# Cook County, Illinois

Report to the County President, Board of Commissioners
and the Audit Committee

May 30, 2014

McGladrey

Assurance ▪ Tax ▪ Consulting

McGladrey LLP

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May 30, 2014

The Honorable Toni Preckwinkle, County Board President and
Members of the County Board of Commissioners, and
The Honorable John P. Daley, Chairman, Cook County Audit Committee
Cook County, Illinois
118 North Clark St. Room 1127
Chicago, IL 60602-1423

We are pleased to present this report related to our audit of the basic financial statements of Cook County, Illinois (the County) for the year ended November 30, 2013, and the audit of the Treasurer's Agency Funds A, B, and D. This report summarizes certain matters required by professional standards to be communicated to you in your oversight responsibility for Cook County's financial reporting process.

This report is intended solely for the information and use of the County Board President and County Board of Commissioners, the Audit Committee and management, and is not intended to be, and should not be used by anyone other than these specified parties. It will be our pleasure to respond to any questions you have about this report. We appreciate the opportunity to continue to be of service to Cook County, Illinois.

McGladrey LLP

## Contents

## Required Communications

Generally accepted auditing standards (AU-C 260, *The Auditor's Communication With Those Charged With Governance*) require the auditor to promote effective two-way communication between the auditor and those charged with governance. Consistent with this requirement, the following summarizes our responsibilities regarding the basic financial statement audit for the County overall and the Treasurer's Agency A, B, and D fund audits as well as observations arising from our audit that are significant and relevant to your responsibility to oversee the financial reporting process.

| Area | Comments |
|---|---|
| **Our Responsibilities With Regard to the Financial Statement Audit** | Our responsibilities under auditing standards generally accepted in the United States of America and *Government Auditing Standards* issued by the Comptroller General of the U.S. have been described to you in our arrangement letter dated January 4, 2014. |
| **Overview of the Planned Scope and Timing of the Financial Statement Audit** | We have issued a separate communication regarding the planned scope and timing of our audit and have discussed with you our identification of and planned audit response to significant risks of material misstatement. |
| **Accounting Policies and Practices** | **Preferability of Accounting Policies and Practices**<br>Under generally accepted accounting principles, in certain circumstances, management may select among alternative accounting practices. In our view, in such circumstances, management has selected the preferable accounting practice.<br><br>**Adoption of, or Change in, Accounting Policies**<br><br>Management has the ultimate responsibility for the appropriateness of the accounting policies used by the County. The County made a significant policy change during the fiscal year pertaining to the Forest Preserve District of Cook County (discretely presented) and the County Employees' and Officers' Annuity and Benefit Fund (Pension Trust and OPEB Trust funds). Through the year ended November 30, 2012, the County included the financial information for these entities for the period that ended in the month following the end of the County's fiscal year. As such, as of November 30, 2012, the financial statements included for these entities were for calendar years that ended on December 31, 2012, as permitted, but not required, under GASB Statement No 14.<br><br>Due to the difference in reporting periods between the County and these component units, coupled with new accounting and auditing standards and increased complexities within the component unit reports, it was increasingly difficult for the County to obtain final statements from these entities with sufficient time to incorporate into the County's Comprehensive Annual Financial Report that is completed within 180 days of fiscal year end. As a result, beginning with fiscal year 2013, the County has included the financial statements of the Forest Preserve District of Cook County (and the County Employees' and Officers' Annuity and Benefit Fund for the years ending December 31, 2012, as permitted under GASB Statement No 14. Availability of more recent financial statements for these entities is also communicated in the notes to the financial statements. |

