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SECRETARY OF STATE
AUDITS DIVISION

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Municipal Newsletter

September 1, 2017

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The Audits Division administers Municipal Audit Law, Oregon Revised Statutes 297.405 to 297.740 and 297.990, which requires Oregon's local governments to comply with statutory annual financial reporting. The purpose of this newsletter is to update the audit community on the Audits Division's efforts in administering Municipal Audit Law and address other issues of interest.

FILING REQUIREMENTS

The 2015 Legislature approved revisions to Municipal Audit Law, which (1) clarified the responsibilities of municipal corporations in addressing deficiencies; (2) enhanced the enforcement authority of the Secretary of State (Secretary); and (3) required the Secretary to annually prepare a summary report providing information about municipal corporations' compliance with Municipal Audit Law.

In conjunction with these revisions, the division will enforce the requirement for auditors to provide the division a copy of audit letters sent to municipal corporations when those letters communicate deficiencies. Below is a summary of the filing requirements.

Division Filing Requirements – Auditors and Municipalities

- Audit and Review reports are due 180 days from fiscal year end.
- Summary of Revenues and Expenditures should be filed by the auditor within 30 days of submitting an audit or review report.
- GAS report or separate letter to management communicating deficiencies must be filed by the auditor within 30 days of delivering the report to the municipal corporation.
- A Plan of Action must be adopted by the governing body when the auditor reports deficiencies. The plan must include a timeline for corrective action and be filed within 30 days of submitting the audit report. Management's response in an auditor letter is not sufficient. Sample letters/resolutions are posted on our website under Municipal Forms and Templates.

The most convenient way to submit reports, letters, and summaries is to email them to municipalfilings.sos@oregon.gov. If email is not an option, you may send a hard copy to us at 255 Capitol St NE, Ste 500, Salem OR 97310.

Enhanced Enforcement Authority

This year was the first year we enforced the 2015 legislation to withhold 10% of state distributions from cities or counties delinquent in filing their annual audit. After several notifications, we initiated the withholding process for cities who had not filed their 2015 or 2016 audit reports. Please continue to educate your clients on the importance of timely filing.

Annual Summary Report

Due to 2015 legislation, Oregon Revised Statute 297.471 now requires the Secretary to present a summary report to the legislative assembly March 1 of every odd year on the reporting activities of all municipal corporations required to have an audit. The Audits Division issued the first summary report on March 1, 2017. Report No. 2017-01 can be found on our website at sos.oregon.gov/audits.

Per statute, the report includes a listing of municipal corporations required to file an audit and indicates whether they filed on time or late, whether they had an approved extension of time to file, the number and type of deficiencies reported, and whether they filed a Plan of Action.

Summary Report Results

More awareness is needed. The Audits Division did not receive all auditor letters communicating deficiencies to their clients, nor did we receive all required Plans of Action from municipalities.

- 800 municipal corporations (70%) filed audits on time or within their approved extension deadline. 320 municipal corporations (28%) filed late. 24 municipal corporations (2%) had not filed their required 2015 audit within 18 months after their fiscal year end.
- 351 audited municipal corporations (30%) reported at least one significant deficiency or material weakness.
- 79% of the deficiencies reported were for internal control weaknesses, 13% were for non-compliance, and 8% were for accounting errors and misstatements.
- Of the 351 municipal corporations with one or more reportable findings, only 106 (30%) filed a Plan of Action with the Secretary as required.

These percentages should improve as understanding and awareness of the new requirements grow.

REVISED SUMMARY FORM

To facilitate the required summary reporting to the legislature, we revised the Summary of Revenues and Expenditures (SRE) form. You will now provide information on the number and type of deficiencies and how you communicated those deficiencies to your client. This will also serve as a reminder to provide to the Audits Division a copy of letters to clients communicating deficiencies.

The revised SRE form is located on the Audits Division website. Please use the new form as the old form will no longer be accepted. If you have questions about disclosing the number and type of deficiencies or other questions about the form, please contact Amy Dale and she'll be happy to help you. We welcome feedback and questions about the form!

