COUNTY OF ERIE

STEFAN I. MYCHAJLIW
COMPTROLLER

September 12, 2014

The Erie County Legislature
92 Franklin Street
Buffalo, New York 14202

Honorable Mark C. Poloncarz
Erie County Executive
95 Franklin Street
Buffalo, New York 14202

Dear Honorable Members and County Executive Poloncarz:

Enclosed is a copy of the external auditor's (Drescher & Malecki LLP) Management Letter for Erie County for the year ended December 31, 2013.

Please be advised that although the Management Letter is dated June 12, 2014, this represents the date that the external auditors completed their audit and field work for the 2013 audit. The letter was actually issued today by Drescher & Malecki.

If you have any questions regarding the 2013 Management Letter, please contact me at 858-8400.

Very truly yours,

Stefan I. Mychajliw
Erie County Comptroller

SIM/nr
Enclosure
c: Robert W. Keating, Director, Budget and Management
Erie County Audit Committee Members
Drescher & Malecki LLP (without Enclosure)

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Drescher & Malecki LLP
3083 William Street, Suite 5
Cheektowaga, New York 14227
Telephone: 716.565.2299
Fax: 716-565-2201

Certified Public Accountants

June 12, 2014

Honorable County Legislature,
County Executive and County Comptroller
County of Erie, New York:

In planning and performing our audit of the basic financial statements of the County of Erie, New York (the "County") as of and for the year ended December 31, 2013, 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, we considered the County's internal control over financial reporting ("internal control") 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 entity's internal control. Accordingly, we do not express an opinion on the effectiveness of the County's internal control over financial reporting.

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. A material weakness is a deficiency, or a 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.

Our consideration of internal control was for the limited purpose described in the first paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

We did identify certain matters involving the internal control and other operational matters that are presented for your consideration. This letter does not affect our report dated June 12, 2014 on the financial statements of the County (which report refers to other auditors). We will review the status of these comments during our next audit engagement. Our comments and recommendations, all of which have been discussed with appropriate members of management, are intended to improve the internal control or result in other operating efficiencies. Our comments are summarized in Exhibit I.

We also summarized new reporting requirements in Appendix A. These should be evaluated to determine the extent the County will be impacted in the future years.

The purpose of this communication, which is an integral part of our audit, is to describe, for management and those charged with governance, the scope of our testing of internal control and the results of that testing. Accordingly, this communication is not intended to be and should not be used for any other purpose.

Drescher & Malecki LLP

June 12, 2014

Classification of Leases

The County does not have a formalized policy for the evaluation of leases as to whether amounts should be classified as operating or capital. We identified areas in which the County was unable to accurately provide essential information to determine the lease classification. Prior to the inception of a lease, the County should evaluate the specified criteria to determine the proper treatment and classification of such transaction in accordance with Governmental Accounting Standards Board ("GASB"). The County should design and implement procedures to reasonably estimate the economic useful life, present value of the minimum lease payments and fair market value of the lease.

We recommend that the County review the specified criteria for capital leases contained in GASB and develop a policy to ensure leases are appropriately evaluated prior to their inception.

Succession Planning

The County continues to face the challenge of ensuring continuity and consistency of service delivery due to employee turnover. Certain key accountants will soon be eligible to retire. While we applaud the County's actions to add accountants, prepare written policies and procedures, and perform cross-training of various job responsibilities within the Comptroller's Office, the County should consider the following key issues and develop strategies concerning succession planning recommended by the Government Finance Officers Association:

- Continually assess potential employee turnover.
- Develop listing of candidates for key accounting positions.
- Provide a formal, written succession plan as a framework for succession initiatives.
- Continually develop written policies and procedures to facilitate knowledge transfer.
- Development of leadership skills should be a key component of any succession planning initiative.

Asset Inventory

The County has established policies and procedures to ensure departmental inventory is periodically tracked and documented; however, while performing tests of controls we noted that the County did not update and maintain some inventory schedules during the 2013 fiscal year.

We recommend that the County redistribute the inventory tracking policy and procedure to applicable County personnel to emphasize its importance and to ensure its compliance. This will help strengthen the safeguarding of assets and reliability of inventory schedules. Further, the County should perform surprise inventory counts to gain confidence that items recorded by the departments are, in fact, available.

