

COMMUNICATIONS WITH THOSE CHARGED WITH GOVERNANCE UNDER SAS NO. 114

To the City Council Members, and
LaVonne Griffin-Valade, City Auditor
City of Portland, 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 Portland, Oregon (the City) as of and for the year ended June 30, 2012, and have issued our report thereon dated December 21, 2012. Professional standards require that we provide you with the following information related to our audit.

OUR RESPONSIBILITY UNDER AUDITING STANDARDS GENERALLY ACCEPTED IN THE UNITED STATES OF AMERICA, THE SINGLE AUDIT ACT, AND THE OFFICE OF MANAGEMENT AND BUDGET CIRCULAR A-133

As stated in audit contract that became effective on May 18, 2012, our responsibility, as described by professional standards, is to form and express an opinion about whether the financial statements prepared by management with your oversight are fairly presented, in all material respects, in conformity with U.S. generally accepted accounting principles. Our audit of the financial statements does not relieve you or management of your responsibilities.

Our responsibility is to plan and perform the audit in accordance with generally accepted auditing standards and to design the 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 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. 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 OMB Circular A-133.

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 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 OMB Circular A-133, we examined, on a test basis, evidence about the City's compliance with the types of compliance requirements described in the "U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement" applicable to each of its major federal programs for the purpose of expressing an opinion on the City's compliance with those requirements. While our audit provides a reasonable basis for our opinion, it does not provide a legal determination on the City's compliance with those requirements.

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We are also responsible for communicating significant matters related to the financial statement audit that, in our professional judgment, are 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.

OTHER INFORMATION IN DOCUMENTS CONTAINING AUDITED FINANCIAL STATEMENTS

Our responsibility for other information in our Independent Auditor's Report and Financial Statements does not extend beyond the financial information identified in our report. We do not have an obligation to perform any procedures to corroborate other information contained in these documents. However, we have read the information and nothing came to our attention that caused us to believe that such information or its manner of presentation is materially inconsistent with the information or manner of its presentation appearing in the financial statements.

PLANNED SCOPE AND TIMING OF THE AUDIT

We performed the audit according to the planned scope previously communicated to you in the contract dated May 17, 2012 to allow sufficient time for our review and testing of the City's financial statements as a result of delays in management's preparation and delivery of the draft CAFR to us.

SIGNIFICANT AUDIT FINDINGS

Qualitative Aspects of Accounting Practices

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by the City are described in Note I to the financial statements. Throughout the course of an audit, we review changes, if any, to significant accounting policies or their application, and the initial selection and implementation of new policies. These policies have been consistently followed during the year. New standards adopted by the City during the year are also disclosed in Note I, and did not require any changes to the financial statements.

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:

- The depreciable lives and the net book value of the City's capital assets.
- The provision for discounts and allowances on the City's accounts and loans receivables.
- The accrued liabilities for the City's claims and judgments and risk financing activities.
- The accruals for City employee post-employment healthcare and retirement benefits.

Financial Statement Disclosures

The disclosures in the financial statements are consistent, clear and understandable. Certain financial statement disclosures are especially sensitive because of their significance to financial statement users. The most sensitive disclosures affecting the financial statements were:

- Note III.A disclosing the City's cash and investments including interest rate, credit, and custodial credit risks inherent in the City's investment portfolio.
- Note III.B disclosing the amount of discounts, allowances, and provision for uncollectible accounts at June 30, 2012.
- Note III.I disclosing changes to the City's long-term debt balances along with details of each debt outstanding and future repayment terms.
- Note IV. A through C disclosing details and accruals for the City's risk financing activities, claims, judgments, commitments, and contingent liabilities.
- Note IV. D and E disclosing on the details of employee post-employment health and retirement benefit programs. As of June 30, 2012, the actuarially determined unfunded liabilities for benefits earned totaled \$2.76 billion, not including the City's portion of the funded status of its involvement in the cost-sharing portion of Oregon PERS. This compares to the recorded liability of only \$1.2 billion.

Significant Difficulties Encountered in Performing the Audit

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management.

Uncorrected Misstatements. The following summarizes the impact of uncorrected misstatements in the fiscal year 2012 financial statements that were identified during the current year audit. Management has determined that the effects of uncorrected misstatements are immaterial, both individually and in the aggregate, to the financial statements taken as a whole.

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Capitalization of PBOT Streetcar Spare Parts Inventory - Approximately \$2.8 million of Streetcar Spare Parts inventory held by the City at June 30, 2011 and before, had been expensed in error and prior to their actual use in operations. The City addressed this by recording an adjustment to recognize the parts inventory as an asset, with an offsetting entry reducing the current year operating expenses, rather than restating prior year financial statement amounts. This adjustment effectively corrected the reporting of the unused parts as an asset as of June 30, 2012, but resulted in an understatement of current year operating expenses by \$2.8 million.

Capital Asset Additions - Certain Parks properties acquired from Multnomah County in 1994 totaling approximately \$2.6 million were expensed in 1994 in error. Management made an adjustment to correct the capital asset reporting by recording the acquisition as current year additions rather than restating prior year financial statements.

Grant Revenue Accrual - Due to a misunderstanding of how the accrual information was being reported from the accounting system, an understatement of grant revenues of approximately \$3.7 million occurred.

The uncorrected errors noted above, and the correcting entries made by management in the current year instead restating prior year financial statements, were determined by management to be immaterial, and we concur with management's assessment.

Major Issues Discussed With Management Prior to our Retention

There were no major issues, including the application of accounting principles, auditing standards or financial reporting, that were discussed with management in connection with our retention as the City's independent accountants.

Disagreements with Management

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

Management Representations

We requested and received certain representations from management that are included in the management representation letter dated December 21, 2012.

Management Consultation with Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the City's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

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Serious Difficulties Encountered in Performing the Audit

We did not encounter any serious difficulties in terms of disagreements with management on the application of accounting principles, responding to our inquiries, or in the facilitation of our audit procedures.

AUDITOR INDEPENDENCE

Auditor independence, in fact and appearance, is essential so that the public may justifiably perceive the audit process as an unbiased review of management's presentation of financial information.

At least annually, we will disclose to the City Council the nature of all relationships between Moss Adams and the City of Portland, Oregon, that, in our professional judgment, may reasonably be thought to bear on our independence.

We are not aware of any relationships between our Firm and the City of Portland, Oregon, for the year ended June 30, 2012, and through the date of this letter, that may reasonably be thought to impact our independence. Accordingly, relating to our audit of the financial statements of the City of Portland, Oregon, as of and for the year ended June 30, 2012, we confirm we are independent with respect to the City within the meaning of Rule 101 of the American Institute of Certified Public Accountants' Code of Professional Conduct, its interpretations and rulings.

This information is intended solely for the information and use of the City Council, City Auditor, management, and others within the organization, and is not intended to be and should not be used by anyone other than these specified parties.

Moss Adams, LLP

Eugene, Oregon
December 21, 2012