

**COUNTY OF HUMBOLDT**

**Management Report  
with Required Communication**

**For the Year Ended June 30, 2016**

THIS PAGE INTENTIONALLY LEFT BLANK

**COUNTY OF HUMBOLDT**

Management Report  
For the Year Ended June 30, 2016

Table of Contents

	<u>Page</u>
Introduction.....	1
Required Communication.....	2-4
Current Year Comments and Recommendations .....	5-9
Status of Prior Year Comments and Recommendations.....	10-11

THIS PAGE INTENTIONALLY LEFT BLANK

To the Honorable Members of the  
Board of Supervisors of the County of Humboldt  
Eureka, California

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the County of Humboldt (County) for the year ended June 30, 2016. Professional standards require that we provide you with information about our responsibilities under generally accepted auditing standards, *Government Auditing Standards* and Title 2 U.S. Code of Federal Regulations (CFR) Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (the Uniform Guidance), as well as certain information related to the planned scope and timing of our audit. We have communicated such information in our engagement letter dated April 4, 2016. Professional standards also require that we communicate to you the following information related to our audit as discussed in the Required Communications section of this report.

In planning and performing our audit of the basic financial statements of the County for the fiscal year ended June 30, 2016, in accordance with auditing standards generally accepted in the United States of America, we considered its internal control over financial reporting as a basis for designing our audit procedures for the purpose of expressing an opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the County's internal control. Accordingly, we do not express an opinion on the effectiveness of the County's internal control.

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 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 would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. In addition, because of inherent limitations in internal control, including the possibility of management override of controls, misstatements due to error or fraud may occur and not be detected by such controls.

We previously reported on the County's internal control in our Single Audit report dated December 22, 2016, which contains our report on significant deficiencies and material weaknesses in the County's internal control. This letter does not affect our report dated December 22, 2016, on the basic financial statements of the County of Humboldt.

During our audit we also became aware of several matters that are opportunities for strengthening internal controls and operating efficiency. The memorandum that accompanies this letter summarizes our comments and suggestions regarding those matters.

This report is intended for the use of management, the Board of Supervisors, and officials of the federal and state grantor agencies.

We thank the County's staff for its cooperation during our audit.



Roseville, California  
December 22, 2016

## COUNTY OF HUMBOLDT

Management Report  
Required Communication  
For the Year Ended June 30, 2016

### **Our Responsibilities Under *U.S. Generally Accepted Auditing Standards and Title 2 CFR Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards (the Uniform Guidance)***

As communicated in our engagement letter dated April 4, 2016, our responsibility, as described by professional standards, is to form and express opinions about whether the financial statements that have been prepared by management with your oversight are presented fairly, in all material respects, in conformity with accounting principles generally accepted in the United States of America. Our audit of the financial statements does not relieve you or management of your respective responsibilities.

Our responsibility, as prescribed by professional standards, is to plan and perform our audit to obtain reasonable, rather than absolute, assurance about whether the financial statements are free of material misstatement. An audit of financial statements includes consideration of 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 entity's internal control over financial reporting. Accordingly, as part of our audit, we considered the internal control of the County of Humboldt solely for the purpose of determining our audit procedures and not to provide any assurance concerning such internal control.

We also considered internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine 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 the Uniform Guidance.

As part of obtaining reasonable assurance about whether the County's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, 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. Also, in accordance with the Uniform Guidance, we examined, on a test basis, evidence about the County's compliance with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) Uniform Guidance Compliance Supplement applicable to each of its major federal programs for the purpose of expressing an opinion on the County's compliance with those requirements. While our audit provides a reasonable basis for our opinion, it does not provide a legal determination on the County's compliance with those requirements.

We are also responsible for communicating significant matters related to the audit that are, in our professional judgment, relevant to your responsibilities in overseeing the financial reporting process. However, we are not required to design procedures for the purpose of identifying other matters to communicate to you.

We have provided our findings regarding material weaknesses over financial reporting noted during our audit in our Single Audit report dated December 22, 2016.

### **Planned Scope of Audit**

We performed the audit according to the planned scope and timing previously communicated to you in our engagement letter dated April 4, 2016.

### **Compliance with All Ethics Requirements Regarding Independence**

The engagement team, others in our firm, and as appropriate, our firm, and our network firms have complied with all relevant ethical requirements regarding independence.

