to the West Covina Housing Authority Fund (the Housing Authority). Only the Housing Authority information is included herein and these financial statements, therefore, do not purport to represent the financial position or results of operations of the City.

Basis of Accounting

These fund financial statements are reported using the modified-accrual basis of accounting. Under the modified-accrual basis of accounting, revenues are recognized when susceptible to accrual (i.e. when they are both measurable and available). “Measurable” means the amount of the transaction can be determined, and “available” means collectible within the current period or soon enough thereafter (within 60 days) to be used to pay liabilities of the current period. Expenditures are generally recognized in the accounting period in which the liability is incurred, if measurable.

Use of Estimates in the Preparation of Financial Statements

The financial statements have been prepared in accordance with generally accepted accounting principles and necessarily include amounts based on estimates and assumptions by management. Actual results could differ from those amounts.

Note 2 – Cash and Investments

Cash at June 30, 2017, consisted of the following:

	<u>Amount</u>
Pooled cash and investments	<u>\$ 5,620,355</u>

The City follows the practice of pooling cash and investments for all funds except for funds required to be held by outside fiscal agents under the provisions of bond indentures.

For more information on the City’s cash and investments as of June 30, 2017, please see the City’s Comprehensive Annual Financial Report.

City of West Covina, California
West Covina Housing Authority Fund
Notes to the Financial Statements
For the year ended June 30, 2017

Note 3 – Notes and Loans Receivable

As of June 30, 2017, the following notes and loans receivable were outstanding:

Housing rehabilitation	\$ 374,988
First time home buyers	285,700
Housing preservation program	712,697
Home improvement program	899,932
Lark Ellen Towers	6,130,701
Executive Lodge Apartments Limited Partnership	5,975,678
West Covina Senior Villas, LLC	2,833,333
West Covina Senior Villas II, L.P.	8,513,885
Other loans	642,892
Allowance for doubtful accounts	<u>(12,103,654)</u>
Total	<u><u>\$ 14,266,152</u></u>

Several housing rehabilitation loans totaling \$374,988 have been made to qualified applicants using Community Development Block Grants received by the City and housing set-aside funds of the former Commission's redevelopment activities. These loans bear interest up to 5% and are repaid when title to the property changes. The City has included 5% of the balance in the allowance for doubtful accounts.

The Housing Authority has loans to first-time home buyers totaling \$285,700. Loans are secured by second trust deeds and bear interest at 5%. Principal and interest are deferred for five years and are due monthly in years 6 through 30. There were 20 individual loans outstanding at June 30, 2017, ranging from \$7,965 to \$22,407. The City has included 5% of the balance in the allowance for doubtful accounts.

The Housing Authority also has housing preservation loans to qualified applicants using housing set-aside funds totaling \$712,697. Principal and interest are deferred for ten years; after the tenth year loans bear interest at 5%. Loans are repaid after the tenth year or when title to the property changes. There were 84 individual loans outstanding at June 30, 2017, ranging from \$205 to \$10,659. The City has included 5% of the balance in the allowance for doubtful accounts.

Several housing improvement loans totaling \$899,932 have been made to qualified applicants. The loans are secured by second trust deeds. The City has included 5% of the balance in the allowance for doubtful accounts.

In May 1997, the Commission loaned \$4,270,000 to Lark Ellen Towers. The loan was transferred to the Housing Authority from the dissolved former Commission. The loan is secured by a deed of trust. The loan accrues interest at 3% per annum and requires annual payments equal to the maximum of \$35,000 or 50% of net profits earned by the project. The outstanding principal and accrued interest at June 30, 2017, is \$6,130,701.

City of West Covina, California
West Covina Housing Authority Fund
Notes to the Financial Statements
For the year ended June 30, 2017

Note 3 – Notes and Loans Receivable, (continued)

In April 1998, the Commission loaned \$5,622,300 to Executive Lodge Apartments Limited Partnership (Promenade Apartments project). The loan was transferred to the Housing Authority from the dissolved former Commission. The loan is secured by a deed of trust. The loan was amended and restated on April 1, 2017, with a principal of \$6,056,621 accruing interest at 2.82% compounded annually and requires annual payments equal to 50% of “Available Cash Flow”. The outstanding principal and accrued interest at June 30, 2017, is \$5,975,678.

