

**City of Falcon Heights
Ramsey County, Minnesota**

Communications Letter

December 31, 2023

**City of Falcon Heights
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Report on Matters Identified as a Result of the Audit of the Basic Financial Statements

Honorable Mayor, Members
of the City Council and Management
Jack Linehan, City Administrator
Roland Olson, Finance Director
City of Falcon Heights
Falcon Heights, Minnesota

In planning and performing our audit of the basic financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Falcon Heights, Minnesota, as of and for the year ended December 31, 2023, 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, we considered the City's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control. Accordingly, we do not express an opinion on the effectiveness of the City's internal control over financial reporting.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and, therefore, material weaknesses or significant deficiencies may exist that have not been identified. In addition, because of inherent limitations in internal control, including the possibility of management override of controls, misstatements due to error, or fraud may occur and not be detected by such controls.

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 over financial reporting, such that there is a reasonable possibility that a material misstatement of the City's basic financial statements will not be prevented, or detected and corrected, on a timely basis. A reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows:

- ◆ *Reasonably possible*. The chance of the future event or events occurring is more than remote but less than likely.
- ◆ *Probable*. The future event or events are likely to occur.

We did not identify any deficiencies in internal control that we consider to be material weaknesses.

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. The significant deficiency identified is stated within this letter.

The accompanying memorandum also includes financial analysis provided as a basis for discussion. The matters discussed herein were considered by us during our audit and they do not modify the opinion expressed in our Independent Auditor's Report dated April 23, 2024, on such statements.

The purpose of this communication, which is an integral part of our audit, is to describe for the information and use of management, the City Council, and others within the City and state oversight agencies the scope of our testing of internal control and the results of the testing. Accordingly, this communication is not intended to be and should not be used for any other purpose.

BerganKDV, Ltd.

Minneapolis, Minnesota
April 23, 2024

City of Falcon Heights Significant Deficiency

Lack of Segregation of Accounting Duties

The City continued to evaluate and improve the segregation of accounting duties among City staff during 2023. Because of a limited number of office personnel, some areas of internal control still remain without proper segregation of accounting duties; however, we can report on the following processes. The lack of adequate segregation of accounting duties could adversely affect the City's ability to initiate, record, process, and report financial data consistent with the assertions of management in the financial statements.

Revenue Cycle

The four areas of segregation in the revenue cycle include mailroom custody, treasurer custody, accounts receivable, and accounting.

We noted some overlap in the mailroom and treasurer custody, with one employee having job responsibilities in both areas.

We also noted overlapping duties between accounts receivable and accounting, in that the person responsible for accounts receivable also is responsible for bank reconciliations.

Purchasing Cycle

The five areas of segregation in the purchasing cycle include purchasing authorization, receiving authorization, accounts payable, treasurer responsibilities, and accounting.

We noted proper segregation between the responsibility of purchasing goods and services, the individual responsible for preparing the purchase order, and the person responsible for approving the purchase order. However, we noted overlapping duties with the approval of purchase orders, input of invoices, and preparing of disbursements being performed by one individual.

Payroll Cycle

The five areas of segregation in the payroll cycle include human resources authorization, immediate supervisor authorization, payroll recording, paymaster custody, and accounting.

In addition to having responsibilities in payroll recording, paymaster custody, and accounting cycles noted above, the Finance Director has full general ledger access and the ability to write and post journal entries. While we believe this access is necessary to efficiently perform the financial duties required, this access has the ability to override many of the controls and segregation listed above.

Journal Entries

The three areas of segregation in journal entries include an employee to write the journal entry, another to post the entry, and finally another employee to review the entry.

We noted some journal entries were not approved by someone other than the person writing the entry.

We recommend a second review/approval to ensure accuracy.

**City of Falcon Heights
Significant Deficiency**

Lack of Segregation of Accounting Duties (Continued)

Bank Reconciliation Process

The two areas of segregation include an employee to prepare the cash reconciliation and another employee to review the reconciliation; ideally, the individual preparing the reconciliation has limited involvement in the revenue and purchasing cycles.

We noted the Finance Director has primary responsibility for bank reconciliations. These are generally delegated to other staff, however, still completed by the Finance Director to ensure accuracy.

We recommend each reconciliation be reviewed to help ensure accuracy.

City of Falcon Heights Required Communication

We have audited the basic financial statements of the governmental activities, business-type activities, each major fund, and the aggregate remaining fund information of the City as of and for the year ended December 31, 2023. Professional standards require that we advise you of the following matters related to our audit.

Our Responsibility in Relation to the Financial Statement Audit

As communicated in our engagement letter, our responsibility, as described by professional standards, is to form and express opinions about whether the basic financial statements 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 basic financial statements does not relieve you or management of its 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 basic financial statements are free of material misstatement. An audit of the basic 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 City'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 judgement, 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.

Generally accepted accounting principles provide for certain Required Supplementary Information (RSI) to supplement the basic financial statements. Our responsibility with respect to the RSI, which supplements the basic financial statements, is to apply certain limited procedures in accordance with generally accepted auditing standards. However, the RSI was not audited and, because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance, we do not express an opinion or provide any assurance on the RSI.

Our responsibility for the supplementary information accompanying the basic financial statements, as described by professional standards, is to evaluate the presentation of the supplementary information in relation to the basic financial statements as a whole and to report on whether the supplementary information is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Planned Scope and Timing of the Audit

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

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.

City of Falcon Heights Required Communication

Significant Risks Identified

We have identified the following significant risks of material misstatement:

- ◆ Improper Revenue Recognition - Revenue recognition is considered a fraud risk on substantially all engagements as it generally has a significant impact on the results of the governments operations. In addition, complexities exist surrounding the calculation and recording of various revenue sources.
- ◆ Management Override of Controls - Overall Financial Statements - Management override of internal control is considered a risk in substantially all engagements as management may be incentivized to produce better results.
- ◆ Pension Valuation - Net Pension Liability, Deferred Outflows of Resources Related to Pensions, and Deferred Inflows of Resources Related to Pensions are generally material to the financial statements and involve significant estimates.
- ◆ Misappropriation of Assets - Misappropriation of assets is considered a risk in substantially all engagements as assets may be misappropriated due to fraud or error.

