

# City of Fort Worth, Texas

Report to Management  
Year Ended September 30, 2010

March 22, 2011

The Honorable Mayor and City Council Members  
City of Fort Worth  
Fort Worth, Texas

Dear Mayor and City Council Members:

In planning and performing our audit of the financial statements of the City of Fort Worth (the "City") as of and for the year ended September 30, 2010 (on which we have issued our report dated March 22, 2011, which included a reference to other auditors), in accordance with auditing standards generally accepted in the United States of America, we considered the City's internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the City's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, in connection with our audit, we have identified, and included in the attached Appendix, certain matters involving the City's internal control over financial reporting that we consider to be material weaknesses or significant deficiencies under standards established by the American Institute of Certified Public Accountants.

We have previously communicated certain matters noted during our audit of the financial statements of the City for the year ended September 30, 2009, which we considered to be material weaknesses or significant deficiencies, in our report to management and those charged with governance dated March 23, 2010. As of the date of this report, we believe the City has not remediated certain of these material weaknesses or significant deficiencies. We have outlined in the attached Appendix those previously reported matters which we believe have not yet been remediated.

We have also identified, and included in the attached Appendix, other deficiencies involving the City's internal control over financial reporting and other matters as of September 30, 2010 that we wish to bring to your attention.

This report does not include the communications of the other auditors on internal control over financial reporting and other matters that are reported on separately by those auditors.

The definitions of a deficiency, a material weakness, and a significant deficiency are also set forth in the attached Appendix.

A description of the responsibility of management for establishing and maintaining internal control over financial reporting and of the objectives of and inherent limitations of internal

control over financial reporting, is set forth in the attached Appendix and should be read in conjunction with this report.

Although we have included management's written response to our comments in the attached Appendix, such responses have not been subjected to the auditing procedures applied in our audit and, accordingly, we do not express an opinion or provide any form of assurance on the appropriateness of the responses or the effectiveness of any corrective actions described therein.

This report is intended solely for the information and use of management, the City Council, others within the organization, and federal and state awarding agencies and is not intended to be, and should not be, used by anyone other than these specified parties.

Yours truly,

*Deloitte & Touche LLP*

## APPENDIX

### SECTION I — SIGNIFICANT DEFICIENCIES IDENTIFIED IN CURRENT AUDIT

We consider the following deficiency in the City's internal control over financial reporting to be a significant deficiency as of September 30, 2010:

#### *Significant Deficiency: Grant Management*

Criteria – Each grant program should be reconciled at least annually to ensure that the activity is accurately recorded and that the ending payable to or receivable from the granting agency accurately reflects that City's position. Grant agreements should be reviewed to ensure proper accounting treatment for special items such as investment income earned on advances, receipts of program income and expenditures from the City's matching funds and program income. In addition, there are a number of revenue recognition matters that must be considered in preparation of the annual financial statements.

Condition – Numerous errors were noted in the City's accrual and deferral of grant revenues and the related receivables, which required adjustments in the accounting records and in the SEFA. Although not material to the City financial statements as a whole or to the SEFA, these errors required substantial effort to research and correct.

Context – For the year ended September 30, 2010, the City managed more than 335 different Federal, State and local grant projects. The funding methods and provisions for these grant awards vary, requiring the Financial Management Services Department to evaluate proper accounting and reporting for each grant award.

Cause – Large numbers of grants accounted for in multiple funds create a difficult process in preparation of the year-end closing entries and in the accumulation of the data for the SEFA. Nonstandard grants require research that was not properly or timely performed by grant accounting personnel.

Effect – Inaccurate accounting for both the receipts and expenditures of grant-related transactions can lead to an improperly prepared SEFA or errors in revenue recognition when related expenditures are not properly reported.

Recommendation – Develop standard policies and procedures for identifying and reporting grants in the general ledger. Continue to educate personnel in all departments on the requirements related to proper accounting and reporting for grants. This information should also include guidance on the nature of grants, both monetary and non-monetary. Use standard funds for accounting for such grants and perform periodic reviews of all departments to ensure that grant accounting standards and compliance requirements are met.

Views of Responsible Officials – Concur. The following steps are being implemented to improve and strengthen controls over grant management:

- Going forward, the City will record new grants in specific funds designated for grant funding.
- Financial Management Services Department ("FMS") will provide additional grant management training to both grant management personnel and grant accountants to

- improve their skills, understanding of grant requirements, and increase communication between grant management personnel and grant accounting.
- As grant awards vary and therefore, the accounting requirements vary, FMS will review and strengthen the current grant accounting procedures so that grants are accounted for based on the specific requirements of each grant award.

