

CITY OF SHERWOOD
Sherwood, Oregon

Schedule of Expenditures of
Federal Awards and Related Reports

Year Ended June 30, 2011

CITY OF SHERWOOD
Sherwood, Oregon

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**INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER
FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS
BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN
ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

March 31, 2012

City Council
City of Sherwood, Oregon
Sherwood, Oregon

We have audited the financial statements of the governmental activities, the business-type activities, each major fund and the aggregate remaining fund information of the City of Sherwood, Oregon, (the City) as of and for the year ended June 30, 2011, which collectively comprise the City's basic financial statements and have issued our report thereon dated March 31, 2012. We conducted our audit 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.

INTERNAL CONTROL OVER FINANCIAL REPORTING

Management of the City is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the City's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, 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 and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying Schedule of Findings and Questioned Costs, we identified certain deficiencies in internal control over financial reporting that we consider to be material weaknesses, and other deficiencies that we consider to be significant deficiencies.

A deficiency in internal control 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

INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS (Continued)

INTERNAL CONTROL OVER FINANCIAL REPORTING (Continued)

A *material weakness* is a deficiency, or combination of deficiencies, in internal control, 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. We consider the deficiencies described in the accompanying Schedule of Findings and Questioned Costs as items 2011-01 and 2011-02 to be material weaknesses.

A significant deficiency is a deficiency or combination of deficiencies in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiency described in the accompanying Schedule of Findings and Questioned Costs as item 2011-03, to be a significant deficiency.

COMPLIANCE AND OTHER MATTERS

As part of obtaining reasonable assurance about whether the City's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

* * * * *

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



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**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH
REQUIREMENTS THAT COULD HAVE A DIRECT AND MATERIAL EFFECT
ON EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER
COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133**



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March 31, 2012

City Council
City of Sherwood, Oregon
Sherwood, Oregon

COMPLIANCE

We have audited the compliance of the City of Sherwood, Oregon, (the City) with the types of compliance requirements described in the U. S. Office of Management and Budget (OMB) Circular A-133, *Compliance Supplement* that could have a direct and material effect on its major federal program for the year ended June 30, 2011. The City's major federal program is identified in the summary of auditor's results section of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to its major federal program is the responsibility of City management. Our responsibility is to express an opinion on the City's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the City's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the City's compliance with those requirements.

In our opinion, the City complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on its major federal program for the year ended June 30, 2011.

INTERNAL CONTROL OVER COMPLIANCE

Management of the City is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the City's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine

INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH REQUIREMENTS THAT COULD HAVE A DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133 (Continued)

INTERNAL CONTROL OVER COMPLIANCE (Continued)

our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the City's internal control over compliance.

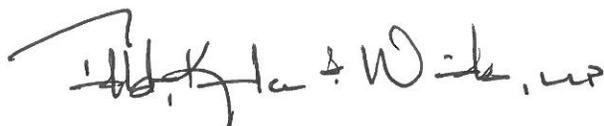
A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

We have audited the basic financial statements of the City as of and for the year ended June 30, 2011, and have issued our report thereon dated March 31, 2012. Our audit was performed for the purpose of forming opinions on the basic financial statements taken as a whole. The accompanying Schedule of Expenditures of Federal Awards is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