In May 2002, the Commission loaned \$4,360,000 to West Covina Senior Villas, LLC. The loan is secured by a deed of trust. The loan does not accrue interest. The loan requires annual payments of \$141,667 through May 2032 that are forgiven by the City unless the borrower defaults on the agreement. The outstanding principal at June 30, 2017, is \$2,833,333. The loan is likely to be forgiven; therefore, the City has included the entire balance in the allowance for doubtful accounts.

In May 2009, the Commission entered into an agreement with West Covina Senior Villas II, L.P. to provide \$8,600,000 for the acquisition of real property in the City and construction and maintenance of an approximately 65-unit apartment complex to be rented to low income and very low income senior citizens. The loan is secured by a deed of trust. The loan does not accrue interest and is forgiven so long as the borrower does not default on the loan. The outstanding principal at June 30, 2017, is \$8,513,885. The loan is likely to be forgiven; therefore, the City has included the entire balance in the allowance for doubtful accounts.

Other notes consist of affordable housing loans of \$400,000. The notes do not accrue interest and are forgiven unless the borrower sells or refinances the property. Additionally, the balance included a note of \$242,892 for low income housing which accrues no interest and is forgivable if the owner maintains the low and moderate income housing status. The outstanding principal of these loans combined at June 30, 2017, is \$642,892. The loan is likely to be forgiven; therefore, the City has included the entire balance in the allowance for doubtful accounts.

City of West Covina, California
West Covina Housing Authority Fund
Notes to the Financial Statements
For the year ended June 30, 2017

Note 4 – Advances to the Successor Agency of the City of West Covina

Prior to the dissolution of the Commission's redevelopment activities on February 1, 2012, the City authorized several advances to be used for completing redevelopment projects throughout the community. As a result of the dissolution, the liabilities related to these advances were transferred to the Successor Agency. At June 30, 2017, the outstanding receivable side of these advances was as follows:

- (a) In May 2010, the Commission made an advance of \$6,529,308 from its housing assets to satisfy the Commission's Supplemental Educational Revenue Augmentation Fund (SERAF) obligation as allowed by Assembly Bill ABX4-26. The advance bears no interest. In May 2011, the Commission made an advance of \$1,344,269 from its housing assets to satisfy SERAF obligation as allowed by Assembly Bill ABX4-26. On February 1, 2012, these advances receivables were transferred to the Housing Authority. The advance bears no interest and the outstanding balance at June 30, 2017, was \$3,264,186.
- (b) The General Fund of the City has made several advances to the Commission totaling \$8,100,000 for administrative and capital improvement construction costs. Eighty percent (80%) of the balance is reported in the City's General Fund and remaining twenty percent (20%) balance is reported in the Housing Authority. The outstanding balance at June 30, 2017, is \$1,593,764.

With regard to repayment of the SERAF advances, repayment was authorized to begin in the 2014-15 fiscal year, and annual repayments are capped pursuant to a statutory formula.

Successor Agency and the Housing Authority management believes, in consultation with legal counsel, that the SERAF advances are enforceable obligations payable by the Successor Agency under the Dissolution Act's repayment restrictions. Therefore, the Housing Authority has not recorded an allowance for uncollectible advances. That said, the Dissolution Act is a complicated statutory scheme and the State and local agency implementation thereof has been the subject of substantial dispute and litigation. As such, repayment of the SERAF advances cannot be guaranteed.

City of West Covina, California
West Covina Housing Authority Fund
Notes to the Financial Statements
For the year ended June 30, 2017

Note 5 – Fund Balance

The following classifications describe the relative strength of the spending constraints placed on the purposes for which resources can be used:

- Nonspendable – amounts that are not in a spendable form (such as inventory) or are required to be maintained intact.
- Restricted – amounts constrained to specific purposes by their providers (such as grantors, bondholders and higher levels of government), through constitutional provisions or by enabling legislation.
- Committed – amounts constrained to specific purposes by a government itself, using the highest level of decision-making authority; to be reported as committed, amounts cannot be used for any other purpose unless the government takes the same highest level action to remove or change the constraint.
- Assigned – amounts a government intends to use for a specific purpose; intent can be expressed by the governing body or by an official or body to which the governing body delegates the authority.
- Unassigned – amounts that are for any purpose; positive amounts are reported only in a general fund.

