

Secretary of State

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# SECRETARY OF STATE

## AUDITS DIVISION

### Municipal Newsletter

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The Division administers Municipal Audit Law, *Oregon Revised Statutes* 297.405 to 297.740 and 297.990, which requires Oregon's local governments, consisting of approximately 1,800 cities, counties, school districts, and special districts, to comply with statutory annual financial reporting. The purpose of this newsletter is to update licensed municipal auditors on some of our recent efforts in administering Municipal Audit Law and address other issues of interest to them and their clients.

#### **Desk Reviews**

This year we reviewed 124 fiscal year 2014 audit reports documenting 792 findings. However, many of the findings were simply the result of not updating reports for new reporting standards, most notably GASBS No. 63 and No. 65. Sometimes, basic financial statements were updated but overlooked were the MD&A, notes, and supplementary information sections to the report. Missing were newer terms like *net position*, *net investment in capital assets*, and *deferred inflows & outflows of resources*. This may be the result of a weakness in the final report review process.

#### **Independent Auditor's Report**

Our desk reviews disclosed only minor issues with the terminology and format required by the clarity standards. Most findings occurred in the introductory and opinion paragraphs describing information not presented in the report. The most frequent error was reporting *aggregate remaining fund information* when none was presented. Another common error was narrating

budgetary schedules as RSI in a cash basis OCBOA presentation.

#### **Report Signatures**

Municipal Audit Law (ORS 297.465) requires the independent auditor sign his or her report. This is a statutory requirement that exceeds professional standards and is a consequence of Oregon's additional licensing requirement for municipal auditors. However, Board of Accountancy (BOA) rule OAR 801-020-0620(4) contains a provision that allows the Independent Auditor's Report to be signed in the firm name if all owners of the firm are on the municipal roster.

There was a time when our office knew all the owners of firms performing municipal audits. Over the years the landscape has changed dramatically. There are several new firms, including some from out-of-state, changes in legal formations, and most notably several retirements. We no longer know who the owners are so we continue to request signed reports.

This summer I attended a BOA meeting to discuss this matter. We concluded that if a firm wishes to use this provision in administrative rules it is the responsibility of the independent auditor to communicate in writing to the Audits Division that all owners of the firm are on the municipal roster and they wish to sign the report in the name of the firm.

#### **Management Discussion and Analysis**

The majority of findings resulted from (1) narratives and condensed financial information not updated for new pronouncements; (2) narratives not updated for current year events and activities; and



(3) spreadsheet errors including hidden rows and columns. This is a reminder that the independent auditor has a responsibility to review the information for completeness and whether the information is presented in accordance with [GASB] established guidelines (SAS AU-C §730).

### **Fund Statements**

Many school districts mistakenly report sources of revenue at the summary level of *local, intermediate, state, and federal*. This is what the Department of Education requires for internal reporting purposes and is appropriate if presented as supplementary information. However, this does not meet GASB standards. Those classifications identify *who* instead of *what* are the sources of revenue. For example, *local* might include property taxes, interest income, tuition, fees, rental income, school activities, etc. *State* would include the state school fund, state grants, etc.

One firm told us their CAFR to the GFOA never received a comment like ours. So we contacted GASB for clarification. They confirmed our understanding. They also suggested that a school could continue to use its current classifications if immediately indented below they also named the each source.

### **Notes to Financial Statements**

The majority of desk review findings are contained in the notes. In general, they fall into four categories including some that are repeated every year.

The first and most frequent type occurs from not updating narratives with new standards.

The second type occurs from not adequately describing what is minimally required. A good example is the retirement note. Each year it has more errors in the narrative than any other disclosure.

Pension accounting has terms and concepts unfamiliar to many. To adequately describe Oregon's PERS it is helpful to understand the differences between a cost-sharing multiple-employer plan and an agent multiple-employer plan; the difference between a defined benefit and a defined contribution pension; and knowledge of the changes in retirement benefits between Tier 1, Tier 2, and OPSRP. Several disclosures miss that OPSRP (ORS Chapter 238A) is one pension plan with two programs; the definite benefit program and the Individual Account Program (IAP), the latter being the defined contribution individual account program.

The third type of error occurs when a finding is only addressed by the municipality reviewed and is not considered for its application to other firm clients. One example is an entity with proprietary funds disclosing pronouncements issued by FASB on or before November 30, 1989. This outdated disclosure was superseded when GASBS No. 62 codified FASB pronouncements into governmental accounting standards. Another example is the policy to capitalize assets with estimated useful lives of three, five, or more years. GASB defines capital assets as those with initial useful lives extending beyond a single reporting period.

The fourth type occurs if a boiler-plate SSAP is not tailored to the individual government. Sometimes overlooked policies are (a) revenue recognition availability periods; (b) types of transactions included in program revenues; (c) defining operating and nonoperating revenues for proprietary funds; and (d) whether to first apply restricted or unrestricted resources to expenses for which both are available.