Qualitative Aspects of the City'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 the notes to the basic financial statements. There have been no initial selection of accounting policies and no changes to significant accounting policies or their application during 2023. 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 basic financial statements prepared by management and are based on management's current judgements. Those judgements 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 basic financial statements and because of the possibility that future events affecting them may differ markedly from management's current judgements. The most sensitive estimates affecting the basic financial statements relate to:

Net Pension Liability, Deferred Outflows of Resources Related to Pensions and Deferred Inflows of Resources Related to Pensions - These balances are based on an allocation by the pension plans using estimates based on contributions.

We evaluated the key factors and assumptions used to develop the 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.

Financial Statement Disclosures

Certain basic financial statement disclosures involve significant judgment and are particularly sensitive because of their significance to financial statement users. The basic financial statement disclosures are neutral, consistent, and clear.

City of Falcon Heights Required Communication

Significant Difficulties Encountered during the Audit

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

Uncorrected and Corrected Misstatements

For the 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 effects of uncorrected misstatements related to prior periods on the relevant classes of transactions, account balances or disclosures, and the basic financial statements taken as a whole and each applicable opinion unit.

Management did not identify, and we did not notify them of any uncorrected financial statement misstatements.

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 basic financial statements or the auditor's report. No such disagreements arose during the course of our audit.

Representations Requested from Management

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

Management's Consultations with Other Accountants

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

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, significant events or transactions that occurred during the year, operating and regulatory conditions affecting the City, 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 auditor.

Other Information Included in Annual Reports

Pursuant to professional standards, our responsibility as auditors for other information, whether financial or nonfinancial, included in the City's annual reports, does not extend beyond the information identified in the audit report, and we are not required to perform any procedures to corroborate such other information.

We applied certain limited procedures to the 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.

**City of Falcon Heights
Required Communication**

Other Information Included in Annual Reports (Continued)

With respect to the supplementary information accompanying the financial statements, 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 financial statements. We compared and reconciled the supplementary information to the underlying accounting records used to prepare the basic financial statements or to the basic financial statements themselves.

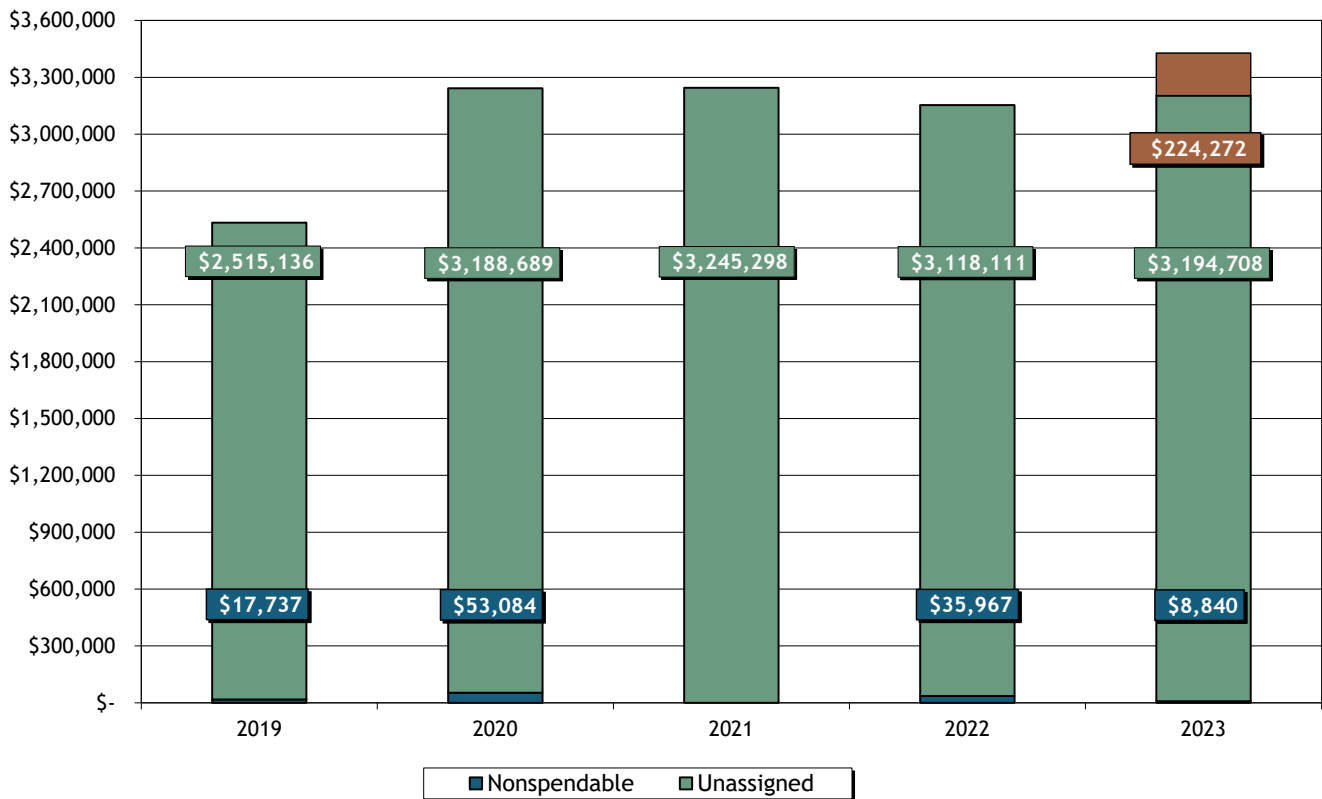
City of Falcon Heights Financial Analysis

The following pages provide graphic representation of select data pertaining to the financial position and operations of the City for the past five years. Our analysis of each graph is presented to provide a basis of discussion of past performance and how implementing certain changes may enhance future performance.