## **SECTION II — MATERIAL WEAKNESSES OR SIGNIFICANT DEFICIENCIES IDENTIFIED IN A PREVIOUS AUDIT THAT HAVE NOT YET BEEN REMEDIATED**

We identified and previously communicated the following deficiencies that were considered to be a material weakness or significant deficiency in the City's internal control over financial reporting during our audit of the financial statements of the City for the year ended September 30, 2009. As of the date of this report, we believe these deficiencies have not yet been remediated by the City:

### ***Material Weakness: Accounting for Capital Assets (updated from fiscal years 2004-2009)***

Criteria – Proper accounting for capital assets requires the maintenance of an accurate, detailed listing of all expenditures that meet the City's criteria for capitalization – those that are long-lived and meet the City's capitalization threshold.

Condition – A significant amount of effort has been made by the City over the past several years to improve the practices used to account for and report the City's investment in capital assets. For fiscal years 2008 through 2010, we did not note the level of errors that were noted in previous years related to capital assets. Audit adjustments for fiscal years 2008 through 2010 related to capital assets were not material and were generally isolated to specific areas of the accounting process. However, there are certain matters that remain unresolved; and when considered cumulatively, we believe these matters represent a potential risk of material error in future years and therefore warrant continued attention by City management. These matters include:

- The need for the City to upgrade its current Excel-based approach to accounting for capital assets to a more controlled database environment, such as a module to the planned ERP system
- A lack of consistent application of the City's now formalized written policies for capital assets by all departments of the City
- A lack of proper communication between the Financial Management Services Department and other City departments regarding Construction-in-Progress ("CIP"), resulting in improper classification of certain projects within CIP
- A lack of timely reporting of disposals of capital assets by City departments to the Financial Management Services Department
- An inappropriate capitalization process for the internally generated intangible assets related to the ERP system implementation costs.
- The need for reassessment of the continuing appropriateness of the practice of recording salvage value for Water System assets

Context – Capital assets represent the City's single largest asset. As of September 30, 2010, the City has approximately \$3.8 billion in net book value of capital assets and has over 1,500 projects set up to track and manage CIP costs.

Cause – The City has multiple departments and contractors managing construction projects and capital assets without consistent, complete application of the proper procedures to account for transactions or purchases. Formal procedures are not in place to establish timely communication regarding capital asset transactions between the various departments and the Financial Management Services Department.

Effect – Inconsistent practices have developed throughout the City for accounting for CIP. Errors in accounting for capital assets could have a material effect on the City’s financial statements. We believe that the City’s current system of accounting for capital assets (both electronic and manual) is not sufficiently designed or implemented to prevent or detect potential material errors in capital assets without a significant effort made at year-end to review transactions for the existence of such errors.

Recommendation – The following recommendations should be considered by City management.

- Implement a more sophisticated system of accounting for capital assets. Such a system should contain automated controls to ensure proper accounting and reconciliation of capital assets. However, consider the importance of fully integrating an electronic capital asset system with the City’s general ledger system and plan appropriate timing for the implementation of any new capital asset system relative to the City’s overall ERP implementation time-table.
- Implement and provide training on the newly designed City policy that defines when CIP projects are considered complete and should be transferred to completed assets. Communicate and implement the City policy that defines the date on which developer contributions should be added to capital assets. In addition, develop consistent application of city policies on accounting for capital assets in general and the related reconciliation processes. Ensure that such policies are implemented and enforced.
- On an overall basis, improve communication between the operating departments and the Financial Management Services Department related to capital assets.
- Implement a policy to count the assets of each department on a rotation basis. Ensure that each asset is counted at least biennially, in order to comply with the requirements established for Federally-funded assets. Require timely communication of all disposals or impairments of capital assets from the City departments to the Financial Management Services Department.
- Review the City’s policies and procedures related to capitalization of intangible assets, particularly those related to the capitalization of ERP system implementation costs.
- Reassess the City’s policy of recording salvage value on water system assets. Consider the use and history of such assets and realistically assess the likelihood and appropriateness of salvage value in those assets.

Views of Responsible Officials – Concur. During each fiscal year, City departments will receive all capital asset listings pertaining to their department regardless of type of capital asset (i.e. improvements, buildings, infrastructure, etc.) from the Financial Management Services Department (FMS) Accounting Division. This interim year verification will help ensure that each department’s capital assets are consistent with calculated depreciation, yearly additions and deletions as maintained by FMS.

FMS will require each department to compare its information – resolving any differences with Accounting’s records. This process will allow for a common information stream and consistent records for internal and external users.