| Area | Comments |
| --- | --- |
| | **Significant or Unusual Transactions**<br>We did not identify any significant or unusual transactions or significant accounting policies in controversial or emerging areas for which there is a lack of authoritative guidance or consensus.<br><br>**Management's Judgments and Accounting Estimates**<br>Summary information about the process used by management in formulating particularly sensitive accounting estimates and about our conclusions regarding the reasonableness of those estimates is in the attached Summary of Significant Accounting Estimates. |
| **Financial Statement Disclosures** | At your request, we will meet with you to discuss the following items as they relate to the neutrality, consistency, and clarity of the disclosures in the financial statements:<br>• Subsidies provided to CCHHS and how they are reported.<br>• Differing balances between employer contributions receivable reported by the Pension Fund, and amounts reported as owed by the County as the employer.<br>• The impact of implementing GASB Statements No. 67 and 68 (the Pension Standards), which are applicable in fiscal year 2015. |
| **Audit Adjustments** | Audit adjustments proposed by us and recorded by the County are shown in Exhibit B. |
| **Uncorrected Misstatements** | Uncorrected misstatements are summarized in the attached Management Representation Letter (Exhibit A). |
| **Disagreements With Management** | We encountered no disagreements with management over the application of significant accounting principles, the basis for management's judgments on any significant matters, the scope of the audit, or significant disclosures to be included in the financial statements. |
| **Consultations With Other Accountants** | We are not aware of any consultations management had with other accountants about accounting or auditing matters. |
| **Significant Issues Discussed With Management** | No significant issues arising from the audit were discussed with or the subject of correspondence with management. |
| **Significant Difficulties Encountered in Performing the Audit** | We did not encounter any significant difficulties in dealing with management during the audit. |
| **Letter Communicating Significant Deficiencies and Material Weaknesses in Internal Control Over Financial Reporting** | We have separately communicated the significant deficiencies and material weaknesses in internal control over financial reporting identified during our audit of the financial statements as required by *Government Auditing Standards*. All of our findings are in the Combined CAFR/ Single Audit reporting package and are included herein as Exhibit C. |
| **Certain Written Communications Between Management and Our Firm** | A copy of the signed Management Representation Letter is attached as Exhibit A. |

**Cook County, Illinois**
**Summary of Significant Accounting Estimates**
**Year Ended November 30, 2013**

Accounting estimates are an integral part of the preparation of financial statements and are based upon management's current judgment. The process used by management encompasses their knowledge and experience about past and current events and certain assumptions about future events. You may wish to monitor throughout the year the process used to determine and record these accounting estimates. The following describes the significant accounting estimates reflected in the County's November 30, 2013, basic financial statements.

| Estimate | Accounting Policy | Management's Estimation Process | Basis for Our Conclusions on Reasonableness of Estimate |
|---|---|---|---|
| Depreciation of capital assets | The County depreciates its capital assets over their estimated useful lives on the straight line basis. | The County has informed us they used all the relevant facts available to them to make the best judgment about depreciation method and estimate. The County establishes estimated useful lives of individual assets based on its expected life and use. | McGladrey reviewed the methodology which appears properly and consistently applied and the resulting estimate appears reasonable. |
| Investments | The County reports investments at their fair value. | The County obtains market value prices from Trustees and reviews for reasonableness. | We independently tested a sample of fair values and concluded amounts recorded by the County were appropriately adjusted to market. |
| Self-Insured Liabilities | The County records an estimate of the probable loss for worker's compensation, medical malpractice, liability and other claims. The accrued liability represents an estimate of the eventual loss on claims including claims incurred but not yet reported. | The County's risk management and legal departments provide details of open cases, reserve estimates, claims payment activity and other information to its actuary. This data is used by the actuary to determine the probable liabilities based on historical trends and other loss factor data. | We obtained the actuarial report directly from the actuary. We agreed source data provided to the actuary to the County's books and records. We had our actuary review the methods and assumptions used by the County's actuary. We concluded the liability was materially accurate. |