General Fund Balance

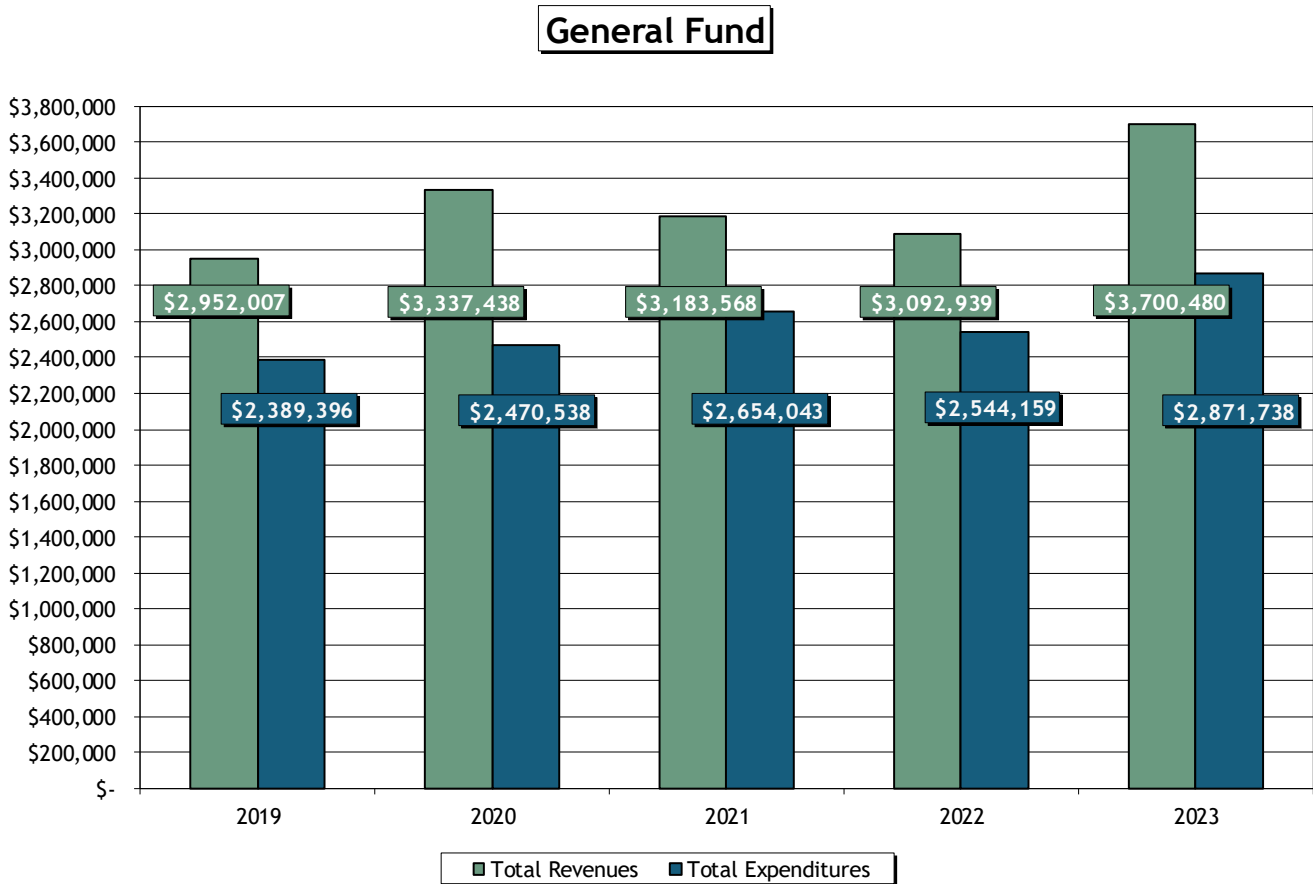
At December 31, 2023, the General Fund balance was \$3,427,820 which is an increase of \$273,742 from 2022. Based on current expenditure levels, the fund balance represents over a year of expenditures.