The City Council establishes (and modifies or rescinds) fund balance commitments by passage of an ordinance or resolution. The Director of Finance has the authority, granted by the Council, to assign City resources. When both restricted and unrestricted resources are available for use when an expenditure is incurred, it is the City’s policy to use restricted resources first, then unrestricted resources as they are needed. It is also the City’s policy to consider committed amounts as being reduced first, followed by assigned amounts and then unassigned amounts when expenditures are incurred for purposes for which amounts in any of those unrestricted fund balance classifications could be used.

The Housing Authority’s governmental fund balance at June 30, 2017, is presented below:

	West Covina Housing Authority Fund
Nonspendable:	
Prepays	\$ 122,500
Advances to Successor Agency	4,857,950
Restricted for:	
Affordable housing	19,879,946
Total fund balance	\$ 24,860,396

REQUIRED SUPPLEMENTARY INFORMATION

City of West Covina, California
West Covina Housing Authority Fund
Budgetary Comparison Schedule
For the year ended June 30, 2017

	Budgeted Amounts		Actual	Variance with Final Budget Positive (Negative)
	Original	Final		
REVENUES				
Investment income	\$ -	\$ -	\$ 819,924	\$ 819,924
Other revenues	-	-	2,398	2,398
Total revenues	-	-	822,322	822,322
EXPENDITURES				
Current:				
Affordable housing	731,019	774,842	408,140	366,702
Net change in fund balance	(731,019)	(774,842)	414,182	1,189,024
Fund balance, beginning of year	24,446,214	24,446,214	24,446,214	-
Fund balance, end of year	\$ 23,715,195	\$ 23,671,372	\$ 24,860,396	\$ 1,189,024

See accompanying note to required supplementary information.

City of West Covina, California
West Covina Housing Authority Fund
Note to Required Supplementary Information
For the year ended June 30, 2017

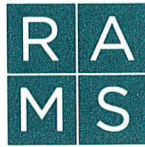
Note 1 – Budgetary Data

The annual budget adopted by the City Council provides for the general operation of the Housing Authority. The annual budget is adopted in summary by the City Council in June of each year. The resolution sets a combined appropriation of the fund for the operation of the Housing Authority.

The City Manager is authorized to transfer budgeted amounts between departments to ensure adequate and proper standards of service. Budgetary revisions, including supplemental appropriations which increase appropriations, must be approved by the City Council. The budgetary level of control is at the fund level. The budgeted figures used in the financial statements' budget to actual comparisons are the final amended amounts.

The budget is formally integrated into the accounting system and employed as a management control device during the year.

Budgets for governmental fund types are adopted on a basis consistent with generally accepted accounting principles. Operating appropriations lapse at the end of the fiscal year.



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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*

Independent Auditor's Report

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Brianna Schultz, CPA
Lisa Dongxue Guo, CPA, MSA

The Board of Directors
West Covina Housing Authority
West Covina, 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 West Covina Housing Authority Fund (the Housing Authority), (a component unit of the City of West Covina (the City), California), as of and for the year ended June 30, 2017, and the related notes to the financial statements, which collectively comprise the Housing Authority's basic financial statements, and have issued our report thereon dated December 12, 2017. The financial statements present only the Housing Authority and do not purport to, and do not, present fairly the financial position of the City.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Housing 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 opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Housing Authority's internal control. Accordingly, we do not express an opinion on the effectiveness of the Housing 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.

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Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting 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 Housing Authority's financial statements are free of 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 Housing Authority'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 Housing Authority's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Rogers, Anderson, Malody & Scott, LLP.

San Bernardino, California
December 12, 2017