| Estimate | Accounting Policy | Management's Estimation Process | Basis for Our Conclusions on Reasonableness of Estimate |
|---|---|---|---|
| Pension Obligations and Other Post-Retirement Benefits | The County accounts for its defined benefit pension and OPEB plans (for its qualified employees) in accordance with GASB 27 and GASB 45. The annual pension /OPEB cost are calculated based on the actual contribution made in relation to the actuarially required contribution, as determined by the County's actuary. | Based on current economic conditions, management determines a discount rate, a long-term rate of return on plan assets and the compensation increase. They submit employee census data to the actuary with the underlying assumptions. From this, the actuary calculates the actuarially required contribution, net pension/OPEB obligations and other disclosed information. | We obtained a copy of the actuaries' reports, together with confirmation of their objectivity. We also obtained a copy of the employee census data provided to the actuaries. On a sample basis, we verified that the census data provided was accurate. We also compared headcount figures to the participant data used by the actuary for completeness. We had a firm actuary review the report, assumptions and methods used. We concluded the calculated amounts were materially accurate. |
| Property Tax Objections Liability | An estimate is accrued for probable tax refunds. The estimate is prepared based on historical trend data, by refund type, and by tax year. | Based on historic refund activity the County takes the average of 10 years of refund activity starting with the second prior year's levy (in FY13 that would be 2011) then the 9 consecutive following prior year activity. This method is applied to both "A or Z" refunds and "Specific Objection" refunds. "Illegal Rate" refunds involve the court system and can take several years to be settled. To estimate the future Illegal Rate refunds liability, the County takes the average of the past 10 years starting with the most recent year of known activity. The respective 10 year average is then used to determine each year's liability where the refunds have not been completed. Management reevaluates this estimation each year. | We reviewed the methodology used and the historical tax collection and refund activity and recalculated the estimate and found it to be reasonable. |

## Exhibit A—Certain Written Communications between Management and Our Firm

Bureau of Finance | Office of the Chief Financial Officer
**IVAN SAMSTEIN**
CHIEF FINANCIAL OFFICER
118 N. CLARK STREET ● Chicago, Illinois 60602 ● (312) 603-6846



May 30, 2014

McGladrey LLP
One South Wacker Drive
Chicago, IL 60006

This representation letter is provided in connection with your audit of the basic financial statements of Cook County, Illinois as of and for the year ended November 30, 2013 for the purpose of expressing an opinion on whether the financial statements are presented fairly, in all material respects in accordance with accounting principles generally accepted in the United States (U.S. GAAP).

We confirm, to the best of our knowledge and belief, as of May 30, 2014:
*Financial Statements*

1. We have fulfilled our responsibilities, as set out in the terms of the audit arrangement letter dated January 2, 2014, for the preparation and fair presentation of the financial statements referred to above in accordance with U.S. GAAP.

2. We acknowledge our responsibility for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

3. We acknowledge our responsibility for the design, implementation, and maintenance of internal control to prevent and detect fraud.

4. Significant assumptions used by us in making accounting estimates, including those measured at fair value, are reasonable and reflect our judgment based on our knowledge and experience about past and current events and our assumptions about conditions we expect to exist and courses of action we expect to take.

5. Related-party transactions, including those with fiduciary funds and component units for which Cook County is accountable, other organizations for which the nature and significance of their relationship with Cook County are such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete, and interfund transactions, including interfund accounts and advances receivable and payable, sale and purchase transactions, interfund transfers, long-term loans, leasing arrangements, and guarantees, have been recorded in accordance with the economic substance of the transaction and appropriately accounted for and disclosed in accordance with the requirements of U.S. GAAP.

6. All events subsequent to the date of the financial statements and for which U.S. GAAP requires adjustment or disclosure have been adjusted or disclosed.

7. The effects of all known actual or possible litigation and claims have been accounted for and disclosed in accordance with U.S. GAAP.

8. The following have been properly recorded and/or disclosed in the financial statements:
    a. Net positions and fund balance classifications.
    b. Line of credit or similar arrangements.
    c. The fair value of investments.
    d. Amounts of contractual obligations for construction and purchase of real property or equipment not included in the liabilities or encumbrances recorded on the books.
    e. Debt issue provisions.
    f. All leases and material amounts of rental obligations under long-term leases.
    g. All significant estimates and material concentrations known to management which are required to be disclosed.
    h. Authorized but unissued bonds and/or notes (subsequent event).
    i. Risk financing activities.
    j. Derivative financial instruments (pension fund).
    k. The effect on the financial statements of Statements No. 65, 66, 67, and 68 which have been issued, but which we have not yet adopted.
    l. Deposits and investment securities categories of risk.
    m. Liens or encumbrances on assets or revenues or any assets or revenues which were pledged as collateral for any liability or which were subordinated in any way.
    n. Pension obligations, post-retirement benefits other than pensions and union contract retroactive pay agreements attributable to employee services rendered through November 30, 2013.