Additionally, the FMS is continuing to work with both City departments and an outside consultant to identify and document processes and procedures related to construction-in-progress and capital asset tracking.. These efforts should result in improved identification, accounting, and reporting of the City's capital assets. This includes:

- 1) Properly classifying and accounting for costs related to capital assets;
- 2) Properly capturing and accounting for contributed assets;
- 3) Reconciling detailed capital asset records to the general ledger;
- 4) Assessing if all assets are accounted for (i.e. physically inventoring assets on a rotation basis);
- 5) Evaluating the useful life and salvage value for classes or types of capital assets;
- 6) Identifying potential impairments;
- 7) Complying with grant requirements for federally funded assets; and
- 8) Ensuring proper internal controls for City capital assets.

To better improve communications with departments, FMS is also using the Fiscal Accountability Committee to educate and coordinate capital asset matters. Future plans are to develop and administer training on accounting and fiscal topics, which includes providing guidance and instruction on proper capital asset management.

The abovementioned improvements will be facilitated with the selection and implementation of an Enterprise Resource Planning (ERP) financial system. This system will provide the means to better administer, monitor and enforce policies and procedures for overall accounting operations, inclusive of capital assets. Planning, requirements gathering, and system selection is in the initial stage, with system implementation scheduled for Fiscal Year 2013.

***Significant Deficiency: Computer System Access Controls (updated from fiscal years 2006-2009)***

Criteria – Access controls are key controls to the City's financial systems to protect financial data from improper accounting and reporting. The City is currently reestablishing and documenting policies and procedures related to controls.

Condition and Cause – Although improvements were made in this area during fiscal year 2010, the following deficiencies were still noted during the review of general computer controls over the City's financial system and the water billing system:

A shared administrator account (QSECOFR) exists on AS400 (SunGard) with privileged access through the ALLOBJ authority granted to this account. The password for this account is stored in a folder to which non-IT administrators (1 administrative assistant and 10 IT programmers in the water department) have access.

On the Mainframe, there are 21 accounts (including legacy accounts) that cannot be traced to individuals who have administrative access to the MARS application.

On the Mainframe hosting MARS and Genesys applications, a code compliance employee and a security group member formerly in the operations group have inappropriate access to production datasets.

On the Court View application 27 users have inappropriate administrative access through the roles granted to them. However we also noted that the roles were cleaned up after year end as part of the SQL upgrade and the users no longer have this access.

Context - Management is ultimately responsible for ensuring that all systems are secure and that unauthorized users do not have access to sensitive data. As such, access should be reviewed periodically and security strengthened to minimize such risks.

Effect- Unauthorized access to an entity's information systems can potentially allow damage to the data which can lead to the integrity of the system or information maintained in the system being compromised.

Recommendation - The following should be considered:

- Privileged access should be restricted to authorized administrators. Inappropriate users' access, including that for programmers, should be removed.
- User access privileges of all user accounts at the application, database, operating system, networks and key security configuration should be reviewed on a regular basis to ensure it is appropriate at all times.

Views of Responsible Officials – Concur. Per Administrative Regulation D-5, dated February 8, 2010, Information Technology Security requires both restricted access to privileged accounts and periodic reviews of user access privileges.

With regard to the specific observations:

- Water Department - Shared administrator account on AS400. Water IT is currently working to resolve this issue of appropriate staff access to the password folder with resolution date by September 30, 2011.
- Financial Management Services Department – Mainframe accounts not traceable within MARS. In FY 2010, FSA implemented a new automated security job which notifies administration of employee terminations. A similar automated job will be implemented by September 30, 2011 for MARS. The unknown logons on this list will be removed with the new job.
- IT Solutions Department – Mainframe inappropriate access. Mainframe security access will be reviewed to ensure privileged access is limited appropriately and that the proper procedures for access are being followed.
- Municipal Courts Department – Inappropriate administrative access. Those users are the upper management, supervisors, IT staff, CJS users. This issue has been addressed with the new profiles built in the Security project that NashWest is implementing. Estimated to be complete by September 30, 2011.



### **SECTION III — REMEDIATED MATERIAL WEAKNESSES OR SIGNIFICANT DEFICIENCIES**

In prior years, we identified the following deficiencies that were considered to be material weaknesses or significant deficiencies in the City’s internal control over financial reporting, and which were remediated by the City as of September 30, 2010:

***Significant Deficiency: Accounting for Contractual Arrangements in a Decentralized Environment (updated from two related Material Weakness in fiscal year 2008)***

Condition – During fiscal 2009 the Financial Management Services Department (“FMS”) was informed that in a previous year, the City had entered into a lease purchase obligation that placed approximately \$9 million into trust for the purchase of certain equipment. However, the transaction was not recorded in the City’s financial statements. Upon discovery of the account, FMS personnel researched the issue and recorded an adjustment to the City’s accounting records.