## COUNTY OF HUMBOLDT

Management Report  
Required Communication  
For the Year Ended June 30, 2016

### **Qualitative Aspects of the Entity's Significant Accounting Practices**

#### *Significant Accounting Policies*

Management has the responsibility to select and use appropriate accounting policies. A summary of the significant accounting policies adopted by the County of Humboldt is included in Note 1 to the financial statements. There have been no initial selection of accounting policies and no changes in significant accounting policies or their application during the year ended June 30, 2016.

No matters have come to our attention that would require us, under professional standards, to inform you about (1) the methods used to account for significant unusual transactions and (2) the effect of significant accounting policies in controversial or emerging areas for which there is a lack of authoritative guidance or consensus.

#### *Significant Accounting Estimates*

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimates affecting the financial statements are discussed below:

- Management believes receivables are fully collectible based on historical experience. Accordingly, no allowance for doubtful accounts is included in the financial statements.
- Management's estimate of the County's general liability self-insurance estimate is based on open claims and an additional allowance.
- Management's estimate of the other post-employment benefits (OPEB) is based on actuarial valuation reports prepared by outside specialists.
- Management's estimate of the net pension liability and related deferred inflows/outflows is based on actuarial valuation reports prepared by CalPERS and outside specialists.

We evaluated the key factors and assumptions used to develop the estimates described above and determined that they are reasonable in relation to the basic financial statements taken as a whole and in relation to the applicable opinion units.

#### **Significant Difficulties Encountered During the Audit**

We encountered no significant difficulties in dealing with management relating to the performance of the audit.

## **COUNTY OF HUMBOLDT**

### **Management Report Required Communication For the Year Ended June 30, 2016**

#### **Corrected and Uncorrected Misstatements**

For purposes of this communication, professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that we believe are trivial, and communicate them to the appropriate level of management. Further, professional standards require us to also communicate the effect of uncorrected misstatements related to prior periods on the relevant classes of transactions, account balances or disclosures, and the financial statements as a whole and each applicable opinion unit. No material misstatements were noted as a result of our audit.

#### **Disagreements with Management**

For purposes of this letter, professional standards define a disagreement with management as a matter, whether or not resolved to our satisfaction, concerning a financial accounting, reporting, or auditing matter, which could be significant to the County's financial statements or the auditor's report. No such disagreements arose during the course of the audit.

#### **Representations Requested from Management**

We have requested certain written representations from management, which are included in the management representation letter dated December 22, 2016.

#### **Management's Consultations with Other Accountants**

In some cases, management may decide to consult with other accountants about auditing and accounting matters. Management informed us that, and to our knowledge, there were no consultations with other accountants regarding auditing and accounting matters.

#### **Other Significant Matters, Findings, or Issues**

In the normal course of our professional association with the County of Humboldt, we generally discuss a variety of matters, including the application of accounting principles and auditing standards, operating and regulatory conditions affecting the entity, and operational plans and strategies that may affect the risks of material misstatement. None of the matters discussed resulted in a condition to our retention as the County's auditors.

This report is intended solely for the information and use of the Board of Supervisors, and management of the County of Humboldt and is not intended to be and should not be used by anyone other than these specified parties.

## COUNTY OF HUMBOLDT

### Management Report – Current Year Comments and Recommendations For the Year Ended June 30, 2016

#### **DISAGGREGATION OF RECEIVABLES**

##### Criteria

Governmental Accounting Standards Board Statement No. 38, *Certain Financial Statement Disclosures*, requires components of significant receivables to be disclosed in the financial statements. Components of receivables include accounts receivable (due from citizens), taxes (property, sales taxes, transient occupancy) receivable, interest receivable, amounts due from other governments and notes receivable.

##### Condition

Currently, the County records accounts receivable, taxes receivable and due from other governments within the same receivable account within its general ledger. However, the County's recently updated its chart of accounts to include separate accounts for the various types of receivables.

##### Cause

The County's chart of accounts did not have separate accounts for the various types of receivables until recently.

##### Effect of Condition

By not properly classifying receivables in its general ledger, the County is relying on external spreadsheets to ensure receivables are properly disclosed for financial reporting.

##### Recommendation

We recommend the County utilize its chart of accounts to account for the various receivable and payable types, including accounts receivable, loans receivable, interfund advances (and payables) and amounts due from other governments. Year-end closing procedures should be modified to capture receivable balances into each of these accounts according to their nature.

##### Management Response

We agree that disaggregation of receivables will aid in accounting for these assets and will establish new accounts and accounting procedures to accomplish that.

