

**City Council Recessed Session
August 9, 2022**

The City Council of the City of Elizabeth City called their previously recessed meeting back to order on Tuesday, August 9, 2022 in Council Chambers, located on the 2nd floor of the Municipal Administration Building, 306 E. Colonial Avenue, Elizabeth City, NC.

MEMBERS PRESENT: Mayor E. Kirk Rivers
Mayor Pro Tem Kem Spence
Councilman Johnson Biggs
Councilman Joe Peel
Councilman Jarvis Gibbs
Councilwoman Rose Whitehurst
Councilwoman Barbara Baxter
Councilman Johnnie Walton

MEMBERS ABSENT: Councilwoman Katherine Felton

OTHERS PRESENT: Interim City Manager Montique McClary
Finance Director Alicia Steward
Assistant Finance Director Brian Lewis
City Clerk April Onley

The City Council recessed session was called back to order by Mayor Kirk Rivers at 5:00 p.m. Mayor Rivers announced this was a continuation of the meeting from Monday, August 8, 2022.

1. Presentation – Local Government Commission:

The purpose of this evening's meeting was to conduct financial training for board members. David Erwin, Natalie Roundtree, Susan McCullen were present. They explained that a governing body has a fiduciary responsibility to the municipality and the taxpayers.

Councilman Peel asked what's the accountability if the board does not do these things? Ms. McCullen advised that the accountability is at the ballot box. The funds of the unit should ultimately be put to the use that the government intends. All authority comes from the statutes. As North Carolina is a Dillon's Rule state, we have no authority except what's given by statute. Councilman Peel noted that only seven states are Dillon Rule – most are Home Rule.

The board sets the tone and expectations for employees to follow the requirements of GS-159. The tone starts at the top - if the employees are ethical, it comes from policies set by the board and manager.

159 article 3 sets forth budget, controls and rules for borrowing money. Not many states have organizations like the LGC that oversee the government. The LGC does approve debt when the organization goes to market for purchase of real property. The LGC was established in 1951 due to governments defaulting on their debt. It is staffed by Department of State Treasurer employees and composed of nine members who meet the first Tuesday of the month.

The LGC has the authority to have a finance officer to complete training, the authority to require contracting with an outside bookkeeper, the authority to impound the books and records of local government and assume full control of all financial affairs. Currently, they are managing seven units, which is the most they've ever managed. Taking over a unit is not something they want to do, but it is the main tool to use if necessary. There is no in between, as the law does not "plan" for in between measures.

David Erwin explained the purpose of a budget ordinance and the process for developing a budget. The operating budget must be balanced. Recurring revenues should equal recurring expenditures. No monies can be spent that are not budgeted. The budget ordinance should include instructions to staff for transferring money within a certain limit, and cover a period of July 1-July 30, annually. Budget prep should include an assessment of community needs, addressing stakeholder concerns, condition of physical assets, quality of government services to citizens.

Councilman Peel asked if there are things you cannot spend municipal money on. Mr. Erwin replied that money spent has to be for a public purpose. Ms. McCullen added that NCGS-160A gives a list that specifies what NC municipalities can spend money on / levy property taxes for, and all must serve a public purpose.

Mr. Erwin continued explaining that a municipality should not be in the business of charitable contributions without a purchase order or contract and that company should be reporting back how those funds are being used.

A unit should not transfer funds from or to an enterprise fund as a subsidy. Appropriation of fund balance should be a one-time revenue source for a special circumstance and not recurring expenditures. The LGC pays close attention to use of fund balance and measures use of fund balance as a percentage of overall budget. Mr. Erwin advised that Elizabeth City's is currently somewhat low compared to our peers, and we should probably create a policy on fund balance.

He explained that a budget officer, usually the city manager, must present a budget message by June 1st. The budget is filed with the clerk who makes copies available to the public and media. A public hearing is held, and 10 days must pass between presentation of the budget and adoption of the budget. The board may make changes to the budget at any time before or after the budget hearing, but those changes must be balanced. The budget must be adopted by a simple majority vote by July 1st. The budget can be amended at any time as long as it stays balanced. Budget amendments do not require public hearings.

Councilman Biggs asked if there's a difference between a budget officer and finance director. Mr. Erwin said most of the time, the budget officer is the city manager in a manager-council form of government.

Finance officers must be bound in amounts of not less than \$50,000 for the protection of the local government. Finance officers are responsible for accounting systems, managing receipts and deposits and money, managing debt and supervising debt.

Mayor Rivers asked what's referenced in supervising investments. Mr. Erwin replied that North Carolina local governments are very conservative on what they can invest in. Ms. McCullen said that it's usually also only things like what the federal government can invest in, such as treasury. The point is not to earn a lot of money, but to be safe with money. It's much different than private investments. While you can earn something, you are required to make sure it's in the right type of legal investments.

