MULTNOMAH COUNTY, OREGON

Management Letter

June 30, 2012

MOSS ADAMS LLP
Certified Public Accountants | Business Consultants

To Mark Campbell, Chief Financial Officer
Multnomah County
Portland, Oregon

Dear Mr. Campbell:

In planning and performing our audit of the financial statements of Multnomah County, Oregon ("the County") as of and for the year ended June 30, 2012, 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 of America, we considered the County's internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the County's internal control. Accordingly, we do not express an opinion on the effectiveness of the County's internal control.

However, during our audit we became aware of several matters that are opportunities for strengthening internal controls and operating efficiency. The memorandum that accompanies this letter summarizes our observations, comments and suggestions regarding those matters.

We will review the status of these comments during our next audit engagement. We have already discussed these comments and suggestions with various County personnel, and we will be pleased to discuss them in further detail at your convenience, to perform any additional study of these matters, or to assist you in implementing the recommendations.

This report is intended solely for the information and use of the management of Multnomah County, the Audit Committee and the Auditor's Office of Multnomah County, and is not intended to be and should not be used by anyone other than these specified parties. We would be happy to further discuss any of the items in this letter with you at your convenience.

Moss Adams, LLP

Eugene, Oregon
December 13, 2012

MOSS ADAMS LLP

Multnomah County
Portland, Oregon
December 13, 2012

FINDINGS FROM LAST YEAR - MANAGEMENT ADVISORY COMMENTS

Time and Effort Reporting Requirements

Finding: During audit procedures for allowable costs of the JAG Cluster (CFDA 16.738, 16.803, 16.804) it was noted that one employee's time in the Department of Community Justice (DCJ) was charged to the award based upon budgeted amounts. This major program was selected for testing in July 2011, prior to closing of the County's accounting records. It is uncertain whether the annual true-up would have occurred based on department internal controls over compliance had this program not been selected for testing so early during the audit process.

Update: A similar finding was noted within a different department during the current year audit. See current year management advisory findings for explanation.

Disbursement Support Documentation

Finding: During audit procedures for the allowable costs of the Distribution of Receipts to State and Local Governments program (CFDA 15.227), a sample of search and rescue meal expenditures were selected for testing. The support documentation provided for these expenditures was inconsistent, ranging from a packet that included detailed receipts and volunteer logs to just a single credit card swipe receipt.

Update: We did not find this issue again in the current audit, and this issue is deemed to have been resolved.

Timely / Appropriate Accounting Entries

Finding: It was noted that several non-routine accounting entries were not made into SAP on a timely basis, or were not made appropriately at the initial time of entry. These non-routine entries included:

- Accounting for the fair value of investments. Treasury did not perform the mark to market analysis in a timely manner, which required adjusting journal entries to be made after the year end close to report certain investments at fair value. This also resulted in the original journal entry to roll forward beginning working capital (BWC) for fiscal year 2012 to be incorrect and to also require an adjustment.

- Accounting for debt proceeds. Debt proceeds in the amount of $500,000 were issued to the County in advance of a total debt issue of $15 million as a good faith deposit. The good faith deposit was received by the County on November 30, 2010, and the entry to record the deposit in SAP was made on January 6th, 2011 with a posting date of December 1, 2010. The balance of the debt issue of $14,500,000 was received by the County on December 14, 2010, and then entered into SAP on January 6, 2011.

- Accounting for 'incurred but not reported (IBNR) liability'. The County records a liability for 'incurred but not reported' claims in the Behavioral Health Care fund and the Federal/State Program fund for claims incurred but not yet paid. In our review of the IBNR liability, we noted the account was not reviewed or adjusted throughout fiscal year 2011 as payments were made and new claims were reported. Because the liability account was not reviewed or adjusted throughout the year, significant year-end adjustments and entries are required, and the County could be reporting an inaccurate cost and liability balances throughout the year.

Update: We did not find these specific issues again in the current audit, however, there were other issues noted during the performance of audit procedures. See current year management advisory findings for explanation.