* * * * *

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CITY OF SHERWOOD

Sherwood, Oregon

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

FOR THE FISCAL YEAR ENDED JUNE 30, 2011

<u>Federal Grantor / Pass Through Grantor / Program and/or Cluster Title</u>	<u>CFDA Number</u>	<u>Dept. or Pass Through Entity Identifying</u>	<u>Federal Expenditures</u>
Housing and Urban Development Passed through Washington County CDBG - Entitlement Grants Cluster	14.218	1214	<u>\$ 102,412</u>
Department of Justice Bulletproof Vest Partnership Program	16.607	Direct	<u>5,767</u>
National Highway Traffic Safety Administration Passed Through OR Dept of Transportation/OR Chiefs of Police Highway Safety Cluster			
State and Community Highway Safety	20.600		4,222
Alcohol Traffic Safety and Drunk Driving Prevention Incentive	20.601		700
Total Highway Safety Cluster			<u>4,922</u>
Environmental Protection Agency Passed through Oregon Infrastructure Finance Authority Capitalization Grants for Drinking Water State Revolving Funds - Loan Balance \$6,000,000	66.468	S10003	<u>951,959</u>
Department of Homeland Security Passed through City of Portland Non-Profit Security Program	97.008	UA07-201	76,930
Non-Profit Security Program	97.008	UA07-202	25,050
Non-Profit Security Program	97.008	UA07-203	39,600
Non-Profit Security Program	97.008	07-0180	743
Non-Profit Security Program	97.008	07-0181	385
Subtotal CFDA 97.008			<u>142,708</u>
Passed through Oregon Military Dept State Homeland Security Program (SHSP)	97.073	09-282	<u>10,110</u>
Total Department of Homeland Security			<u>152,818</u>
			<u>\$ 1,217,878</u>

See Notes to Schedule of Expenditures of Federal Awards.

CITY OF SHERWOOD

NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

FOR THE FISCAL YEAR ENDED JUNE 30, 2011

PURPOSE OF THE SCHEDULE

The accompanying Schedule of Expenditures of Federal Awards (the "Schedule") is a supplementary schedule to City of Sherwood's (the City's) financial statements and is presented for purposes of additional analysis. Because the Schedule presents only a selected portion of the activities of the City, it is not intended to and does not present either the financial position or the results of operations of the City.

SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The information in the Schedule is presented in accordance with OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*.

Federal Financial Assistance

The Single Audit Act Amendment of 1996 and OMB Circular A-133, federal financial assistance is defined as assistance provided by a federal agency, either directly or indirectly, in the form of grants, contracts, cooperative agreements, loans, loan guarantees, property, interest subsidies, insurance, or direct appropriations. Accordingly, nonmonetary federal assistance, including federal surplus property, is included in federal financial assistance and, therefore, is reported on the Schedule, if applicable. Federal financial assistance does not include direct federal cash assistance to individuals. Solicited contracts between the state and federal government for which the federal government procures tangible goods or services are not considered to be federal financial assistance.

Major Programs

The Single Audit Act Amendment of 1996 and OMB Circular A-133 establish criteria to be used in defining major federal financial assistance programs. Major programs for the City are those programs selected for testing by the auditor using a risk-assessment model, as well as certain minimum expenditure requirements, as outlined in OMB Circular A-133. Programs with similar requirements may be grouped into a cluster for testing purposes.

Reporting Entity

The reporting entity is fully described in Notes to Financial Statements. Additionally, the Schedule includes all federal programs administered by the City for the year ended June 30, 2011.

Revenue and Expenditure Recognition

The receipt and expenditure of federal awards are accounted for under the modified accrual basis of accounting.

CITY OF SHERWOOD, OREGON

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

YEAR ENDED JUNE 30, 2011

SECTION I - SUMMARY OF AUDITOR'S RESULTS

Financial Statements:

Type of auditor's report issued: Unqualified

Internal control over financial reporting:

Material weakness(es) identified? Yes

Significant deficiency(ies) identified not considered to be material weakness(es)? Yes

Noncompliance material to financial statements noted? No

Federal Awards:

Internal control over major programs:

Material weakness(es) identified? No

Significant deficiency(ies) identified not considered to be material weakness(es)? No

Type of auditor's report issued on compliance for major programs: Unqualified

Any audit findings disclosed that are required to be reported in accordance with Section 510 (a) of *Circular A-133*? No

Identification of major programs:

CFDA NUMBER

NAME OF FEDERAL PROGRAM OR CLUSTER

66.468

Capitalization Grants for Drinking Water State Revolving Funds

Dollar threshold used to distinguish between type A and B programs: \$300,000

Auditee qualified as low-risk auditee? Yes

CITY OF SHERWOOD, OREGON

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS (Continued)

YEAR ENDED JUNE 30, 2011

SECTION II – FINANCIAL STATEMENT FINDINGS

Finding 2011-01:

Criteria: A restatement of previously issued financial statements required to correct errors in those financial statements typically indicates a material weakness in internal control over financial reporting, such that the system of internal control did not prevent or detect the error that ultimately led to the restatement.