Councilman Biggs asked Director Steward where some of our investments as a City are. Director Steward replied NC Capital Management Trust and First Citizens were two of them. Ms. McCullen advised that NC Capital Management is like a money market but for local government and it's a fairly low yield, but when we need more money for debt service payments, they are liquid and we can get the money out that day.

Mr. Erwin stated that only approved banks in the state can be invested in.

Ms. Steward questioned if it's feasible to have so many capital project ordinances? Is there a way to consolidate them? Ms. McCullen noted that you can do it either way; you can have a separate fund for each project, but it gets messy. Mr. Erwin explained that you can have a fund for each one, like streets, electric, etc., and then each project would be a set of self-balancing accounts within that. Ms. McCullen pointed out that our financial system should be able to do that and we can talk to your software provider about how to set that up for us so they self-balancing within the bigger project fund and you want it to be multi-year.

Councilman Biggs asked what is the bond for our Finance Director. Ms. Steward replied that she was bonded at \$100,000.

Ms. McCullen advised that a law just passed a few weeks ago, and when insurance will be renewed next year, our Finance Director will have a change in the bonding program, but we have just started working on that.

Mr. Erwin continued that the governing board should insist on a monthly financial board to review with a budget to actual for each fund. Check registers and cash balances do not serve much in where you are in the budget year. He urged the Council to get perspective on "outlier" accounts that are expected to over-perform or be over-spent. Don't try to make decisions without financial reports. Third-party bookkeepers should turn in reports before being paid. He

explained that the 8% rule is a myth, as that usually calculates to a single month of expenses. Units may talk about 8%, but it will never be enough.

Councilwoman Whitehurst noted that in a personal budget, three or six months of cushion is recommended. Is there a certain percentage here where we hit a warning if we hit it? Like a "we're in trouble with the state" amount?" Mr. Erwin replied that if there's a downward trend over the years, that's what they really look at. If the balance is going down continuously, that's what they're really looking at. When it gets down below 20% for a unit our size, they'd start analyzing. Ms. McCullen said they have reports on their website that look at units that are in the same expenditure levels that Elizabeth City is and they would group us with that and that would be what we'd want to use as a target. For units over \$10 million, the median should be 46% and a minimum should be 25%, which would work out to about three months of expenses. You might not have 46%, but you don't want to go below 25%. You'd want to consider as you think about types of policies you want to set, what kind of fund balance policy do we want and what are the consequences if our audit comes in and we're below?

Councilman Walton asked if there were three cities they would you say would be model cities compared to Elizabeth City in general fund. Ms. McCullen said she was not sure which ones without looking at report on website. Councilman Walton asked if there was a document available for such a comparison. Ms. McCullen said they can get one for the Finance Director or Interim City Manager and send the emails and get you to it so you can see where your peers are and what their actual fund balance available is and where they were in that range. "You can use it to help you develop a fund balance policy to help you make sure you have money to meet your unit's needs."

Councilman Peel said we need it for emergencies and cash flow because that's cyclical. Ms. McCullen agreed that was correct, and you only know your fund balance when you get your audit.

Councilman Biggs asked if fund balance percentage needed to be increased if you operate a public utility or does that not just take into account general fund but all funds? Ms. McCullen said that percentage is just for general fund. Water and sewer should have its own set of reserves in there.

Councilman Peel noted that the electric fund is a critical one too. Ms. McCullen said electric funds are usually some of the healthier funds, but noted she had not looked at ours in some time. Water and sewer can be draining on a community.

Ms. McCullen explained the pre-audit process. Once you've adopted a budget and you're going to start spending from the budget, but you don't spend or incur expenses if there isn't money available in that budget to spend. You cannot spend against it if there's not enough money left in the budget to purchase. You have to consider the original amount, what's been spent to date and what remains. The monthly report helps keep an eye on this. Pre-audit language says there's money available in the budget to pay for things. A finance director cannot sign the pre-audit certificate without knowing that. If the bank statements are not reconciled, she can't really sign off because she doesn't have good numbers. Empower your finance directors to say no because they need to be able to tell department heads they can't buy things if there isn't available money and you need to back her up because the legal responsibility falls to her. If you don't back her up, the town will over-spend. Town can't disburse funds without signature of finance officer that says there's cash available to pay. Pre-audit language also goes on checks. The pre-audit process must take place before a contract or purchase order is signed. If you failed to pre-audit, the contract or purchase order is void.

Councilman Biggs said he didn't know if we have an internal policy or something set up where at a certain point in a year everything is cut off without manager or finance director's approval to cut back on budget amendments to stop frivolous spending. Is that a best practice? Ms. McCullen said lots of governments do that, depending on the year some of them stop for large ones between April 15 or May 1, which gives the finance department a month to figure out where they are with budgets so they'll know who needs what and where with their budget. If your budget dies on June 30th, you can't do any amendments. You need a "clean-up" ordinance before the end of the fiscal year where you can move things around if you need to in June.

