

Honorable Mayor and Members
of the City Council
City of Hercules
Hercules, California

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of City of Hercules as of and for the year ended June 30, 2018, and have issued our report thereon dated December 28, 2018. We have previously communicated to you information about our responsibilities under auditing standards generally accepted in the United States of America, *Government Auditing Standards*, and Title 2 U.S. *Code of Federal Regulations Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance), as well as certain information related to the planned scope and timing of our audit. Professional standards also require that we communicate to you the following information related to our audit.

Significant audit findings

Qualitative aspects of accounting practices

Accounting policies

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by City of Hercules are described in Note 1 to the financial statements.

The City changed accounting policies related to Postemployment Benefits Other Than Pensions (OPEB) by adopting Governmental Accounting Standards Board (GASB) Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other than Pensions*. The cumulative effect of the change resulted in a decrease to net position of \$1 million as of the beginning of the fiscal year.

We noted no transactions entered into by the entity during the year for which there is a lack of authoritative guidance or consensus. All significant transactions have been recognized in the financial statements in the proper period.

Accounting estimates

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimate(s) affecting the financial statements was (were):

- Management believes receivables are fully collectible based on historical experience. Accordingly, no allowance for doubtful accounts is included in the financial statements.
- Management's estimate of risk liability is derived from actuarial valuations obtained from experts. We compared the claims liability reported in the financial statements to those reported in actuarial reports prepared and issued during the year being audited. Considering the total

liability at year-end is based on a third-party actuarial, the liability amount was deemed reasonable.

- Management's estimate of OPEB liability is derived from actuarial valuations obtained from experts. We compared the liability reported in the financial statements to the actuarial report prepared and issued for the year under audit. Considering the total liability at year-end is based on a third-party actuarial, the liability amount was deemed reasonable.
- Management's estimate of pension liability is derived from actuarial valuations obtained from PERS. We compared the liability reported in the financial statements to the actuarial report prepared and issued for the year under audit and tested underlying census data.
- With the dissolution of the redevelopment agency on February 1, 2012 there is uncertainty as to whether the City's funds will be repaid the accumulated \$51.1 million in loans owed by the Agency, now a private purpose trust fund of the City. Management is currently working with the State Department of Finance to determine the outcome of these loans. The possible outcome of this matter cannot presently be determined. Accordingly, no provision for any allowance for doubtful accounts has been made in the financial statements for possible forgiveness of these loans.

Financial statement disclosures

Certain financial statement disclosures are particularly sensitive because of their significance to financial statement users. There were no particularly sensitive financial statement disclosures.

The financial statement disclosures are neutral, consistent, and clear.

Difficulties encountered in performing the audit

We encountered no significant difficulties in dealing with management in performing and completing our audit.

Uncorrected misstatements

Professional standards require us to accumulate all misstatements identified during the audit, other than those that are clearly trivial, and communicate them to the appropriate level of management. The attached schedule summarizes uncorrected misstatements of the financial statements. Management has determined that their effects are immaterial, both individually and in the aggregate, to the financial statements taken as a whole.

Corrected misstatements

The attached schedule summarizes all misstatements (material and immaterial) detected as a result of audit procedures that were corrected by management.

Disagreements with management

For purposes of this letter, a disagreement with management is a financial accounting, reporting, or auditing matter, whether or not resolved to our satisfaction, that could be significant to the financial statements or the auditors' report. No such disagreements arose during our audit.

Management representations

We have requested certain representations from management that are included in the management representation letter dated December 28, 2018.

Management consultations with other independent accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a “second opinion” on certain situations. If a consultation involves application of an accounting principle to the entity’s financial statements or a determination of the type of auditors’ opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Significant issues discussed with management prior to engagement

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to engagement as the entity’s auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our engagement.

Other information in documents containing audited financial statements

With respect to the required supplementary information (RSI) accompanying the financial statements, we made certain inquiries of management about the methods of preparing the RSI, including whether the RSI has been measured and presented in accordance with prescribed guidelines, whether the methods of measurement and preparation have been changed from the prior period and the reasons for any such changes, and whether there were any significant assumptions or interpretations underlying the measurement or presentation of the RSI. We compared the RSI for consistency with management’s responses to the foregoing inquiries, the basic financial statements, and other knowledge obtained during the audit of the basic financial statements. Because these limited procedures do not provide sufficient evidence, we did not express an opinion or provide any assurance on the RSI.