Condition: The City restated beginning net assets in the governmental and business-type activities, as well as beginning fund balance in the General Fund, the Water Fund, the Sanitary Sewer Fund, the Storm Water Fund and the Telecommunications Fund in the City's fund statements. The restatement serves to properly report the Street Fund as a governmental fund as of June 30, 2010, as well as properly report capital assets and an interfund loan not properly reported in the prior year.

Context: The Street Fund, which is primarily supported through intergovernmental revenues and has expenditures primarily related to the maintenance and construction of general streets and roads infrastructure, was incorrectly reported as an enterprise fund in the prior year.

Capital assets in the governmental activities, related primarily to easements and land, totaling approximately \$2.5 million were not properly reflected in the financial statements for the City's fiscal year ended June 30, 2010. Capital assets in the Water, Sanitary Sewer and Storm Water Funds (enterprise funds) were misstated in the prior year by an aggregate total of approximately \$660,000.

An interfund loan between the Telecommunications Fund (a business-type activity) and the General Fund (governmental activity) in the amount of approximately \$937,000 was previously reported as revenues and expenditures/expenses through the fund statements and the entity-wide Statement of Activities.

Effect: Beginning net assets in the governmental activities was increased by approximately \$38 million, offset by a reduction in beginning net assets in the business-type activities. The restatements are offset by the various components of assets and liabilities associated with the Street Fund as reported at June 30, 2010 in the governmental and business-type activities, respectively.

Related to the misstatement of capital assets in the prior year, beginning net assets in the governmental activities and the business-type activities were increased by approximately \$2.5 million and \$660,000, respectively, offset by increases in capital assets. Beginning fund balance in the enterprise funds were restated, again offset by increases to reported

CITY OF SHERWOOD, OREGON

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS (Continued)

YEAR ENDED JUNE 30, 2011

SECTION II – FINANCIAL STATEMENT FINDINGS (Continued)

Finding 2011-01: (Continued)

Effect (Continued): capital assets in the respective funds, by a collective amount of approximately \$660,000.

Beginning net assets in the governmental activities were restated to reflect proper reporting of an interfund loan in the amount of approximately \$937,000, offset by a restatement in the business-type activities. Similarly, beginning fund balance in the General Fund and the Telecommunications Fund were restated to properly reflect the interfund loan between those funds.

Cause: The previous reporting of the Street Fund as an enterprise fund appears to have resulted from a misinterpretation in prior years, of the basis for reporting enterprise funds as prescribed in Governmental Accounting Standards Board (GASB) Statement No. 34.

The misstatement of capital assets in prior years appears to result from a lack of proper consideration given to easements as required under GASB Statement No. 51, and a lack of proper procedures in prior years to properly capture and value contributed assets.

Improper reporting of the interfund loan appears to have resulted from management's inexperience in past years with the reporting for such transactions under current GASB pronouncements.

Recommendation: The City has correctly reflected the Street Operations Fund and the Street Capital Fund (previously combined as the Street Fund) as governmental funds in their financial statements for the year ended June 30, 2011. We recommend that as the City considers additional funds in the future, that they evaluate the reporting of those funds within the parameters of GASB Statement No. 34.

Current management has developed practices to capture, evaluate and report contributed assets and intangibles in accordance with current guidance. We recommend that management continue to monitor and evaluate related transactions for proper reporting in the financial statements, and to ensure completeness of reported capital assets.

Current management identified the lack of proper reporting of the interfund loan during the audit. We recommend that management continue to monitor interfund transactions for proper classification as loans when applicable, and provide for proper reporting within the financial statements going forward.