Restricted Resources

Finding: When management implemented GASB 54, the County's Finance and Budget Policies were revised to include the order of spending of resources with restricted resources spent first, followed by committed, then assigned, and with unassigned resources spent last. The County's policies also state that only the Board of County Commissioners, within the County, can place constraints on resources outside of a restriction placed by an external party. A department had designated a particular resource stream as restricted and did not get a resolution from the Board placing any type of constraint on this resource stream that would meet the County's Finance and Budget Policies. The County had incurred significant expenditures that met the department's restrictions, but the department chose not to use the restricted resources. Restricted funds should have been spent prior to spending unrestricted General fund dollars in order to comply with the provisions of GASB 54 and with County policies.

Update: We did not find this issue again in the current audit, and this issue is deemed to have been resolved.

Issuance and Related Spending of Debt

Finding: During the audit of the County's long-term debt, it was noted the County had a significant balance of unspent debt proceeds related to a debt issuance from March of 2010. The County issued $9.8 million in Full Faith and Credit Obligations on March 31, 2010. As of June 30, 2011, there was approximately $7 million in unspent debt proceeds. In fiscal year 2011, the County paid interest expense of $328,497 on the outstanding debt at a rate of approximately 3.5%. The longer unspent bond proceeds exist, the more interest costs are incurred that could have been avoided, and the risk of incurring arbitrage liabilities and compliance issues increases.

Update: We did not find this issue again in the current audit, and this issue is deemed to have been resolved.

CURRENT YEAR - MANAGEMENT ADVISORY COMMENTS

Time and Effort Reporting Requirements

Finding: Over the past few years the County has experienced repeat findings in the Single Audit with respect to time and effort reporting where grants have been charged for County personnel costs based on budgets or preliminary estimates. If personnel costs are charged to grants based upon budgetary amounts, there is a requirement for quarterly historical assessments and then comparison with an annual reconciliation between the historical assessments and budgetary charges. Since fiscal year 2007, the County has worked very hard to review and revise payroll tracking and reporting processes in order to be in compliance with Federal requirements. This is an on-going effort as smaller divisions and offices in the County receive Federal awards that may not be fully aware of specific time and effort reporting requirements. During audit procedures for allowable costs of the Weatherization Assistance Program (CFDA 81.042) it was noted that of the twenty payroll samples selected from the Department of County Human Services (DCHS) for testing, the quarterly assessment had not been performed for one employee.

Recommendation: We commend the County for its efforts to address this issue over the past several years, and recommend continued diligence especially for smaller departments that may not be fully knowledgeable regarding the compliance requirements.

Management's Response: The County has made significant improvement in time and effort reporting, but management recognizes that we still have work to do in this area to be fully compliant with our Federal grants. Due to the size of our organization and the number of Federal grants we receive, it is a continuous challenge to ensure complete compliance with time and effort reporting across the County.

DCHS management is currently reviewing the existing time and effort reporting process for the Weatherization Assistance Program to identify and correct the breakdown in the process. DCHS management will evaluate the current process for time and effort reporting for the Weatherization Assistance Program to ensure we are meeting the requirements of OMB A-87 as well as our business needs. In addition, DCHS management will work to provide additional time and effort training to the Weatherization Assistance Program and other smaller program areas.

Accounting Period Cutoff for Grants

Finding: During audit procedures for the Grants to States Program (CFDA 45.310) received by the Library and the State Energy Program (CFDA 81.041) received by the Department of County Assets, it was noted that the population of expenditures provided did not agree to the expenditures reported on the schedule of expenditures of federal awards (SEFA). The differences were immaterial to both programs: approximately $33,160 for the Grants to States Program and $17,450 for the State Energy Program. Per inquiry of Department grant personnel and central finance, these differences were due to the inclusion of expenditures from prior accounting periods that should have been reported in prior years.

Recommendation: It is recommended that grant personnel record grant related transactions timely, especially at the end of the fiscal year. Grant personnel should anticipate potential grant related expenditures at the end of the fiscal year and ensure these expenditures are recorded in the proper accounting period.

Management's Response: Annual year-end trainings help Department finance staff be mindful of year-end cutoff considerations and the importance of recording revenues and expenditures to the proper period. For the fiscal year 2013 close, we will be sure to emphasize the importance of cutoff and especially with respect to our Federal awards. Further discussion with those Departments involved in the Single Audit will also occur prior to year-end close as a reminder.

Use of Negative Confirmation as a Compliance Control

Finding: During audit procedures for the Grants to States Program (CFDA 45.310) received by the Library, it was noted that within the sample of three cash draws selected for testing, in one case grant personnel relied upon negative confirmation for management approval of the cash drawdown request. An email was sent by the Library finance supervisor to the manager for approval, requesting a response if the manager did not approve of the cash drawdown request.