***Significant Deficiency: Documentation of Policies and Procedures Related to Accounting and Financial Reporting (updated from fiscal years 2006-2008)***

Condition – There is currently a general lack of documented policies and procedures related to accounting and reporting. As a result, there are instances of improper accounting entries recorded that require subsequent correcting journal entries. The City is currently using a combination of intensive internal supervisory reviews as well as additional reviews by an outside consultant to analyze year-end trial balances and make corrections before performing final closes and preparing financial statements. This process appears to be identifying most errors; however, a better process would be the correct recording of entries initially and prior to review by supervisors or consultants. Heavy reliance on this review process could result in some errors not being detected and corrected on a timely basis.

***Significant Deficiency: Change Management of Computer Controls (updated from fiscal years 2006-2008)***

Condition – The City has designed and implemented a Change Management Policy, but the current processes do not require that all changes are processed through the change management policy.

### **SECTION IV — OTHER MATTERS**

Our observations concerning other matters related to operations, compliance with laws and regulations, and best practices involving internal control over financial reporting that we wish to bring to your attention are as follows:

***Financial Management Services Department Staffing***

Criteria – The current complexity of governmental accounting and reporting, combined with the size and activity of the City of Fort Worth, require a Financial Management Services Department that is staffed and trained to a high level of expertise and competency.

Condition and Context – Because of certain material errors and issues in the City’s financial records, the City’s annual financial reporting was delayed for the 2004 through 2008 fiscal years. Beginning with the 2007 fiscal year, the City contracted an outside firm to augment the City accounting staff to enable the City to address the accounting and reporting issues and to put the City’s annual reporting back onto a normal timetable. The restoration of a timely reporting process was accomplished in fiscal 2009. However, this outsourcing of the annual closing and reporting process has resulted in a lack of development of City staff in the skills necessary to perform these functions without outside assistance. City staff should have strong analytical skills to appropriately record and review financial activity throughout the year and not only at year-end in preparation for the annual audit.

Cause – City personnel in the Financial Management Services Department have suffered a certain amount of turnover and change to their department such that the current staff have not been responsible for the closing and reporting process for several years.

Effect – Although the accounting and reporting function can certainly be outsourced on a permanent basis, we understand that it is the City’s desire to bring this function back into the Financial Management Services Department. However, the skills necessary to do so have not been developed among the current City staff. Therefore we do not believe the current Financial Management Services Department personnel have the background, training, experience and analytical skills necessary to accomplish the financial reporting responsibilities without assistance from an outside consultant.

Recommendation – We commend the City for the significant improvements that have been made in recent years in financial accounting and reporting, and we further commend the City for its efforts to upgrade and modernize the City’s IT systems through the ERP system implementation under way. We recommend the City now focus on completing the ERP implementation and training. Additional support should be provided to the Financial Management Services Department personnel to ensure that, as the outside contractor begins withdrawing from full responsibility for the closing and reporting process, the City staff will be capable and prepared to take on the role. This is critically important to ensure a smooth transition back to full Financial Management Services Department responsibility for these processes, without reverting back to prior practices that at one time caused financial reporting errors and delays for the City.

### ***Recently Issued Governmental Accounting Standards Board (“GASB”) Statements***

#### *GASB 54: Fund Balance Reporting and Governmental Fund Type Definitions*

Observation — GASB Statement No. 54, Fund Balance Reporting and Governmental Fund Type Definitions, addresses the usefulness of fund balance information by providing clearer fund balance classifications that can be more consistently applied and by clarifying the existing governmental fund type definitions. This Statement establishes fund balance classifications that comprise a hierarchy based primarily on the extent to which a government is bound to observe constraints imposed upon the use of the resources reported in governmental funds. This Statement is effective for the City in fiscal year 2011.

#### *GASB 57: OPEB Measurements by Agent Employers and Agent Multiple Employer Plans*

Observation – GASB Statement No. 57, OPEB Measurements by Agent Employers and Agent Multiple Employer Plans, clarifies that when actuarially determined OPEB measures are reported by an agent multiple-employer OPEB plan and its participating employers, those measures should

be determined as of a common date and at a minimum frequency to satisfy the agent multiple-employer OPEB plan's financial reporting requirements. This Statement is effective for the City in fiscal year 2012.