General Fund Balance



City of Falcon Heights Financial Analysis

General Fund

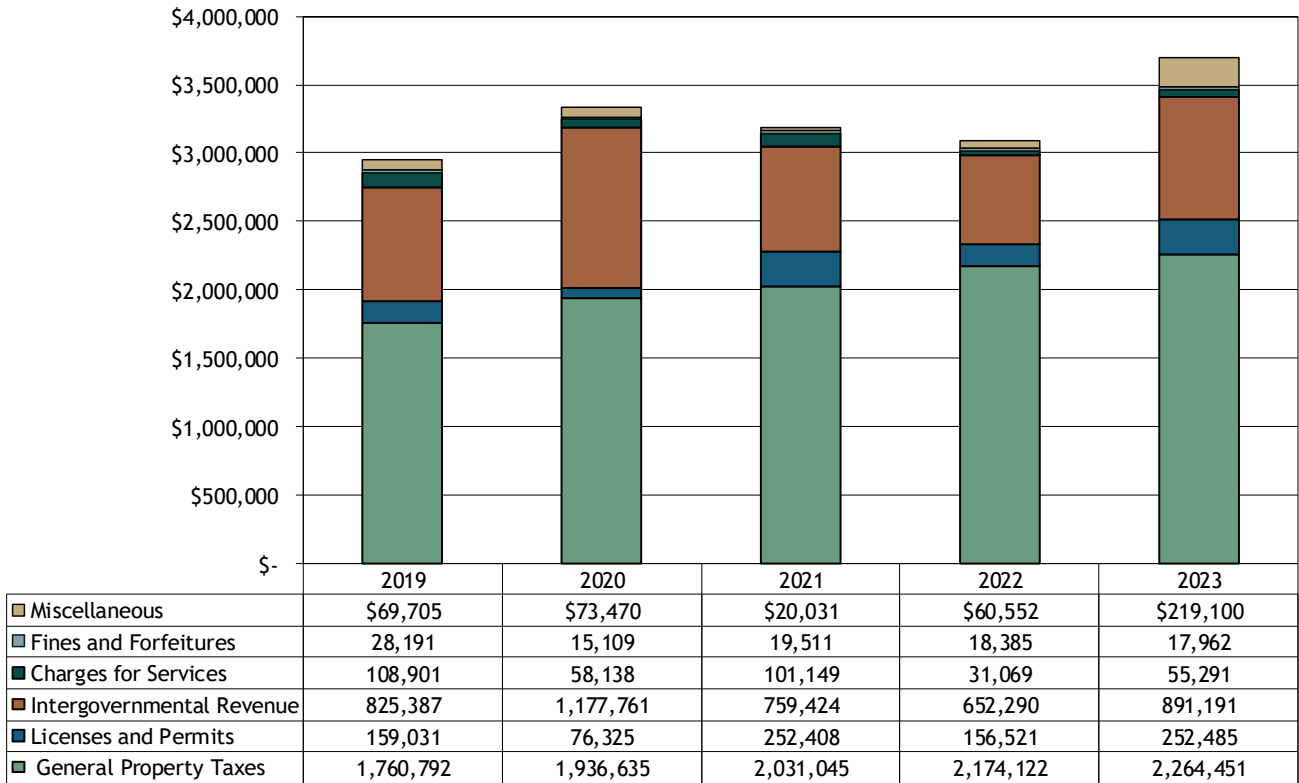


General Fund revenues increased by \$607,541, or 19.6%, in 2023. Expenditures in the General Fund increased by \$327,579, or 12.9%, and resulted in total revenues exceeding expenditures by \$828,742. Further detailed explanations regarding variances will follow in subsequent charts.

**City of Falcon Heights
Financial Analysis**

General Fund Revenues

General Fund Revenues



Intergovernmental revenue increased \$238,901 as a result of receiving additional public safety aid that was new in 2023. Miscellaneous revenues increased \$158,548 from the prior year due to receiving more interest income with better market conditions in 2023. Licenses and permit revenues increased \$95,964 due to an increase in building permits. Property tax revenue increased \$90,329 due to an increase in levy.

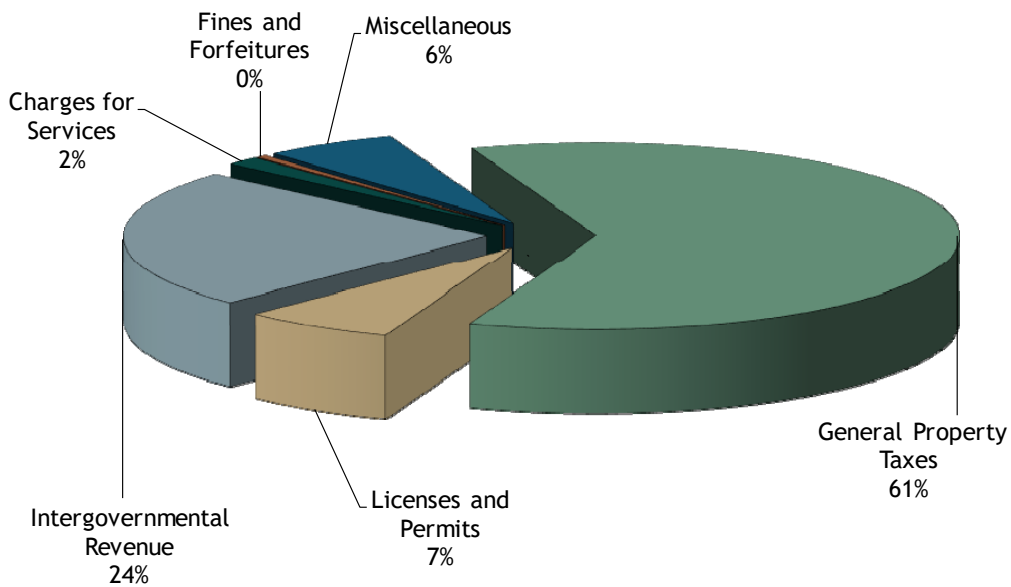
The other remaining General Fund revenues in 2023 stayed relatively consistent with the prior year.

City of Falcon Heights Financial Analysis

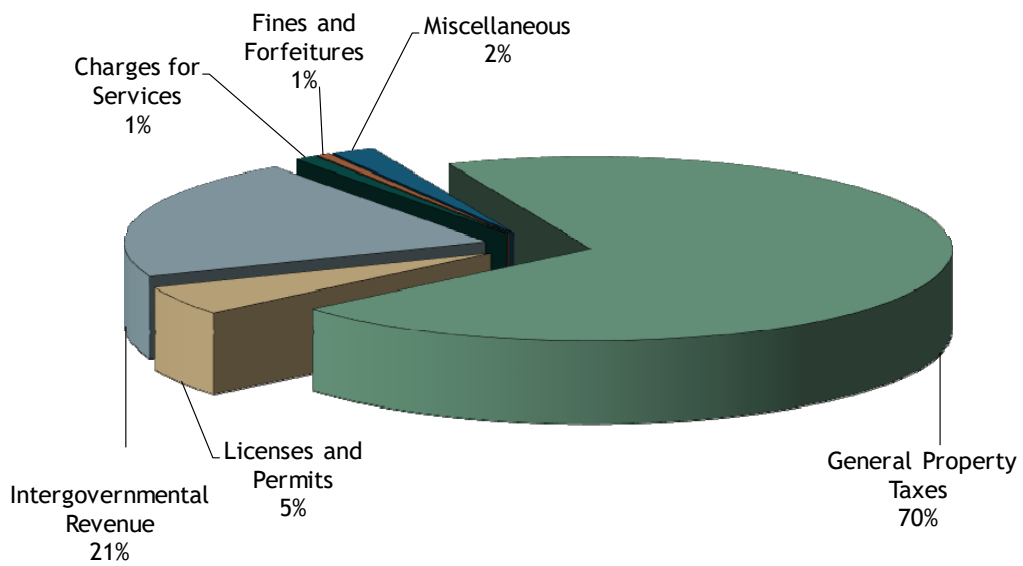
General Fund Revenues (Continued)

The following charts depict the components of the General Fund revenues by percentages:

General Fund Revenues 2023



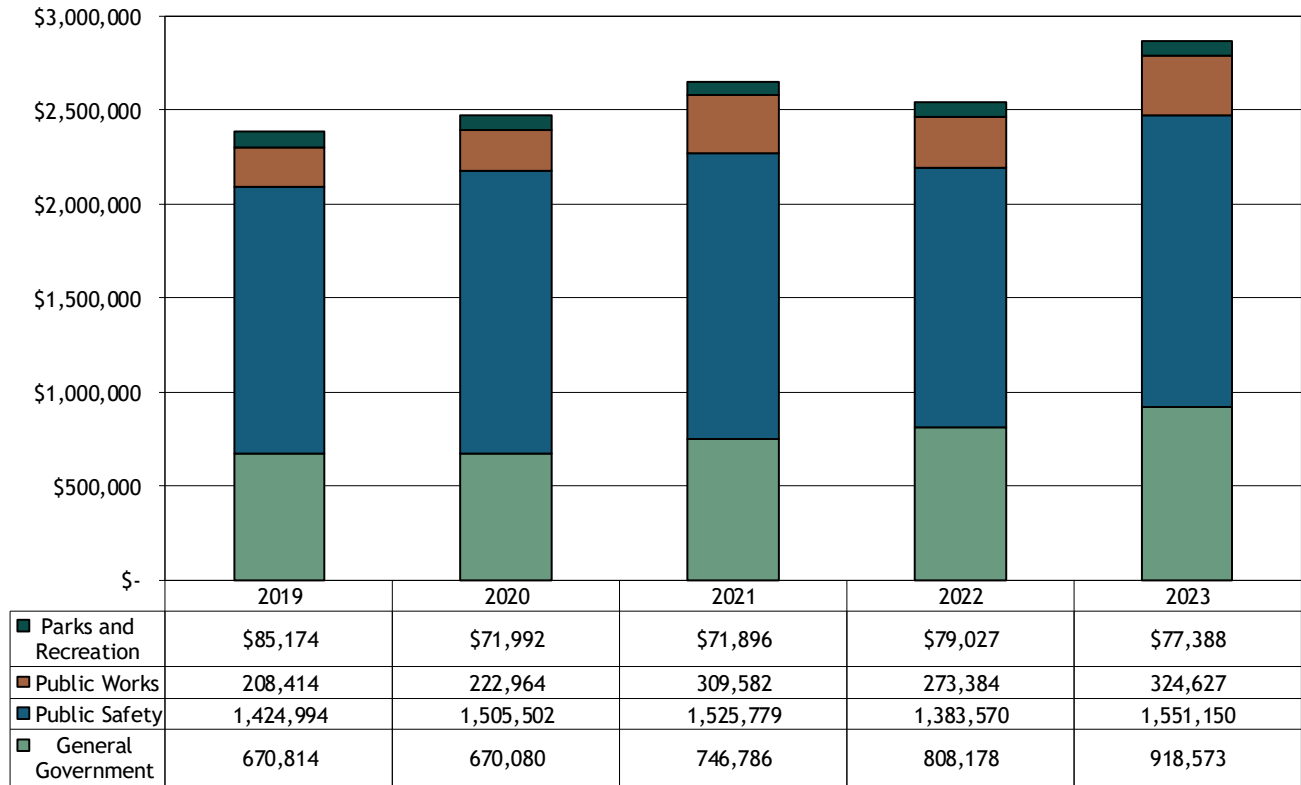
General Fund Revenues 2022



**City of Falcon Heights
Financial Analysis**

General Fund Expenditures

General Fund Expenditures



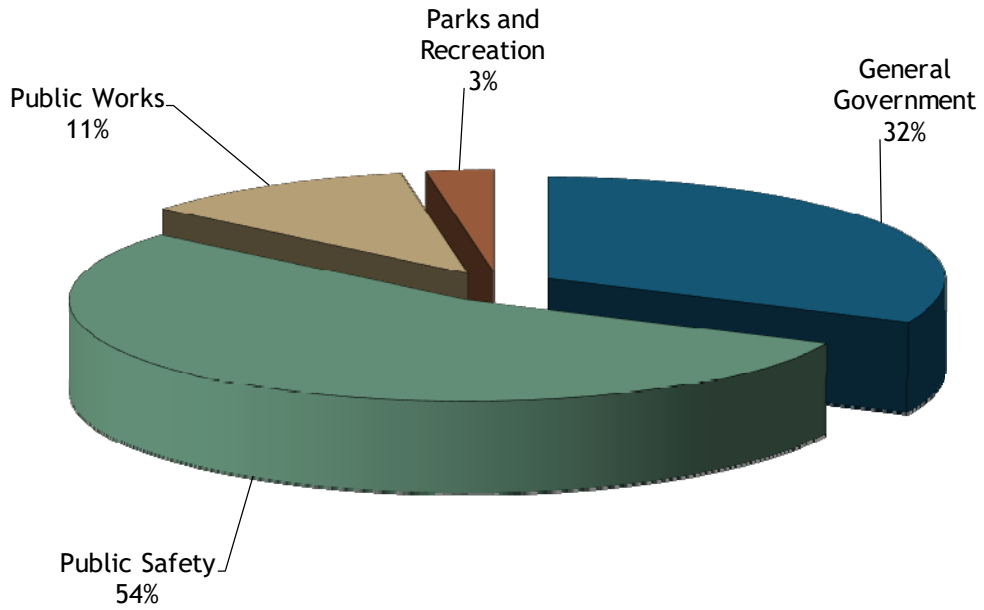
In 2023, expenditures increased \$327,579, or 12.9%, from 2022. Public safety expenditures increased \$167,580, or 12.1% in 2023. This was related to an increase in police service during the year. General government expenditures increased \$110,395 as a result of more consulting fees as well as normal salary increases. Public works increased \$51,243 due to more tree maintenance in 2023.

Other expenditures stayed relatively consistent with the prior year.