View of Responsible Officials:

Management understands and concurs with this finding.

CITY OF SHERWOOD, OREGON

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS (Continued)

YEAR ENDED JUNE 30, 2011

SECTION II – FINANCIAL STATEMENT FINDINGS (Continued)

Finding 2011-02:

Criteria: A system of internal control over financial reporting is required to ensure amounts reported are fairly stated in all material respects in relation to the basic financial statements taken as a whole, and in relation to the various opinion units of those financial statements.

Condition: Several balances identified as significant in our audit were identified as being materially misstated. Those balances include accounts receivable and related revenues in the Sanitary Sewer Fund, capital asset additions resulting from developer contributions impacting governmental activities, and the enterprise funds, and intergovernmental revenue and related receivables of \$2.3 million attributable to the prior year, but reported in 2011.

Context: Accounts receivable and revenues in the Sewer Fund related to billings and collection transactions between the City and Clean Water Services of Washington County were over stated due to an overbilling by the City in the amount of approximately \$126,000.

Capital assets in the governmental activities, and the Water, Sanitary Sewer and Storm Water Funds were misstated by an aggregate amount of approximately \$533,000, and subsequently corrected through adjustments to properly reflect the value of contributed infrastructure.

The City properly reported expenditures of federal grant dollars on their Schedule of Expenditures of Federal Awards for the year ended June 30, 2010, but did not accrue the receivable or revenue related to those expenditures to that year, totaling approximately \$2.3 million. The reimbursement of those expenditures was received in fiscal 2011, and recorded as revenue for that year.

Effect: Accounts were initially, materially misstated as of and for the year ended June 30, 2011 in the amounts specified above in the trial balance presented for audit. Adjustments were proposed and recorded to correct balances for the misstatements at year end.

Cause: The overstatement of receivables and revenue in relation to the City's transactions with Clean Water Services appear to have resulted from miscommunication between City departments on the status of projects and related billings.

The City recorded capital assets (infrastructure) contributed by private developers valued based on preliminary estimates of the projects rather than actual costs.

CITY OF SHERWOOD, OREGON

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS (Continued)

YEAR ENDED JUNE 30, 2011

SECTION II – FINANCIAL STATEMENT FINDINGS (Continued)

Finding 2011-02 (Continued):

Cause (Continued): The City's overstatement of revenues related to federal grants in 2011 appears to result from revenue recognition related to the timing difference between when expenses were incurred the related request for reimbursement.

Recommendation: We recommend that the City reevaluate current policies and procedures related to revenue recognition including those around interagency billings, estimations of value related to private contributions, and grant revenues based on qualifying expenditures. Consideration of a centralized contract and grants management function for the City may also provide enhanced oversight and controls over these transactions and related reporting.

View of Responsible Officials: Management understands and concurs with this finding.

Finding 2011-03:

Criteria: A system of internal control over financial reporting is required to ensure proper segregation of duties, specifically in functions that may be considered incompatible.

Condition: In our audit, we noted that personnel in the City's Finance Department have access and authority within the financial system to create vendors and process payments through accounts payable. We believe that these functions are incompatible in a single position, in the absence of mitigating or compensating controls.

Context: There appear to be no compensating or mitigating controls in the form of management review of change logs within the vendor master file, etc.

Effect: The ability to both create/edit vendors and process related accounts payable transactions presents an opportunity to potentially create and process a fraudulent payment within the financial system, which may go undetected given current controls in place.

Cause: The responsibility in a single position for both establishing vendors and processing accounts payable appears to result from a prioritization of scarce personnel resources.

Recommendation: We recommend that management either segregate the creation/edit of vendor files from the processing of payments, or implement reviews or other compensating/mitigating controls over accounts payable.

View of Responsible Officials: Management understands and concurs with this finding.

CITY OF SHERWOOD, OREGON

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS (Continued)

YEAR ENDED JUNE 30, 2011

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

None