*GASB 59: Financial Instruments Omnibus*

Observation — GASB Statement No. 59, Financial Instruments Omnibus, was issued in June 2010 to update and improve existing standards regarding financial reporting and disclosure requirements of certain financial instruments and external investment pools for which significant issues have been identified in practice. The standard is intended to improve financial reporting by providing more complete information, by improving consistency of measurements, and by providing clarifications of existing standards. Applying the reporting provisions of Statement 31 for interest-earning investment contracts to unallocated insurance contracts improves consistency of investment measurements that are reported by pension and other postemployment benefit plans. Emphasizing the applicability of SEC requirements to 2a7-like external investment pools provides practitioners with improved guidance. Limiting interest rate risk disclosures for investments in mutual funds, external investment pools, and other pooled investments to debt investment pools provides better guidance regarding the applicability of interest rate risk disclosures. Finally, addressing the applicability of Statement 53 to certain financial instruments refines which financial instruments are within the scope of that Statement. This statement is effective for the City in fiscal year 2011.

*GASB 60: Accounting and Financial Reporting for Service Concession Arrangements*

Observation — GASB Statement No. 60, Accounting and Financial Reporting for Service Concession Arrangements, was issued in December 2010 to improve financial reporting by addressing issues related to service concession arrangements (SCAs), which are a type of public-private or public-public partnership. The standard addresses SCAs in which there is an arrangement between a transferor (a government) and an operator (governmental or nongovernmental entity) in which (1) the transferor conveys to an operator the right and related obligation to provide services through the use of infrastructure or another public asset (a “facility”) in exchange for significant consideration and (2) the operator collects and is compensated by fees from third parties. The statement also includes required disclosures about the SCAs. This standard becomes effective for the City in fiscal year 2013.

*GASB 61: The Financial Reporting Entity: Omnibus—an amendment of GASB Statements No. 14 and No. 34*

Observation — GASB Statement No. 61, The Financial Reporting Entity: Omnibus—an amendment of GASB Statements No. 14 and No. 34, was issued in November 2010 to improve financial reporting for a governmental reporting entity. The standard modifies certain requirements for inclusion of component units, amends criteria for blending, and clarifies the reporting of equity interests in legally separate entities. This standard becomes effective for the City in fiscal year 2013.

*GASB 62: Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*

Observation – GASB 62, Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements, was issued in December 2010 to incorporate into the GASB's authoritative literature certain accounting and

financial reporting guidance that is included in the following pronouncements issued on or before November 30, 1989, which does not conflict with or contradict GASB pronouncements:

1. Financial Accounting Standards Board (FASB) Statements and Interpretations
2. Accounting Principles Board Opinions
3. Accounting Research Bulletins of the American Institute of Certified Public Accountants' (AICPA) Committee on Accounting Procedure.

This standard becomes effective for the City beginning in fiscal year 2013.

Recommendation – Review the recently issued standards to determine the approach the City will take to implement them as they become effective.

## **SECTION V — DEFINITIONS**

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

The definitions of a deficiency, a material weakness, and a significant deficiency that are established in AU 325, *Communicating Internal Control Related Matters Identified in an Audit*, are as follows:

A *deficiency* in internal control over financial reporting exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when (a) a properly designed control does not operate as designed, or (b) the person performing the control does not possess the necessary authority or competence to perform the control effectively.

A *significant deficiency* is a deficiency, or combination of deficiencies, in internal control over financial reporting that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

A *material weakness* is a deficiency, or combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

## **SECTION VI — MANAGEMENT'S RESPONSIBILITY FOR AND THE OBJECTIVES AND LIMITATIONS OF INTERNAL CONTROL**

The following comments concerning management's responsibility for internal control over financial reporting and the objectives and inherent limitations of internal control over financial reporting are adapted from auditing standards generally accepted in the United States of America.

## **Management's Responsibility**

The City's management is responsible for the overall accuracy of the financial statements and their conformity with generally accepted accounting principles. In this regard, management is also responsible for establishing and maintaining effective internal control over financial reporting.

## **Objectives of Internal Control over Financial Reporting**

Internal control over financial reporting is a process affected by those charged with governance, management, and other personnel and designed to provide reasonable assurance about the achievement of the entity's objectives with regard to reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations. Internal control over the safeguarding of assets against unauthorized acquisition, use, or disposition may include controls related to financial reporting and operations objectives. Generally, controls that are relevant to an audit of financial statements are those that pertain to the entity's objective of reliable financial reporting (i.e., the preparation of reliable financial statements that are fairly presented in conformity with generally accepted accounting principles).

## **Inherent Limitations of Internal Control over Financial Reporting**

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

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