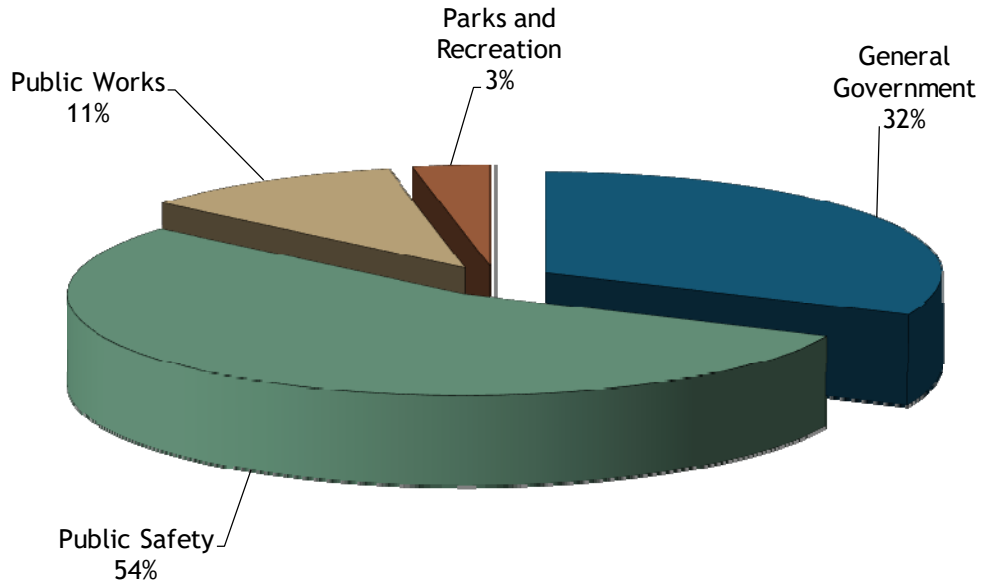
City of Falcon Heights
Financial Analysis

General Fund Expenditures (Continued)

General Fund Expenditures 2023



General Fund Expenditures 2022



**City of Falcon Heights
Financial Analysis**

General Fund Budget

	Original and Final Budget	Actual Amounts	Variance with Final Budget - Over (Under)
Revenues			
Taxes	\$ 2,284,612	\$ 2,264,451	\$ (20,161)
Tax increments	-	18,374	18,374
Licenses and permits	82,750	252,485	169,735
Intergovernmental	645,810	891,191	245,381
Charges for services	46,650	55,291	8,641
Fines and forfeitures	15,000	17,962	2,962
Miscellaneous	16,500	200,726	184,226
Total revenues	3,091,322	3,700,480	609,158
Expenditures			
General government	919,711	918,573	(1,138)
Public safety	1,560,276	1,551,150	(9,126)
Public works	352,045	324,627	(27,418)
Parks and recreation	104,290	77,388	(26,902)
Total expenditures	2,936,322	2,871,738	(64,584)
Excess of receipts over disbursements	155,000	828,742	673,742
Other Financing Sources (Uses)			
Transfers in	-	21,000	21,000
Transfers out	(176,000)	(576,000)	(400,000)
Net change in fund balance	\$ (21,000)	\$ 273,742	\$ 294,742

Overall, General Fund revenues were over budget by 19.7%, or \$609,158. The largest budget variance was in intergovernmental revenue, which exceeded budget amounts by \$245,381. This variance is a result of receiving public safety aid that was new in 2023 that was not anticipated. Miscellaneous revenue was over budget \$184,226 due to an increase in investment income as a result of better market conditions in 2023. Licenses and permits were over budget \$169,735 due to more building permits than anticipated. Other categories were relatively on budget.

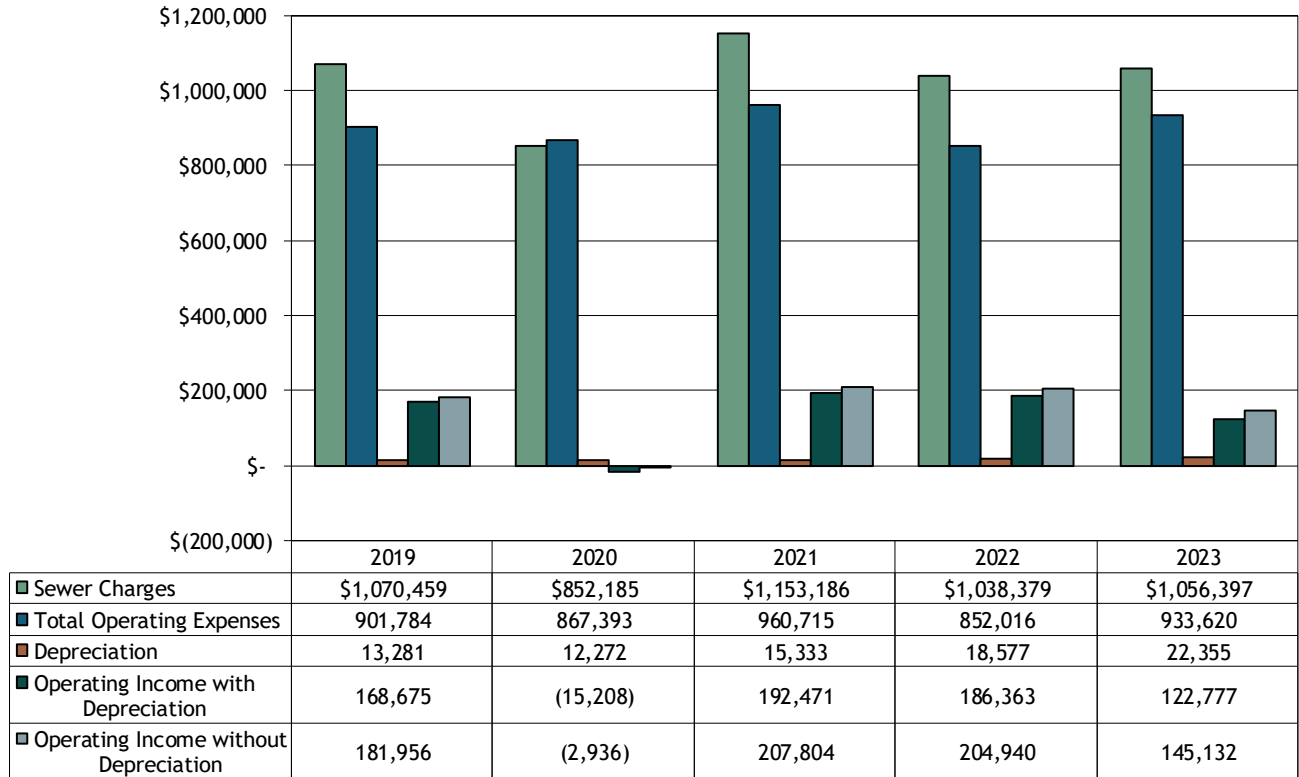
Expenditures were under budget by \$64,584, or 2.2%. All categories were relatively on budget.