### **Capital Assets**

We documented 24 capital asset note disclosure findings. Most of the errors are in the presentation of the schedule. GASB requires the schedule be presented using three criteria in descending order: (1) the



schedule should first group assets associated with governmental activities from business-type activities; (2) then separate assets being depreciated from those that are not [our most frequent finding]; and (3) next classify assets by major categories such as land, buildings, vehicles, machinery, equipment, as applicable (GASB Cod. § 2300.117-118 and §1400).

### **Interfund Balances and Transfers**

This disclosure results in a finding when the reasons for the activities are not adequately explained. The purposes for interfund transfers and loans should be stated. Further, interfund loans not expected to be repaid within one year should be explained; the reason being that the loan(s) may in substance be a transfer (GASB Cod. §2300.126-127).

### **Budgetary Comparison Schedules**

This is a reminder that financial statements prepared on the cash or modified cash basis of accounting should not present budgetary comparisons for the general fund and each major special revenue fund as RSI that is required in a GAAP presentation. The schedules should be presented following the notes as *supplementary information* (AICPA State and Local Governments Audit Guide, Chapter 15.06 and SAS AU-C Section 725).

### **Electronic Extension of Time to File**

In an effort to streamline and ease requests for additional time to file reports, we've created a fillable form parties can submit electronically. You may still file hardcopy but electronic filings take less effort and have a quicker response time. Electronic requests will receive responses via email. One big change to the form itself is the names of the requesting government official and independent auditor can be typed instead of personally signed. We encourage you to try it. Check out the **new form** on our website at <http://sos.oregon.gov/audits/Pages/muniaudits.aspx>

### **Property Tax Schedule**

The property tax schedule is no longer required information. It involved the preparation of a time-consuming schedule of estimated amounts for an immaterial year-end receivable. It is no longer considered essential information to meet the needs of the reader. We've updated the Minimum Standards for audits and reviews to delete the requirement.

### **2015 Legislative House Bill 2174**

What follows is the substance of a letter to the municipal audit community dated May 29, 2015. It is repeated here for the benefit of those that may be unaware of the amendments to municipal audit law enacted this year by the legislative assembly.

The 2015 legislature enacted House Bill 2174 in April. The Bill amends Municipal Audit Law ORS Chapter 297.425; 297.465; and 297.466. SECTION 7 to the Bill contains an emergency clause making the amendments effective upon passage. The amendments were signed into law by Governor Brown on April 16, 2015.

The changes are significant. Some amendments are specific to cities and counties; other amendments apply to all municipal corporations. What follows are some of its highlights. The final "Enrolled" version to the Bill can be viewed on the Oregon State website

<https://olis.leg.state.or.us/liz/2015R1/Downloads/MeasureDocument/HB2175/Enrolled>

SECTIONS 2(3)(a) and 3(6): If a city or county does not file its audit report with the Secretary of State (Secretary) within one year of its fiscal year-end, except for *extraordinary circumstances*, the Secretary may take action to withhold 10% of state revenue distributions to the city or county until the report is filed.



SECTION 3(3)(a): Within 30 days of filing its audit report, a municipal corporation is required to file with the Secretary a *plan of action* to address the deficiencies noted in the report. This amendment applies to modified opinions, management letters communicating significant deficiencies, and violations of laws, rules, and regulations including those identified in the report required by the Minimum Standards for Audits of Oregon Municipal Corporations.

To help clarify what does not constitute reportable deficiencies to the Secretary, there are oftentimes verbal or written communications of a less serious nature commonly known as “other matters”. These do not require the municipality to follow-up or respond to in writing, do not generally rise to the level of a required *Plan of Action*, and therefore, need not be reported to the Secretary.

SECTION 5: The Secretary is required to summarize the reporting activities of all municipal corporations required to have an audit. The results will be presented in a report to the legislative assembly each biennial session.

SECTION 2(2): The law was amended to make it the responsibility of the municipal corporation to request an extension of time to file its report. This was previously the responsibility of the independent accountant.

SECTION 1(2): Contracts between the municipal corporation and its independent accountant are no longer prescribed or subject to the approval of the Secretary. That provision in law was enacted by the legislature decades ago to provide written guidance to municipal corporations at a time when contracts for personal services were oftentimes only verbal. Today municipal corporations follow Public Contracting Code ORS Chapters 279A, 279B, and 279C.

Moving forward, the amendments in law will first be applied to municipalities with a fiscal year ending June 30, 2015. Our desire is to communicate these changes in law to all municipal corporations as quickly as possible. The law is currently in effect and does not require new rules to be in force.

#### **GASBS No. 68 Note Disclosure**

We’ve received several calls from firms looking for examples of a GASBS No. 68 note disclosure. The OSCPA Governmental Accounting and Auditing Strategic Committee devoted considerable time to develop some examples on its website. Take a look at [https://www.orcpa.org/professional\\_development/resources](https://www.orcpa.org/professional_development/resources)