City of Fort Worth, Texas

Report to Management
Year Ended September 30, 2012

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March 19, 2013

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, 2012 (on which we have issued our report dated March 19, 2013, 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 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, 2011, which we considered to be material weaknesses or significant deficiencies, in our report to management and those charged with governance dated March 20, 2012. 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, 2012 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

SECTION I — 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, 2011. As of the date of this report, we believe these deficiencies have not yet been remediated by the City:

Significant Deficiency: Accounting for Capital Assets (updated from fiscal years 2004-2011)

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 2012, 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 2012 related to capital assets were generally isolated to specific areas of the accounting process. However, there are certain matters that remain unresolved. 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 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 completed projects within CIP and improper timing of reclassification of CIP to capital assets in use, specifically in smaller enterprise funds for fiscal 2012

Context – Capital assets represent the City's single largest asset. As of September 30, 2012, the City has over $4 billion in net book value of capital assets and has over 2,000 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 significant 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 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. 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 City's policy that defines when CIP projects are considered complete and should be transferred to completed assets.
- On an overall basis, improve communication between the operating departments and the Financial Management Services Department related to capital assets.

SECTION II —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, 2012:

Significant Deficiency: Grant Management (updated from fiscal year 2010)

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 Schedule of Expenditures of Federal and State Awards ("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.

Significant Deficiency: Computer System Access Controls (updated from fiscal years 2006-2010)

Condition and Cause – Although improvements continue to be made in this area during fiscal year 2011, the following deficiencies were still noted during the performance of our procedures over general computer controls related to the City's financial system and the water billing system:

- On the Mainframe: 6 users (4 Police Department personnel, 1 former Help Desk person, and 1 Finance IT person) have inappropriate access to the Mainframe RACF toolkit, which allows these users access to create shell Mainframe accounts and perform password resets.
- On the Mainframe: 1 Help Desk Supervisor has access to migrate changes to production for the Mainframe environment.
- On the SQL database supporting CourtView: the Builtin Administrator group is assigned SYSADMIN access, which inappropriately grants privileged database access to members of the Platform Technology group.

SECTION III — 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 preparation of the financial statements and 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. 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 in financial reporting.

Recently Issued Statements Of The Governmental Accounting Standards Board ("GASB")

GASB 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* 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* 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.

GASB 63: *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position* was issued in June 2011 to improve financial reporting for a governmental reporting entity. The standard provides financial reporting guidance for deferred outflows of resources and deferred inflows of resources. Concepts Statement No. 4, *Elements of Financial Statements*, introduced and defined those elements as a consumption of net assets by the government that is applicable to a future reporting period, and an acquisition of net assets by the government that is applicable to a future reporting period, respectively. This standard becomes effective for the City in fiscal year 2013.

GASB Statement No. 65: *Items Previously Reported as Assets and Liabilities* was issued in March 2012 and establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources of inflows of resources, certain items that were previously reported as assets and liabilities. This standard becomes effective for the City in fiscal year 2014.

GASB Statement No. 66: *Technical Corrections - 2012 - an Amendment of GASB Statements No. 10 and No. 62* was issued in March 2012 and amends Statement No. 10, Accounting and Financial Report for Risk Financing and Related Insurance Issues, by removing the provision that limits fund-based reporting of a state and local government's risk financing activities to the general fund and the internal service fund type. GASB 66 also modifies the specific guidance on accounting for (1) operating lease payments that vary from a straight-line basis, (2) the difference between the initial investment (purchase price) and the principal amount of a purchased loan or group of loans, and (3) servicing fees related to mortgage loans that are sold when the stated service fee rate differs significantly from a current (normal) servicing fee rate. This standard becomes effective for the City in fiscal year 2014.

GASB Statement 67: *Financial Reporting for Pension Plans* was issued in June 2012. This Statement replaces the requirements of Statements No. 25, Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans, and No. 50, Pension Disclosures, as they relate to pension plans that are administered through trusts or equivalent arrangements that meet certain criteria. Most significantly, this statement requires the net pension liability to be measured as the total pension liability, less the amount of the pension plan's fiduciary net position. Actuarial valuations of the total pension liability are required to be performed at least every two years, with more frequent valuations encouraged. This standard becomes effective for the City in fiscal year 2014.

GASB Statement No. 68: *Accounting and Financial Reporting for Pensions* was also issued in June 2012 and establishes accounting and financial reporting requirements related to pensions for governments whose employees are provided with pensions through pension plans, as well as for nonemployer governments that have a legal obligation to contribute to those plans. This statement requires the recognition of the entire net pension liability and a more comprehensive measure of pension expense, along with additional required footnote disclosures. This standard becomes effective for the City in fiscal year 2015.

GASB Statement No. 69: *Government Combinations and Disposals of Government Operations* was issued in January 2013 and establishes accounting and financial reporting standards related to government combinations and disposals of government operations. As used in this Statement, the term *government combinations* includes a variety of transactions referred to as mergers, acquisitions, and transfers of operations. This standard becomes effective for the City in fiscal 2015.

Recommendation – Review all GASB Statements listed above and their implications to determine the potential impact on the District's financial statements.

SECTION IV — DEFINITIONS

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 V — 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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