**City of Falcon Heights
Financial Analysis**

Sanitary Sewer Fund

The graphs below and on the next page illustrate the current operations of the Sanitary Sewer and the Storm Drainage Funds.

Sanitary Sewer Fund



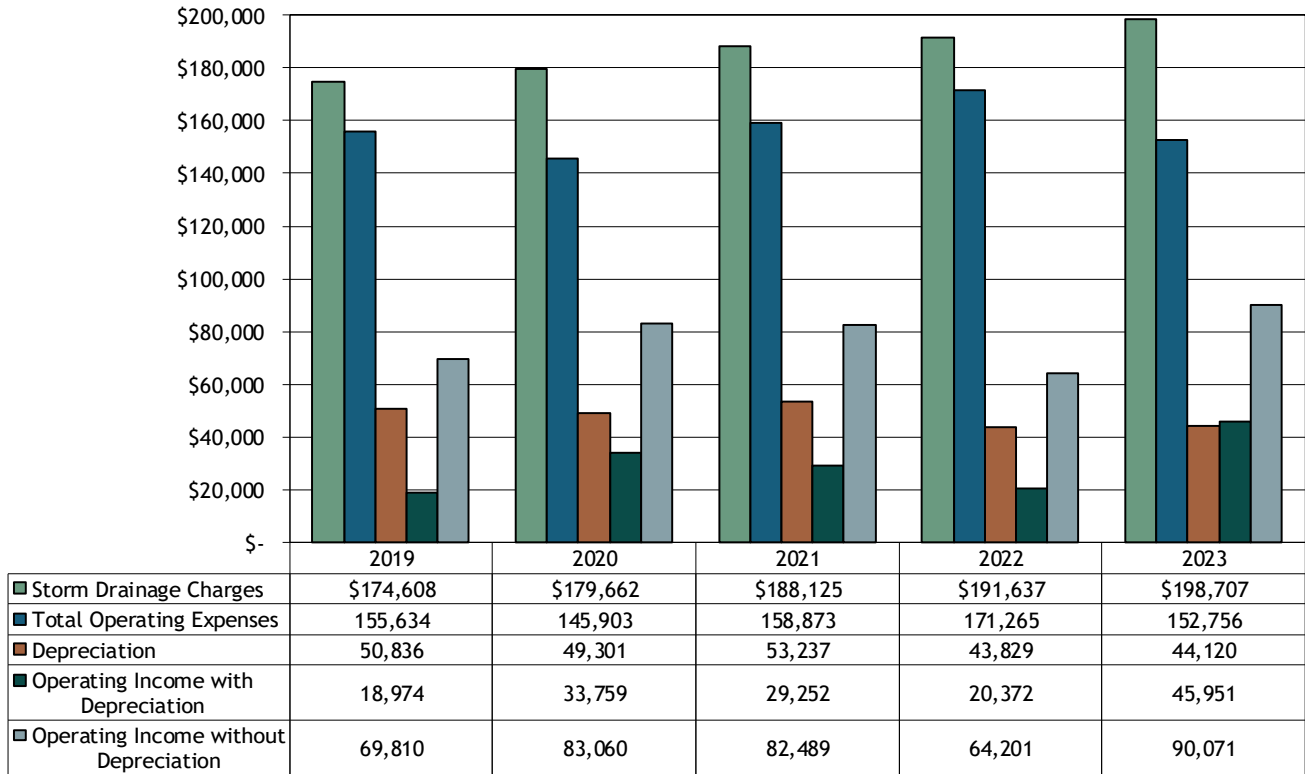
The Sanitary Sewer Fund realized operating income of \$122,777 during 2023. Sewer charges in 2023 increased by \$18,018 from 2022. This increase was primarily the result of a slight increase in fees.

With an operating income of \$122,777, \$722,326 in nonoperating revenue, the change in the Sanitary Sewer Fund net position was an increase of \$845,103. Total net position increased to \$3,831,843 in 2023. Of this amount, \$1,065,096 represents the net investment in capital assets and \$2,766,747 is unrestricted.

**City of Falcon Heights
Financial Analysis**

Storm Drainage Fund

Storm Drainage Fund



Storm sewer charges for services stayed relatively consistent with the prior year, increasing \$7,070. Operating expenses decreased in 2023 by \$18,509. The Storm Drainage Fund had operating income of \$45,951 in 2023.

With \$15,631 in investment income, the Storm Drainage Fund had a total increase in net position of \$61,582. Ending net position at December 31, 2023, was \$1,800,395. Of this amount, \$1,494,070 represents the net investment in capital assets and \$306,325 is unrestricted.

City of Falcon Heights Emerging Issues

Executive Summary

The following is an executive summary of financial related updates to assist you in staying current on emerging issues in accounting and finance. This summary will give you a preview of the new standards that have been recently issued and what is on the horizon for the near future. The most recent and significant updates include:

- ◆ **Implementation Guide No. 2021-1 - Amending Capitalization Requirements**
GASB has issued Implementation Guide No. 2021-1, amending previously issued guidance regarding capitalization requirements for capital assets that are significant in the aggregate but below the government's capitalization threshold individually.
- ◆ **Accounting Standard Update - GASB Statement No. 100 - Accounting Changes and Error Corrections**
GASB has issued GASB Statement No. 100 relating to accounting and financial reporting for accounting changes and error corrections. The requirements of this Statement will improve the clarity of the accounting and financial reporting requirements for accounting changes and error corrections, which will result in greater consistency in application in practice. In turn, more understandable, reliable, relevant, consistent, and comparable information will be provided to financial statement users for making decisions or assessing accountability.
- ◆ **Accounting Standard Update - GASB Statement No. 101 - Compensated Absences**
GASB has issued GASB Statement No. 101 relating to accounting and financial reporting for compensated absences. The unified recognition and measurement model in this Statement will result in a liability for compensated absences that more appropriately reflects when a government incurs an obligation. In addition, the model can be applied consistently to any type of compensated absence and will eliminate potential comparability issues between governments that offer different types of leave.