Recommendation: It is recommended that grant personnel use a process that provides a distinct record of approval for the cash drawdown requests. This should include evidence from the manager that the cash drawdown request has been reviewed and approved for processing.

Management's Response: Since this was brought to our attention, the Library has improved this process: the finance supervisor emails the manager requesting his/her review and approval for the cash draw request, the manager will evidence his/her approval by emailing it back to the finance supervisor and noting the approval in the email. This will provide for an audit trail on the approval process and we will also print the email exchange for our grant files.

Timely / Appropriate Accounting Entries

Finding: It was noted that several non-routine accounting entries were not made into SAP on a timely basis, or were not made appropriately at the initial time of entry. These non-routine entries included:

- Sellwood Bridge Construction Project: The Sellwood Bridge construction project is a significant and material project in the financial statements. In fiscal year 2012, the County setup a separate special revenue fund (2511) to track and account for all Sellwood Bridge transactions. During the performance of audit procedures, several aberrations were observed and noted below:
    - June 2012 ODOT Revenues (SAP Document #1813002208) indicates this transaction was reversed from fiscal year 2013 and re-entered into fiscal year 2012. Department of Community Services (DCS) did not properly record fiscal year 2012 revenues to the general ledger timely.
    - There was a $1 million write-off of the June 2011 ODOT receivable which affects federal grant revenues, essentially overstating the County's SEFA for fiscal year 2011. We have discussed this particular error with management, and DCS has since implemented additional controls over receivables and has

taken steps to improve communication with ODOT (grantor agency) to ensure revenues are properly recorded.
  - Subsequent to year end, review of the available cash balance in the Sellwood Bridge fund noted the fund was operating with a cash deficit of approximately $784,000 in September 2012. On September 28, 2012, the County drew an additional $25 million on the non-revolving line of credit for the Sellwood Bridge to meet cash needs. However, prior to that point, the Sellwood Bridge fund did not have the necessary resources to pay current liabilities. The County has a process in place to review cash balances by fund after the month-end closing process, however there does not appear to be a process in place to detect when funds may report negative cash balances.

  As this will be a continuing project for the next several years, and the County intends to issue long term debt to finance the project, we are obliged to stress to management the importance of properly recording and accounting for this project.

- Use of the Federal / State Program Special Revenue Fund: The County utilizes the Federal / State Program Special Revenue Fund (Fund 1505) to properly account for revenue sources that are subject to external restrictions and the associated expenditures that meet those external restrictions. Use of this special revenue fund is also critical for accurate and timely preparation of the SEFA. During the performance of audit procedures, it was noted that:
  - A State Justice Institute Grant award received by the Department of County Assets for $40,500 was budgeted within the Federal / State Program Special Revenue Fund (1505), but the expenditures against this award (SAP Document #1012109549 and #1812033750) recorded in the Facilities Management Fund (Fund 3505).
  - A State Homeland Security Program grant in the Sheriff's Office was miscoded to the Direct State general ledger accounts instead of the Federal through State general ledger account by the Sheriff's Office.

- Capital Asset Disposition: during performance of audit procedures over current year capital asset dispositions, it was noted there was a building disposition (Kelly Building) that was not recorded timely by the Department of County Assets, and the initial transaction was not posted correctly. The transaction was originally recorded "net" instead of being correctly posted "gross". Central Finance detected and corrected this error as part of the financial close and reporting process.

Recommendation: We recommend the County implement procedures to support timely and appropriate accounting entries for non-routine transactions.

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Multnomah County
Portland, Oregon
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Management's Response:
Sellwood Bridge Construction Project: Since activity on the Sellwood Bridge project has increased significantly over the past year, the Department of Community Services (DCS) continues to implement additional controls over project invoicing and billing. Some of these controls include an additional review over all grant related invoices for the Sellwood Bridge Fund. In addition, DCS management has been working on improving our communications with our primary grant funder, ODOT, to ensure ODOT's costs agree with the County's spreadsheets and accounts. Internal communications have also been strengthened with regular check-in meeting between the DCS Sellwood Project Managers and the Finance staff. The Sellwood Bridge project also uses an Owner's Representative firm that has helped with reviewing project invoices and ensuring the costs meet Federal Highway Administration funding eligibility.