#### **GOVERNMENTAL TRUST FUNDS**

##### Criteria

Under Governmental Accounting Standards Board Statement No. 34 (GASB 34), amounts formally held in trust but used to support the County's own programs should be reported as funds within the County's reporting entity so as to ensure all economic resources that can be used by the County are reported in their financial statements. Activity in these accounts is required to be included in the County's reporting entity, either as additional funds or transactions in existing county funds.

Use of the agency fund type is limited to resources the County holds purely in a custodial capacity for individuals or other organizations, such as school districts and special districts not governed by the County Board of Supervisors.

## COUNTY OF HUMBOLDT

### Management Report – Current Year Comments and Recommendations For the Year Ended June 30, 2016

#### **GOVERNMENTAL TRUST FUNDS** (continued)

##### Condition

The County is currently maintaining more than 150 governmental trust funds to track activity benefitting the General Fund and other primary operating funds of the County.

##### Cause

Before GASB Statement No. 34 took effect, the County's current treatment was permitted. Although reporting requirements have changed, the County still has a need to account for these resources separately from other general fund resources.

##### Effect of Condition

By excluding transaction activity in these funds, balances for revenues and expenses in the County's own financial reports (including budgetary reports) are not complete.

There is the potential to double-report revenues when resources are transferred into operating funds. Using multiple funds within the accounting system to control the flow of revenues increases the potential for reporting revenues twice.

As the County does not budget for any activity occurring in these governmental trust funds, any deviations from the adopted budget are not apparent until well after the end of the fiscal year and thus cannot be addressed when they occur.

##### Recommendation

We recommend the County analyze each of its governmental trust funds to determine if there is a particular need to account for resources separately from the primary operating funds of the County. We further recommend the County implement controls to minimize the double reporting of revenues and expenditures when utilizing these trust funds for controlling the flow of resources.

##### Management Response

Generally accepted accounting principles hold that the ideal number of trust funds a government should have is the smallest number that enables that government to achieve its purposes. The number of trust funds established by the County of Humboldt over the past several decades has proliferated with adverse effect on accounting controls, especially in light of the reduced number of accounting staff overseeing the general ledger in recent years.

We agree that many currently active trust funds should be closed and those funds moved into budgeted accounts in the main County operating trusts. The Auditor-Controller and County Administrative Office will work with departments to identify trust funds that should be closed in order to simplify our account structure.

## COUNTY OF HUMBOLDT

### Management Report – Current Year Comments and Recommendations For the Year Ended June 30, 2016

#### USE OF MISCELLANEOUS REVENUE ACCOUNT

##### Criteria

The miscellaneous revenue account should be used to record revenues that fall outside of the other revenue categories, such as intergovernmental revenues and charges for services, and that are considered to be infrequent in nature.

##### Condition

We noted that the County's use of the miscellaneous revenue account (i.e., account 808000) includes various types of revenue, including intergovernmental revenues and revenue generated from charges for services. During the audit, we noted that the miscellaneous revenue accounts aggregated for County funds were in excess of \$3.8 million.

##### Cause

Departments have initial responsibility for classifying cash receipts for financial reporting and may not have adequate knowledge or guidance to properly classify certain revenues. In the absence of other guidance, departments likely record revenues they are unsure of in the miscellaneous revenue account.

##### Effect of Condition

When revenues are improperly classified as miscellaneous revenues the true condition of the fund may be misleading. The level of detail for classifying transactions should be sufficiently categorized so as to be meaningful to management in making decisions.

##### Recommendation

We recommend that the County consider restricting the use of its miscellaneous revenue account for revenue sources that cannot be categorized under the existing revenue types, including charges for services, fines, intergovernmental revenues, and licenses and permits.

##### Management Response

The generic revenue object, 808000, is primarily used in fiduciary or agency funds where the name of the fund identifies the revenue stream. For the most part these funds are used to channel a single type of revenue so further identification of the revenue isn't necessary for staff familiar with that particular program. Using more descriptive revenue objects would however help auditors and others who are less familiar with these programs, so we see the value of creating more revenue objects to convey more specific information about these revenue streams. We will work with the departments and administration to assign more descriptive revenue objects to our various programs.

## COUNTY OF HUMBOLDT

### Management Report – Current Year Comments and Recommendations For the Year Ended June 30, 2016

#### **EXPAND CHART OF ACCOUNTS IN CERTAIN FUNDS**

##### Criteria

The County's chart of accounts should be detailed enough as to provide adequate management information.

