

METROPOLITAN WASHINGTON COUNCIL OF GOVERNMENTS
777 North Capitol Street NE
Washington, DC 20002

Date: November 5, 2008
To: COG Board of Directors
From: David Robertson, Executive Director
Subject: FY 2008 Audit

I am pleased to report that the Metropolitan Washington Council of Governments (COG) again received an unqualified or “clean” audit for FY 2008 (July 1, 2007 to June 30, 2008) from Bert Smith & Company, COG’s auditor for the period FY 2005 through FY 2008.

Background

Effective with the FY 2008 audit, responsibility for audit oversight was shifted to a new Audit Committee. Previously, audit oversight was the responsibility of the COG Budget and Finance Committee. The new committee was established to provide more focused and independent review of COG’s audit and to comply with new audit standards and guidelines affecting not-for-profit corporations, such as COG.

FY 2008 Audit Committee members included: *Tony Knotts*, Prince George’s County; *Dan Tangherlini* (Merav Bushlin, alt.), District of Columbia; and *Lori Waters*, Loudoun County. The Committee met twice with COG management and representatives of Bert Smith & Company in performance of its audit oversight responsibilities on July 16 and October 22.

Audit Findings

Bert Smith & Company reviewed the draft FY 2008 audit with the Committee on October 22. COG received an unqualified or “clean” audit. Bert Smith & Company noted two FY 2008 financial statement findings in its report. In addition to the financial statement findings, the Committee discussed several issues and made suggestions for how the FY 2008 audit could be better presented to the COG Board on November 10.

- *Financial Statement Finding 2008-1 (page 37)*
Because of the nature of COG funding, budgets are organized by project or grant funding source. The auditor recommended that COG establish written procedures concerning the process and frequency of budget updates to ensure the currency of all project and operating account budgets.

Management Response: Management concurs with the finding and will develop written procedures.

- *Financial Statement Finding 2008-2 (page 38)*
COG accounting staff makes regular entries in its accounting system throughout the fiscal year. The auditor initially found some adjusting entries had insufficient approval and/or documentation, which was subsequently provided. The auditor recommended that COG establish written procedures for all adjusting entries.

Management Response: Management concurs with the finding and has implemented written procedures.

- *FY 2007 Audit Findings*
COG management and the auditor noted that the two financial statement findings from the FY 2007 audit were corrected as recommended.

Management Response: No response required.

- *FDIC Insurance (page 18)*
The Committee recommended that there be a reference to the new higher limit on FDIC insurance on deposits and that COG collateralize its account balances to limit exposure from accounts in excess of the new FDIC limit.

Management Response: The disclosure in the FY2008 audit report will be expanded to include the new FDIC limit. Management will explore possibility of collateralizing the bank accounts. The excess cash is invested in a pool of high-rated US government securities in compliance to the investment policy.

- *Credit Risk (page 18)*
The Committee discussed the credit risk of COG investments and requested that the clarifying text be included in this section.

Management Response: Management has investigated the credit risk and found that COG bonds are still AAA rated and backed by the US Government.

- *Annual Pension Cost (page 20, 21)*
The Committee discussed the annual cost of COG's defined benefit pension plan. The auditor extracts information from the actuary report provided by COG's pension actuary, Cheiron, Inc.

Management Response: The pension cost figures were revised by Cheiron. COG has not significantly modified its pension plan benefit since 2001 when benefits were adjusted and COG and employee contributions reduced to begin a gradual process of reducing its pension plan surplus. The surplus in part stemmed from pension investment returns that exceeded benchmarks and expectations. Cheiron has projected that the surplus is now largely exhausted and that with uncertain market conditions, pension contributions will likely need

to increase in the future to address pension liabilities. Effective October 2008, COG and employee pension contributions were increased by one percent, respectively. The Pension Plan Administrative Committee (which has three COG Board representatives) will meet prior to the end of 2008 to review COG's pension investment policy, investment performance, and updated actuarial projects and develop recommendations, as warranted, for COG Board review and action.

- **COG Reserve**
COG added \$764,414 to its General Fund Reserve balance as of the end of FY 2008, for a total of \$8,515,178. The Committee discussed COG's reserve fund balance and asked that this information be presented in the context of the COG Board approved reserve fund policy and targets.

Management Response: The COG reserve policy was adopted by the COG Board of Directors in November 2004. The COG Board approved reserve targets based on the adopted fiscal year Work Program and Budget (WPB), provided for limited use of building and interest income for capital or operating contingency expenses as part of the fiscal year budget, and greatly limited use of reserve "principal" except in the most extraordinary of circumstances. COG Board approval is required for any use of capital and operating contingency or the endowment/general reserve. FY 2008 reserve fund target and balance information is shown in the table below.

| RESERVE | TARGET | FY 2008 AMT |
|----------------------------------|-----------------------------------|-------------|
| FY 2008 Approved WPB | | \$25.8 M |
| Endowment Reserve | 25% of WPB, not less than \$1.5 M | \$6.5 M |
| General Reserve | 15% of WPB, not less than \$2.5 M | \$3.9 M |
| Total Reserve Target | | \$10.3 M |
| FY 2008 Reserve Balance | | \$8.5 M |
| Reserve Target Surplus/(Deficit) | | (\$1.8 M) |

Additional Information

The COG Board of Directors has recommended that COG select a new auditor on a competitive solicitation basis every three to four years and that the immediate past auditor not be eligible to compete for this contract award. Bert Smith & Company has been COG's auditor for four years, including the important transition period in 2007 following the retirement of Sonny Amores, the prior Chief Financial Officer and the appointment of Ray Rawlins, the current Chief Financial Officer. COG will solicit proposals for a new auditor in early 2009. COG management appreciates the support and assistance provided by Bert Smith & Company these past four years.

Following COG Board review and acceptance, copies of the FY 2008 audit will be posted on COG's web site and made available to grantor and funding agencies and member governments.