DESK REVIEWS – FY2016 AUDIT REPORTS

Every year we review a sample of financial reports from the nearly 1,800 cities, counties, school districts, fire districts, and other special districts in the state of Oregon. Our goal is to provide timely feedback to the audit community for consideration in planning upcoming engagements. This year we reviewed approximately 70 fiscal year 2016 audit reports, focusing on some of the smaller districts, such as irrigation, water, fire, and urban renewal agencies.

Although we have a few new items to point out this year, many findings repeat what we've seen and reported in prior years. We encourage auditors to consider our findings and the matters included in this newsletter as they plan and perform future engagements. The results of some of these reviews are included in this newsletter starting on page 5.

WHAT'S NEW?

New Look – Website Resources

The Municipal Audit and Local Government Resource section of the Secretary's website has been updated! Included in this update are some additional resources including a revised Summary of Revenues and Expenditures form, Plan of Action templates, updated filing instructions, and a new feature allowing anyone involved or interested in municipal audits to sign up to receive news and information relevant to the program.

New E-mail List – Municipal Audit Program Communication

This annual newsletter is primarily intended for the audit community. It is mailed to all licensed municipal auditors and also posted to our website to make it available to the public and municipalities. However, we receive many requests for information and improved communication targeted to municipal officers and staff. In response, we've created an email listing through GovDelivery that we will use to periodically circulate information to subscribers. The target audience is local government officials and staff, but the information will also be useful to municipal auditors and citizens. We suggest that all municipal auditors subscribe to this list and encourage your clients to subscribe as well.

Sign up for "Municipal Audit Program" emails at <http://sos.oregon.gov/audits>.

You can manage your subscription to include any other list offered through GovDelivery. Please know that you must self-subscribe to each listing for participation. Subscribing to the Municipal Audit Program listing will *not* automatically enroll you on any other list.

Comments from the New Municipal Audit Manager

I assumed the role of Municipal Audit Manager in January 2017, just a few weeks before Phil Hopkins retired. I have been with the Audits Division for over 15 years and worked in the municipal audit program with Phil for several years. I am thrilled to step into this position and continue his good work.

When Phil retired he took a lot of institutional knowledge and technical expertise with him. But he also left us with a program that is operating well with good relationships amongst practitioners, municipalities, the OSCPA, and Board of Accountancy. I want to build on that good foundation and be alert to ways we can improve the usefulness, communication, and quality of the municipal audit program. If you have suggestions or comments to improving the program, please contact me at (503) 986-5160 or amy.dale@oregon.gov.

I look forward to our continuing partnership,

A handwritten signature in blue ink that reads "Amy Dale". The signature is written in a cursive style with a long horizontal flourish extending to the right.

DESK REVIEWS – FY 2016 AUDIT REPORTS

REPEAT FINDINGS:

Management's Discussion and Analysis (MD&A)

The presentation of MD&A continues to improve. However, we still find outdated terminology and condensed financial information that does not agree to the financial statements presented.

MD&A should provide a fact-based analysis of the current year financial results in comparison with the prior year. GASB §2200.106 specifically requires the analysis to address reasons for significant changes or budget variations. It is not enough to simply state the percentage or amount of change. The analysis should provide the reader some insight into the reasons for the variance or why amounts that normally vary remain unchanged.

Further, when MD&A is presented with cash basis or modified cash basis statements it should not be referred to as *required* supplementary information (RSI). MD&A can only be referred to as *required* when presented in financial statements presented in accordance with GAAP.

Aggregate Remaining Funds

The last three newsletters reported errors in how the independent auditor's report addressed aggregate remaining funds in the introductory and opinion paragraphs of the independent auditor's report. Specifically, aggregate remaining fund information was referred to and opined on when none was presented. Or, reference to it was left out when the report presented such information. What constitutes aggregate remaining funds can be complicated; such as when a government chooses to report a non-major fund on the face of the basic financial statements because there is only one non-major fund and combining statements would be impractical. In this case, the non-major fund should be clearly marked as non-major, and the auditor's opinion should reference the aggregate remaining fund opinion unit (the single non-major fund).