##### Condition

During our review of the County's debt service fund, we noted that the County recorded its annual net change in the cash with fiscal agent account balance to a single expenditure account.

##### Cause

The County relies on various spreadsheets to track certain accounts at a more detailed level. For example, the County maintains a spreadsheet to track the activity of the debt service fund, including interest earnings and debt service payments.

##### Effect of Condition

In some cases, the chart of accounts is too general to provide the information needed for management to make decisions or for the County to prepare its annual State Controller's report and annual financial statements without having to rely on spreadsheets and other records external to the general ledger.

##### Recommendation

We recommend the County expand its chart of accounts in certain funds where applicable to be used for significant accounts, such as major sources of revenues and expenditures. In the debt service fund, for example, the County should report the change in the cash with fiscal agent account as adjustments to debt service principal and interest expenditures and interest earnings rather than as a net change to trust fund expenditures.

##### Management Response

As noted in our previous response, we do have room in our chart of accounts for more descriptive account objects. Especially in dealing with debt service, accounts for principal and interest should be clearly identified and we will make that change.

## COUNTY OF HUMBOLDT

### Management Report – Current Year Comments and Recommendations For the Year Ended June 30, 2016

#### **FORMAL CAPITAL ASSET POLICY**

##### Criteria

The County has a significant investment in capital assets, such as land, buildings, roads and equipment. Adopting a policy will help ensure that the County's capital assets are acquired, safeguarded, controlled, disposed of and accounted for in accordance with state and federal regulations, audit requirements and generally accepted accounting principles.

##### Condition

At the time of our audit, we noted that the County did not have a formal capital asset policy.

##### Cause

The County has not yet written a formal policy for the capitalization of assets.

##### Effect of Condition

Without a written capitalization policy, inconsistencies and misunderstandings regarding proper policy capitalization thresholds and estimated useful asset lives are likely to occur. In addition, misstatement of net capital assets as well as a lack of comparability between years can result when policies and procedures regarding capital assets are unclear.

##### Recommendation

We recommend that the County adopt a comprehensive capitalization policy which includes all required capital asset accounting elements.

##### Management Response

We agree that the County should adopt a comprehensive capitalization policy and will conduct research to find an appropriate model that can be adopted for our use.

## COUNTY OF HUMBOLDT

### Management Report – Status of Prior Year Comments and Recommendations For the Year Ended June 30, 2016

#### **DISAGGREGATION OF RECEIVABLES**

##### Recommendation

We recommend the County utilize its chart of accounts to account for the various receivable and payable types, including accounts receivable, loans receivable, interfund advances (and payables) and amounts due from other governments. Year-end closing procedures should be modified to capture receivable balances into each of these accounts according to their nature.

##### Status

Partially implemented. The County expanded its chart of accounts to include various types of receivables.

#### **GOVERNMENTAL TRUST FUNDS**

##### Recommendation

We recommend the County analyze each of its governmental trust funds to determine if there is a particular need to account for resources separately from the primary operating funds of the County. We further recommend the County implement controls to minimize the double reporting of revenues and expenditures when utilizing these trust funds for controlling the flow of resources.

##### Status

In Progress.

#### **USE OF MISCELLANEOUS REVENUE ACCOUNT**

##### Recommendation

We recommend that the County consider restricting the use of its miscellaneous revenue account for revenue sources that cannot be categorized under the existing revenue types, including charges for services, fines, intergovernmental revenues, and licenses and permits.

##### Status

Not implemented.

#### **EXPAND CHART OF ACCOUNTS IN CERTAIN FUNDS**

##### Recommendation

We recommend the County expand its chart of accounts in certain funds where applicable to be used for significant accounts, such as major sources of revenues and expenditures. In the debt service fund, for example, the County should report the change in the cash with fiscal agent account as adjustments to debt service principal and interest expenditures and interest earnings rather than as a net change to trust fund expenditures.

##### Status

In progress. The County recently added additional accounts to its general ledger.

## COUNTY OF HUMBOLDT

### Management Report – Status of Prior Year Comments and Recommendations For the Year Ended June 30, 2016

#### **FORMAL CAPITAL ASSET POLICY**

##### Recommendation

We recommend that the County adopt a comprehensive capitalization policy which includes all required capital asset accounting elements.

##### Status

Not implemented.