In December 2012 the County issued $128 million in Full Faith & Credit Obligations for the Sellwood Bridge project. Additionally, in December the County completed negotiations for the maximum price (MP) from the contractor for the bridge main span and interchange construction. The MP will produce a contractor schedule which will be used to update the County's cash flow model. As we track our spending for the Sellwood project, we will also monitor our cash balances in the Sellwood Bridge fund. Any anticipated cash deficits will be communicated early with the CFO to determine if additional resources are needed to assist with the Sellwood Bridge fund's operations.

Use of the Federal / State Program Special Revenue Fund: To ensure that Federal funds are recorded to the proper general ledger account and captured in the County's Schedule of Expenditures of Federal Awards and Single Audit, a mid-year review of general ledger revenue accounts by Fiscal Compliance will help identify if any Federal funds have been miscoded to the wrong account. We will also emphasize the importance of recording Federal awards to the correct account and fund during our year-end communications.

Capital Asset Disposition: The Department of County Assets (DCA) was formed on July 1, 2011 and as this Department continues to take shape, opportunities for strengthening processes and procedures as well as improving our internal controls arise. DCA Management is currently in the process of streamlining the finance staff's operations, and will continue to work with finance staff who oversee grant accounting, reporting and assisting with budgeting for grants. DCM and DCA management are working closely together to help develop the support functions in DCA, including Finance and Budget administration. Over the next year we will continue to refine our support processes and procedures and work to identify where efficiencies can be gained and where controls can be strengthened.

Assumptions within Actuarial Valuation Reports

Finding: The County relies upon an actuarial valuation report for determining and reporting its other post employment benefit obligation. This actuarial report is based upon several key assumptions, including the discount rate used to determine the present value of the County's liability for these obligations. The most recent report issued on October 10, 2011 utilizes a discount rate of 4.0%. The applicable accounting standards require that the discount rate to be used should match the expected rate of return realized on the resources used to fund benefit payments. The County is paying benefits from cash and investments held internally in its treasury. Current practice by similar entities that pay benefits out of their internal cash and investment pool is to use a discount rate of between 3.0% to 3.5%. It is noted that a minor change in the discount rate can have a significant impact on the current year expense calculation, and to the overall liability; and the difference could be material to the financial statements.

Recommendation: The County will be acquiring a new actuarial report within the next fiscal year. It is recommended that the discount rate used within the new report be adjusted downward to more accurately reflect current economic conditions and the long-term expected rate of return on cash and investments held in the County's internal investment pool.

Management's Response: The County is in the process of developing a contract for OPEB actuarial services. As we move further in this process and begin working on the 1/1/2013 actuarial valuation we will take a closer look at the assumptions used in the past to calculate our OPEB liability. These discussions between management and our actuaries will also include an evaluation of what is an appropriate discount factor to consider and use in our valuation. In addition, the County will be looking at options to establish a separate trust fund in connection with the requirements of GASB #45 to help prefund OPEB obligations which will in turn impact the discount rate.

Individual Entering and Approving Their Own Time in Payroll System

Finding: During audit procedures of internal control over the payroll cycle, analysis techniques were performed over the payroll module population data. From the population of approximately 1.5 million entries, it was discovered that 282 of those entries consisted of an individual entering their own time into the payroll system and approving that same time for processing. This is noted as a segregation of duties issue in that the roles of entering payroll and reviewing and approving the payroll should be separated. Additional analysis was performed over these records, and the total time entered for each day was consistently 8 hours, there was no overtime noted for this employee within the records examined. We did not compare the employee's timecards to the payroll entries as this was beyond the scope of the audit.

Recommendation: In most cases, the ability to enter payroll and then perform review and approval of the payroll entries is separated by roles created within SAP. In those rare instances in which an employee has been granted the authority to perform both functions, policy and standard practice should be voluntary separation of these roles within the department processing payroll.

Management's Response: Since this exception was brought to our attention during the external audit, Central Payroll met with the District Attorney Department and helped implement additional manual controls to ensure segregation of duties is achieved and prevent an employee from entering and approving her/his own time. In addition, the payroll manager will review time entry and SAP approval roles on a semi-annual basis to ensure segregation of duties are achieved and manual controls are followed for those offices that have been granted an exception.