



To the Members of the City Council
City of Brea, 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 the City of Brea, California, (City) for the year ended June 30, 2017. Professional standards require that we provide you with information about our responsibilities under generally accepted auditing standards, *Government Auditing Standards*, and the Uniform Guidance, as well as certain information related to the planned scope and timing of our audit. We have communicated such information in our letter to you dated August 15, 2017. We also met with the City’s Finance Committee on August 29, 2017 and March 8, 2018. Professional standards also require that we communicate to you the following information related to our audit.

Significant Audit Findings

Qualitative Aspects of Accounting Practices

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by the City are described in Note 1 to the financial statements. As described in Note 1 to the financial statements, the City adopted Governmental Accounting Standards Board (GASB) Statement No. 82, *Pension Issues – An Amendment of GASB Statements No. 67, No. 68, and No. 73*, as of July 1, 2016.

As described in Note 4 to the financial statements, management has reported prior period adjustments for the equity investment in California Domestic Water Company (CDWC) to reflect the consolidated entity, including Cadway, Inc., a wholly-owned subsidiary of CDWC. Further, preferred stock of CDWC held by the City has been reclassified as “water rights” within capital assets.

All significant transactions have been recognized in the financial statements in the proper period.

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 estimates affecting the City’s financial statements were:

Management’s estimate of the:

- The measurement of fair value of investments is based on observable market inputs and information from the City’s safekeeping custodian banks,
- Amounts related to the City’s other postemployment benefit (OPEB) asset are based on actuarial valuations,
- Amounts related to the net pension liability, deferred outflows of resources and deferred inflows of resources, pension expense, and the related disclosures, are based on actuarial valuations.

We evaluated the key factors and assumptions used to develop these estimates in determining that they appeared reasonable in relation to the financial statements taken as a whole.

Certain financial statement disclosures are particularly sensitive because of their significance to financial statement users. The most sensitive disclosures affecting the financial statements were:

Note 3 to the financial statements discloses authorized investments, interest rate and credit risks, and fair value measurements.

Note 4 to the financial statements discloses the City's activities with CDWC including water rights and equity in CDWC.

Note 9 to the financial statements discloses the City's agent-multiple employer pension plan's net pension liability, and related deferred inflows and outflows of resources, and pension expense. The valuation of the net pension liability and related deferred inflows and outflows are sensitive to the underlying actuarial assumptions used, including but not limited to, the investment rate of return and discount rates. As disclosed in Note 9, a 1% increase or decrease in the discount rate has a significant effect on the City's net pension liability.

Note 13 to the financial statement discloses the City's restatements of the prior year financial statements.

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

Difficulties Encountered in Performing the Audit

Certain matters arose during the audit regarding the accounting treatment and disclosures of transactions with CDWC, including the equity method reporting of common stock and the treatment of the City's preferred stock with CDWC. The completion of our audit was delayed to allow for management to provide additional information to address the accounting treatment and disclosures described in Notes 4, 13, and 15 to the financial statements, and the time for us to review and conclude on such information.

Corrected Misstatements

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are clearly trivial, and communicate them to the appropriate level of management. Management has corrected all such misstatements. The following material misstatements detected as a result of audit procedures were corrected by management:

- Transactions between the City and California Domestic Water Company (CDWC) were adjusted to reflect the equity investment of the consolidated entity (which included Cadway). The adjustments posted were \$4.2 million to beginning net position.
- Capital assets of \$2.8 million were restated from Construction-in-progress to Infrastructure.
- Opening net position/fund balance for the prior year audited financial statements totaling \$163 thousand related to a prior year proposed audit adjustment
- Net Pension Liability and related Deferred Outflows of Resources, Deferred Inflows of Resources, and Pension Expense in the amounts of \$6.2 million, \$338 thousand, \$938 thousand and \$7.5 million, respectively.
- The market value adjustment on the PARS investment account in the amount of \$373 thousand.

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 auditor's report. We report that there were no such disagreements.

Management Representations

We have requested certain representations from management that are included in the management representation letter dated May 31, 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 City's financial statements or a determination of the type of auditor's 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.

Other Audit Findings or Issues

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

Other Matters

We applied certain limited procedures to management's discussion and analysis, schedule of changes in the net pension liability and related ratios for the Miscellaneous and Safety Plans, schedule of plan contributions for the Miscellaneous and Safety Plans, schedule of funding progress, and schedules of revenues, expenditures and changes in fund balance – budget and actual for the General fund and each major special revenue fund and related note, which are required supplementary information (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.

We were engaged to report on the combining and individual nonmajor fund financial statements, budgetary comparison schedules, and the schedule of expenditures of federal awards, which accompany the financial statements but are not RSI. With respect to this supplementary information, 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 financial statements or to the financial statements themselves.

We were not engaged to report on the introductory and statistical sections, which accompany the financial statements but are not RSI. Such information has not been subjected to the auditing procedures applied in the audit of the basic financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

Restriction on Use

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

Yaurinek, Trine, Day & Co., LLP

Laguna Hills, California

May 31, 2018