Due Diligence on Bank and Treasury Management Providers

The County has the fiduciary duty to protect and safeguard the public funds entrusted to them, one of which is the proper selection of, and ongoing oversight of, bank depositories and treasury management service providers. County cash and near-cash assets are processed and held by banks and their third-party partners; therefore, it is important to carefully choose bank vendors and to perform on-going supervision and evaluation of each bank that processes and/or holds government assets. As part of a due diligence program, County management should review the quarterly and annual financial reports of key counterparty banks as well as summary reports retrieved from each bank's regulator. These quarterly summary reports are known as Call Reports. Regulators establish certain key publicly reported financial standards for banks, such as the Total Risk Based Capital Ratio, the Tier 1 Risk Based Capital Ratio or the Leverage Ratio. Banks must maintain sufficient book equity capital to meet the regulatory minimums otherwise the regulator will require that the bank raise new capital.

The Government Finance Officers Association ("GFOA") recommends that government treasury practitioners review the regulated banks and regulated and non-regulated bank partners that process, validate, transfer, disburse and "hold on deposit" cash and near cash assets and apply prudent due diligence throughout the life of the relationship. As part of the ongoing due diligence and prudent management of relationships, the GFOA further recommends that governments evaluate their key bank(s) and issue an internal Bank Review Summary on a quarterly basis. In addition to monitoring and reporting, the government's operating relationship with a bank processor of cash and near cash assets should be managed pro-actively.

Implementing OMB Uniform Guidance

In late 2013, the U.S. Office of Management and Budget ("OMB") published final guidance in the Federal Register entitled *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* ("Uniform Guidance"). The Uniform Guidance supersedes and combines the requirements of eight previous OMB Circulars (including, but not limited to, A-133) with the intent to streamline the federal grant-making and monitoring process, to ease administrative burden for grant applicants and recipients, and to reduce the risk of waste, fraud and abuse. The Uniform Guidance is located in Title 2, Part 200 of the *Code of Federal Regulations*. State and local governments need to take appropriate steps to ensure that they comply fully with the new Uniform Guidance, which sometimes differs in subtle, but important ways from previous guidance.

The County should take all of the following steps to ensure they fully comply with the provisions of the OMB's Uniform Guidance:

- Communicate to all agencies, departments, and personnel throughout the County that the requirements for federal awards have changed.
- Inform its agencies, departments, and personnel that the Uniform Guidance is first effective for audits for the fiscal year ending December 31, 2015.
- Determine what monitoring activity may be necessary for any recipients that no longer will obtain a Single Audit or a program-specific audit because the Uniform Guidance raised the spending threshold from $500,000 to $750,000.
- For subrecipients that will require monitoring, the subaward agreement should include: 1) all of the requirements that must be met by the subrecipient to ensure that the federal award is used in accordance with federal statutes, regulations, and the specific terms and conditions of the federal award; and 2) any additional requirements that the subrecipient must meet for the County to fulfill its own responsibility to the federal awarding agency, including identification of any required financial and performance reports.
- Identify what, if any, specific performance measurement requirements relate to a particular federal award to ensure that the County will be able to comply with them.

APPENDIX A

NEW REPORTING REQUIREMENTS

The Governmental Accounting Standards Board ("GASB") has adopted several new pronouncements, which may have a future impact upon the County:

GASB Statement No. 67—The County is required to implement GASB Statement No. 67, *Financial Reporting for Pension Plans—an amendment of GASB Statement No. 25*, effective for the fiscal year ending December 31, 2014. The objective of this Statement is to improve financial reporting by state and local governmental pension plans.

GASB Statement No. 68—The County is required to implement GASB Statement No. 68, *Accounting and Financial Reporting for Pensions—an amendment of GASB Statement No. 27*, effective for the fiscal year ending December 31, 2015. The primary objective of this Statement is to improve accounting and financial reporting by state and local governments for pensions.

GASB Statement No. 69—The County is required to implement GASB Statement No. 69, *Government Combinations and Disposals of Government Operations*, effective for the fiscal year ending December 31, 2014. This Statement establishes accounting and financial reporting standards related to government combinations and disposals of government operations.

GASB Statement No. 70—The County is required to implement GASB Statement No. 70, *Accounting and Financial Reporting for Nonexchange Financial Guarantees*, effective for the fiscal year ending December 31, 2014. The objective of this Statement is to enhance comparability of financial statements among governments by requiring consistent reporting by those governments that extend nonexchange financial guarantees and by those governments that receive nonexchange financial guarantees.

GASB Statement No. 71—The County is required to implement GASB Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date—an amendment of GASB Statement No. 68*. The provisions of this Statement should be applied simultaneously with the provisions of Statement No. 68. The objective of this Statement is to address an issue regarding application of the transition provisions of Statement No. 68, *Accounting and Financial Reporting for Pensions*. The issue relates to amounts associated with contributions, if any, made by a state or local government employer or nonemployer contributing entity to a defined benefit pension plan after the measurement date of the government's beginning net pension liability.