The following are extensive summaries of the current updates. As your continued business partner, we are committed to keeping you informed of new and emerging issues. We are happy to discuss these issues with you further and its applicability to your City.

Implementation Guide No. 2021-1 - Amending Capitalization Requirements

Implementation Guide No. 2021-1, amended previously issued guidance contained in Implementation Guide No. 2015-1 regarding capitalization requirements for capital assets that are significant in the aggregate.

Original guidance stated that it *may be* appropriate for a government to establish a capitalization policy that would require capitalization for certain types of assets with individual acquisition costs that are less than the threshold for an individual asset.

Amended guidance states that a government *should* capitalize assets whose individual acquisition costs are less than the threshold for an individual asset if those assets in the aggregate are significant. Computers and classroom furniture are common examples of asset types that could be significant collectively. The amended guidance clarifies that if 100 computers costing \$1,500 each totaling a \$150,000 aggregate amount is significant, the government *should* capitalize the computers.

Information provided above was obtained from www.gasb.org.

City of Falcon Heights Emerging Issues

Accounting Standard Update - GASB Statement No. 100 - *Accounting Changes and Error Corrections - an Amendment of GASB Statement No. 62*

The primary objective of this Statement is to enhance accounting and financial reporting requirements for accounting changes and error corrections to provide more understandable, reliable, relevant, consistent, and comparable information for making decisions or assessing accountability.

This Statement defines accounting changes as changes in accounting principles, changes in accounting estimates, and changes to or within the financial reporting entity and describes the transactions or other events that constitute those changes. As part of those descriptions, for (1) certain changes in accounting principles and (2) certain changes in accounting estimates that result from a change in measurement methodology, a new principle or methodology should be justified on the basis that it is preferable to the principle or methodology used before the change. That preferability should be based on the qualitative characteristics of financial reporting - understandability, reliability, relevance, timeliness, consistency, and comparability. This Statement also addresses corrections of errors in previously issued financial statements.

This Statement prescribes the accounting and financial reporting for (1) each type of accounting change and (2) error corrections. This Statement requires that (a) changes in accounting principles and error corrections be reported retroactively by restating prior periods, (b) changes to or within the financial reporting entity be reported by adjusting beginning balances of the current period, and (c) changes in accounting estimates be reported prospectively by recognizing the change in the current period. The requirements of this Statement for changes in accounting principles apply to the implementation of a new pronouncement in absence of specific transition provisions in the new pronouncement.

This Statement also requires that the aggregate amount of adjustments to and restatements of beginning net position, fund balance, or fund net position, as applicable, be displayed by reporting unit in the financial statements.

This Statement requires disclosure in notes to financial statements of descriptive information about accounting changes and error corrections, such as their nature. In addition, information about the quantitative effects on beginning balances of each accounting change and error correction should be disclosed by reporting unit in a tabular format to reconcile beginning balances as previously reported to beginning balances as restated.

Furthermore, this Statement addresses how information that is affected by a change in accounting principle or error correction should be presented in Required Supplementary Information (RSI) and Supplementary Information (SI). For periods that are earlier than those included in the basic financial statements, information presented in RSI or SI should be restated for error corrections, if practicable, but not for changes in accounting principles.

GASB Statement No. 100 is effective for reporting periods beginning after June 15, 2023. Earlier application is encouraged.

Information provided above was obtained from www.gasb.org.

City of Falcon Heights Emerging Issues

Accounting Standard Update - GASB Statement No. 101 - *Compensated Absences*

The objective of this Statement is to better meet the information needs of financial statement users by updating the recognition and measurement guidance for compensated absences. That objective is achieved by aligning the recognition and measurement guidance under a unified model and by amending certain previously required disclosures.

This Statement requires that liabilities for compensated absences be recognized for (1) leave that has not been used and (2) leave that has been used but not yet paid in cash or settled through noncash means. A liability should be recognized for leave that has not been used if (a) the leave is attributable to services already rendered, (b) the leave accumulates, and (c) the leave is more likely than not to be used for time off or otherwise paid in cash or settled through noncash means. Leave is attributable to services already rendered when an employee has performed the services required to earn the leave. Leave that accumulates is carried forward from the reporting period in which it is earned to a future reporting period during which it may be used for time off or otherwise paid or settled. In estimating the leave that is more likely than not to be used or otherwise paid or settled, a government should consider relevant factors such as employment policies related to compensated absences and historical information about the use or payment of compensated absences. However, leave that is more likely than not to be settled through conversion to defined benefit postemployment benefits should not be included in a liability for compensated absences.

This Statement requires that a liability for certain types of compensated absences - including parental leave, military leave, and jury duty leave - not be recognized until the leave commences. This Statement also requires that a liability for specific types of compensated absences not be recognized until the leave is used.

This Statement also establishes guidance for measuring a liability for leave that has not been used, generally using an employee's pay rate as of the date of the financial statements. A liability for leave that has been used but not yet paid or settled should be measured at the amount of the cash payment or noncash settlement to be made. Certain salary-related payments that are directly and incrementally associated with payments for leave also should be included in the measurement of the liabilities.

With respect to financial statements prepared using the current financial resources measurement focus, this Statement requires that expenditures be recognized for the amount that normally would be liquidated with expendable available financial resources.

This Statement amends the existing requirement to disclose the gross increases and decreases in a liability for compensated absences to allow governments to disclose only the net change in the liability (as long as they identify it as a net change). In addition, governments are no longer required to disclose which governmental funds typically have been used to liquidate the liability for compensated absences.

GASB Statement No. 101 is effective for reporting periods beginning after December 15, 2023. Earlier application is encouraged.

Information provided above was obtained from www.gasb.org.