Councilman Peel noted they'd done such a practice in school districts and it also helped people indiscriminately spending their fund balance. Ms. McCullen pointed out that some may also be lapsed salary and it doesn't mean you won't get it next year, but that's the mentality.

Councilman Biggs agreed and noted that it doesn't mean they wouldn't get it, it just might mean it has to have a higher level signature on it. He said he'd like to bring some of these items back for further discussion during the August 22, 2022 Work Session for Finance Committee.

Director Steward asked what's your opinion for handling emergency situations that the finance officer may not be aware of? Ms. McCullen said there are very few emergencies – most of the time it's people not planning well. Mr. Erwin said you should create an emergency PO policy. If you have to purchase something at midnight, come in at 8 am the next morning to discuss it. Ms. McCullen agreed that there are ways to deal with it and policy is a good idea.

Ms. McCullen continued that local governments must have an annual audit by an independent certified public accountant. Audit is an examination of accounting records. Get an opinion of whether the financial reports follow GAAP. An unmodified opinion is a clean audit. There are no local governments in NC now that are not receiving unmodified opinions. Modified opinions are audits with issues. Unmodified opinions do not mean that everything is 100% correct, but they are materially correct. It is not a guarantee that there has not been fraud, but auditors usually do not find fraud. It's usually found by a tip or a whistleblower.

Councilwoman Whitehurst asked if there is a hotline number for reporting fraud. Ms. McCullen said the state auditor has a hotline that anyone in the state could use, but lots of employee tips might come from someone telling the manager something or the finance director something.

Ms. McCullen continued that an unmodified opinion is also not a statement that you did a good job. If you have a single audit, which kicks in at \$750,000 in grant money, in addition to your financial audit, usually in the same report but includes additional work looking into the internal controls of how you dealt with the grant. With ARPA money, you will have single audits in your future, but you probably have them now with the size of your budget. If you have statutory violations such as overspending your budget at the department level. Responsibility of the board to make sure audit is on time, which could mean hiring a third-party bookkeeper. Audit is due to LGC by Oct 31st.

Mayor Rivers asked what happens if we miss that date?

Ms. McCullen explained that we have a grace period between Nov 1st and Dec 1st because we get so many in on Oct 31st that we won't know if yours isn't in on that date anyway. Ones after that will have to amend your contract and ask for more time. The LGC will have a corrective action plan that we'll ask the finance director and the auditor to develop and the Council to weigh in on and send a response letter about what you'll do to correct it. After Oct 31st, if your audit is late, we will not take your debt. So, Elizabeth City with where you are with the audit now, we could not take any debt to the LGC for you.

Councilman Whitehurst noted, so 2021 is already late, but are you still expecting 2022 by Oct 31st? Ms. McCullen replied that they were.

Director Steward advised that she had spoken with the auditors and asked where we are and Greg Isley firm may be able to help us a little. The contract ends August 31st and they have been making progress. The list is very short now. The audit was delayed several weeks because fixed assets were out about \$4 million, but they should get it done this week. The list is must shorter now. The statements have not been written yet because they don't have a good trial balance yet. They've done most of their testing. It's the just the fixed assets.

Ms. McCullen said it didn't sound like we'll make August 31st, but we might make September. Then our auditor will turn right around and start the 2022 work. Director Steward advised that she'd been meeting with the assistant finance director and restricting some things. They've created notes of what the auditors are asking for to be ready for 2022. Ms. McCullen pointed out that we won't be able to execute the next contract until this one is finished. So, when your auditor presents the 2021 numbers to you, and they are required by law to do that, then shortly after you should see the 2022 contract so you can move. It's going to be tight, but remember how late 2021 is. You may be late in 2022 because they don't turn around over night, but once you catch up, then in 2023, you should be in better shape. We know it takes a while and we do look at improvement dates. We are delighted when units shave months off so that the 2022 audit is not almost a year late, it's just two or three months. That's a win.

Councilman Walton asked if we meet those time frames, what's the best time for our status to change? Ms. McCullen said they update the UAL every March or April. They have to analyze a lot to know what the unit's percentages are and look at about as many of the 500

municipalities to update the UAL. The UAL for June 30, 2022 will be updated next March or April. If we catch up and there are no other issues, we could go off then in 2023. If we make the progress they hope to see us make, we may be looking at one more year and coming off at 2024.