The independent auditor's report is a critical piece of work and the auditor should take care to review each one they sign, ensuring it is accurate and appropriate in the specific circumstances.

Summary of Significant Accounting Policies

Nearly half of the reports we reviewed had errors in the Summary of Significant Accounting Policies (SSAP) including an insufficient description of the cash or modified-cash basis of accounting being applied, references to basis of accounting or fund descriptions not applicable to the statements being presented, not defining operating and non-operating revenues of proprietary funds, not disclosing the dollar threshold for capitalizing assets, outdated terminology, and not disclosing the entity's policy regarding whether to first apply

restricted or unrestricted resources when an expense is incurred for purposes for which both restricted and unrestricted net position are available.

NEW MATTERS:

How Many General Funds?

We noticed something unusual that we haven't seen before. A few reports included more than one general fund in their governmental fund statements. And there were instances where no general fund was reported, not even under a different title (a general fund can be called something else but must be treated as a general fund in presentation and disclosure).

GASB 54 ¶ 29 states that "the general fund should be used to account for and report all financial resources not accounted for and reported in another fund." The definition of the general fund precludes multiple general funds (GASB Cod. §1300.116). The general fund of a blended component unit should be reported as a special revenue fund (GASB 14 ¶ 54).

Deferred Inflows/Outflows -

Property Taxes

Occasionally, we see deferred inflows for *property taxes* reported in the same amount on both the government-wide statement of net position (full accrual) and the governmental funds balance sheet (modified accrual). As an imposed non-exchange revenue, a government would recognize a receivable when the property taxes are levied. This is true under both full-accrual and modified accrual. Under the modified accrual basis of accounting, the government recognizes revenue when the property taxes are deemed available, or collectible within 60-90 days of year end. Under the full accrual basis of accounting, the availability criteria does not apply and all property taxes are reported as revenue when levied. As a result, deferred inflows for *unavailable property taxes* should only appear on the governmental funds balance sheet. (GASB Cod. §P70, §N50)

Pensions

Over 25% of the reports reviewed received a comment related to pension disclosures and reporting, and specifically related to the requirements of GASB 68 (GASB §P20).

PERS provides each participating employer with a detailed breakdown of the various inflows and outflows to use when preparing their financial statements and notes. GASB allows deferred inflows related to pensions to be aggregated. Deferred outflows related to pensions may also be aggregated. However, deferred inflows and outflows may not be netted against each other; they should retain their character as deferred inflows or outflows.

The amount of contributions made subsequent to the measurement date during an employer's fiscal year are recognized as deferred outflows of resources during the *current* year, but should reduce the net pension liability in the *next* measurement period. Many

statements incorrectly reported the reduction of liability in the current period. The GASB 68 Implementation Guide (Q&A, question 147 and 195) clarifies this and is a good resource for many disclosure and reporting questions.

Cash or Modified Cash Basis of Accounting

Modified cash-basis financial statements are becoming more common. The report must still comply in substance with the basic GAAP financial statement presentation and disclosure requirements as applicable. Cash and modified cash basis statements are not considered appropriate in form unless the financial statements include informative disclosures similar to those required by GAAP when the financial statements contain items that are the same as, or similar to, those in financial statements prepared in accordance with GAAP. Though the financial statement presentation and disclosure requirements of GAAP still apply in context, it's important to make sure statements and schedules are appropriately titled to clarify the basis of accounting being used.

Modified cash or cash basis statements should only involve financial statement elements resulting from cash related events. They should *not* involve financial statement elements resulting from accruals and noncash transactions or events. When preparing or auditing financial statements where noncash related transactions are wanting to be included, consider whether it's more appropriate to consider presenting a GAAP framework with departures.

Investments – LGIP

We noted many reports that disclosed the fair value hierarchy of investments in the LGIP, and external investment pool. GASB's 2017 Implementation Guide, question 4.36, states that positions in these pools are not required to be categorized within the fair value hierarchy for purposes of Statement 72. Further, GASB staff clarified that not only is the disclosure not required, it would be incorrect to do so.

Also, several entities incorrectly disclosed the LGIP is a 2A7-like pool.