With respect to the schedule of expenditures of federal awards (SEFA) accompanying the financial statements, on which we were engaged to report in relation to the financial statements as a whole, we made certain inquiries of management and evaluated the form, content, and methods of preparing the SEFA to determine that the SEFA complies with the requirements of the Uniform Guidance, the method of preparing it has not changed from the prior period or the reasons for such changes, and the SEFA is appropriate and complete in relation to our audit of the financial statements. We compared and reconciled the SEFA to the underlying accounting records used to prepare the financial statements or to the financial statements themselves. We have issued our report thereon dated December 28, 2018.

Our auditors’ opinion, the audited financial statements, and the notes to financial statements should only be used in their entirety. Inclusion of the audited financial statements in a document you prepare, such as an annual report, should be done only with our prior approval and review of the document.

Honorable Mayor and Members of the City Council
City of Hercules
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This communication is intended solely for the information and use of the Honorable Mayor, Members of the City Council and management of City of Hercules and is not intended to be, and should not be, used by anyone other than these specified parties.

A handwritten signature in black ink that reads "CliftonLarsonAllen LLP". The signature is written in a cursive, flowing style.

CliftonLarsonAllen LLP

Roseville, California
December 28, 2018

Client: 205-49920000 - Hercules City
Engagement: AUD 2018 - City of Hercules
Period Ending: 6/30/2018
Trial Balance: 0900.00 - TB
Workpaper:
Fund Level: All
Index: All

Account	Description	W/P Ref	Debit	Credit
Adjusting Journal Entries				
Adjusting Journal Entries JE # 103		1305.02		
HB - to adjust unavalable revenue posted as revenue for amounts not received within the City's availability period				
CP02.4030	INTERGOVERNMENTAL REVENUES		770,009.00	
CP02.4030	INTERGOVERNMENTAL REVENUES		84,990.00	
CP02.2502	UNAVAILABLE REVENUES			772,850.00
CP02.4030	INTERGOVERNMENTAL REVENUES			82,149.00
Total			<u>854,999.00</u>	<u>854,999.00</u>
Adjusting Journal Entries JE # 104				
Adjusting Journal Entries JE # 104		1350.02		
HB - To record payment on BioRAD lease receivable during the year.				
DS02.2502	UNAVAILABLE REVENUES		108,315.00	
DS02.1272	LONG-TERM RECEIVABLES, LONG TERM			108,315.00
Total			<u>108,315.00</u>	<u>108,315.00</u>
Adjusting Journal Entries JE # 105				
Adjusting Journal Entries JE # 105		2500.10		
HB - To record accrued interest expense on WW loan as calculated by State Water Resources				
EN01.6110	DEBT SERVICE: INTEREST		244,598.00	
EN01.2103	ACCRUED INTEREST			244,598.00
Total			<u>244,598.00</u>	<u>244,598.00</u>
Adjusting Journal Entries JE # 903				
Adjusting Journal Entries JE # 903		1350-2500		
EZ - To eliminate LT receivable from State and LT loan payable for amounts not yet drawn down for wastewater expansion project (similar AJE in 2017)				
EN01.2732	NOTES PAYABLE, LONG TERM		10,154,838.00	
EN01.2732	NOTES PAYABLE, LONG TERM		1,179,668.00	
EN01.1251	NOTES/LOANS RECEIVABLE			10,154,838.00
EN01.1251	NOTES/LOANS RECEIVABLE			1,179,668.00
Total			<u>11,334,506.00</u>	<u>11,334,506.00</u>
Adjusting Journal Entries JE # 905				
Adjusting Journal Entries JE # 905		2500		
EZ - to reversed entry for accrued interest posted to GF - This is a LT liability and will be posted as a conversion entry.				
GF01.2103	ACCRUED INTEREST		442,778.00	
GF01.6110	DEBT SERVICE: INTEREST			442,778.00
Total			<u>442,778.00</u>	<u>442,778.00</u>

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Account	Description	W/P Ref	Debit	Credit
Proposed Journal Entries				
Proposed Journal Entries JE # 401		2400		
EZ - pass on reallocation of pension liability due to disaggregation on cost sharing plans				
EN01.1915	DEFERRED OUTFLOWS - PENSION		32,724.00	
EN01.2915	DEFERRED INFLOWS - PENSION		553.00	
EN01.8020	SERVICES AND SUPPLIES		116,361.00	
GB34.2796	PENSION LIABILITY		149,638.00	
EN01.2796	PENSION LIABILITY			149,638.00
GB34.1915	DEFERRED OUTFLOWS - PENSION			32,724.00
GB34.2915	DEFERRED INFLOWS - PENSION			553.00
GB34.6020	PUBLIC SAFETY			116,361.00
Total			<u>299,276.00</u>	<u>299,276.00</u>
Total Proposed Journal Entries			<u>299,276.00</u>	<u>299,276.00</u>
Total All Journal Entries			<u>299,276.00</u>	<u>299,276.00</u>