Mayor Rivers asked what can the board do now that we're a year late? Just get more resources? Ms. McCullen said exactly, support the finance officer. Make sure that finance has the resources that they need. Make sure they know how important it is. Have the finance committee be interested in the progress of the audit and whether or not it's progressing like it needs to. Are there other third-party resources that should be put to it? Is the auditor not doing what they need to? Monitoring and keeping it so that the community, your auditor, your finance department knows you value it.

Councilman Biggs added the reason we're still waiting on the 2021 audit is a director correlation to the previous auditor, is that a fair assessment? Director Steward replied that it was. Also, the previous finance director and city manager turnover.

Councilman Biggs stated that the \$4 million in the fixed assets, that was a discrepancy brought to the Council very late in the game. He said he considered it a perfect storm. Ms. McCullen said she definitely believed it was an auditor issue but we have a good firm now and are in better hands. When they see units start getting late and it steamrolls on them, they plan when the auditor is going to come in and because of lots of other things, the unit is not ready. The auditor already has their whole audit season planned out and they have other commitments, so then you go to the end of the line, that's just how it works. Everything you can do to be ready when the auditors are, just try to do that.

Councilman Biggs said it was the intention of the Council have someone from Greg Isley's firm or the auditor give us a report at least once a month so we'll have some direct access.

Councilman Walton said he didn't see us catching up if we haven't caught up yet. If we know where the mix up was, we should be able to put the pieces there. Ms. McCullen said she thinks the new firm, the new auditors will be able to help us with that. Councilman Walton asked how long does the process take? Ms. McCullen said it takes a while, that's why she said she thinks we'll be looking at at least one more year on the UAL. A government audit is a big lift.

Councilman Biggs pointed out that if our 2021 audit gets completed by October and they start immediately on the next year's audit, a lot of what delayed them and the groundwork is done. Up until this point, they've been cleaning up a mess this whole time. Once they get the process in place, they can start moving better.

Councilman Walton said if they knew where the flaw began, they should be able to fix it. Ms. McCullen said \$4 million in fixed assets is huge. Councilwoman Whitehurst agreed and said the Council wanted an answer on where that went.

Councilman Biggs opined that's the difference between a \$13,000 and a \$50,000 audit, and the state auditor is starting to crack down on these things.

Ms. McCullen urged the Council to ask the auditor questions. They are your provider and should answer your questions. If you don't understand, ask again. You can also ask the LGC. She noted that they can't answer about their professional judgements or decisions, but they can understand financial statements.

Councilman Walton asked if she would send over some questions that we could possibly ask to help us clarify some things when the auditor comes; and Ms. McCullen agreed that she would.

Ms. McCullen said she'd like to touch on a few indicators of concern. If there are metrics that are outside of the thresholds, the auditors will know it when they present the statements to the board. The indicators are based on data that will allow the auditors to tell the board about area of concern for the LGC. The auditors will help develop a response letter that tells the LGC what the board intends to do to correct these areas on concern. They are able to tell you what your trends are doing when the statements are presented, and this is brand new this year and statewide.

Ms. Roundtree briefed the Council on debt policy. How much debt, when will it be paid off and how, what does the LGC require?

Councilman Gibbs related that his campaign manager told him not to do a gas giveaway while campaigning, but said he could do it after he won. He added that his aunt told him not to do it as elected official at all. Ms. Roundtree said she would agree that you should not do that. Councilman Gibbs asked if Council should not do things such as those to give back? Ms. Roundtree said that to her, that would go back to the code of ethics. "Does it smell funny? Look funny? What's the public perception? Sometimes it's not the truth, but how it looks can be hard." She urged the Council to always err on the side of caution.

Ms. McCullen said that it does feel counterintuitive at times, but it really is all about appearances being reality. Even though as a public official you mean no harm, you have to think about how things will play out in public. There may be some ways you can do what you want to do, and she urged the council to talk to the town's attorney and the League who will be teaching an ethics class the council will be attending at some point. She pointed out that under the ethics they signed as section manager at the state, they can't even accept pizza.

Mr. Erwin explained internal controls consist of policies and procedures. Signs of problems are records that are not ready to be audited in a timely manner, bank reconciliations not done in a timely manner, the board is not receiving accurate monthly financial statements, expenditures exceed authorized budget on a regular basis, sensitive documents are easily accessible. Boards should implement written policies for procurement cards and credit cards, petty cash and reconciliations, cash receipts and deposits, unit-owned assets, ethics and conflicts of interest.

Mr. Erwin noted that it's not a good idea for Council to have credit cards. Mayor Rivers concurred and said that our Council does not – they pay for it upfront and settle up afterwards.

Mayor Rivers thanked everyone for attending the training seminar and providing such valuable information.

7. Adjournment:

Having no other business to discuss, Mayor Rivers declared the meeting adjourned at 8:12 p.m.

E. Kirk Rivers
Mayor

April Onley, NCCMC
City Clerk