9. Net positions (net investment in capital assets, restricted; and unrestricted) and fund balances are properly classified and, when applicable, approved.

10. Expenses or expenditures have been appropriately classified in or allocated to functions and programs in the statement of activities, and allocations have been made on a reasonable basis.

11. Revenues are appropriately classified in the statements of activities within program revenues and general revenues.

12. Capital assets, including infrastructure assets, are properly capitalized, reported, and depreciated.

13. We agree with the findings of specialists in evaluating the County's pension liabilities, OPEB liabilities and self-insured liabilities, and we have adequately disclosed the qualifications of the specialists in determining the amounts and disclosures used in the financial statements and underlying accounting records. We did not give or cause any instructions to be given to specialists with respect to the values or amounts derived in an attempt to bias their work, and we are not otherwise aware of any matters that have had an impact on the independence or objectivity of the specialists.

14. There are no unasserted claims or assessments that our lawyer has advised us are probable of assertion and must be disclosed in accordance with Statement of Financial Accounting Standards No.5 and/or GASB Statement No.10.
15. We have no direct or indirect, legal or moral obligation for any debt of any organization, public or private that is not disclosed in the financial statement.
16. We have complied with all aspects of contractual agreements that would have a material effect on the financial statements in the event of noncompliance.
17. To the best of our knowledge and belief we have informed you of all uncorrected misstatements as of and for the year ended November 30, 2013, management believes that the effects of the uncorrected misstatements aggregated by you and attached in Appendix A are immaterial, both individually and in the aggregate to the opinion units of the basic financial statements..For purposes of this representation, we consider items to be material, regardless of their size, if they involve the misstatement or omission of accounting information that, in light of surrounding circumstances, makes it probable that the judgment of a reasonable person relying on the information would be changed or influenced by the omission or misstatement.

*Information Provided*

18. We have provided you with:
    a. Access to all information, of which we are aware that is relevant to the preparation and fair presentation of the financial statements such as records, documentation, and other matters;
    b. Additional information that you have requested from us for the purpose of the audit;
    c. Unrestricted access to persons within the entity from whom you determined it necessary to obtain audit evidence.
    d. Minutes of the meetings of the County board and committees, or summaries of actions of recent meetings for which minutes have not yet been prepared.
19. All transactions have been recorded in the accounting records and are reflected in the financial statements.
20. We have disclosed to you the results of our assessment of risk that the financial statements may be materially misstated as a result of fraud.
21. We have no knowledge of allegations of fraud or suspected fraud, affecting the entity's financial statements involving:
    a. Management.
    b. Employees who have significant roles in the internal control.
    c. Others where the fraud could have a material effect on the financial statements.
22. We have no knowledge of any allegations of fraud or suspected fraud affecting the entity's financial statements received in communications from employees, former employees, analysts, regulators, or others.
23. We have disclosed to you all known instances of noncompliance or suspected noncompliance with laws and regulations whose effects were considered when preparing financial statements.
24. We have disclosed to you all known actual or possible litigation and claims whose effects should be considered when preparing the financial statements.

25. We have disclosed to you the identity of the entity's related parties and all the related-party relationships and transactions of which we are aware.
26. We have informed you of all significant deficiencies, including material weaknesses, in the design or operation of internal controls that could adversely affect the Entity's ability to record, process, summarize, and report financial data.
27. We are aware of no communications from regulatory agencies concerning noncompliance with, or deficiencies in, financial reporting practices.

*Supplementary Information*

28. With respect to supplementary information presented in relation to the financial statements as a whole:
    a. We acknowledge our responsibility for the presentation of such information.
    b. We believe such information, including its form and content, is fairly presented in accordance with accounting principles generally accepted in the United States of America.
    c. The methods of measurement have not changed from those used in the prior period. The presentation has changed to add additional budget detail to comply with the requirements of the GFOA Certificate Program.
29. With respect to required supplementary information presented as required by the Governmental Accounting Standards Board (GASB) to supplement the basic financial statements:
    a. We acknowledge our responsibility for the presentation of such required supplementary information.
    b. We believe such required supplementary information is measured and presented in accordance with guidelines prescribed by accounting principles generally accepted in the United States of America.
    c. The methods of measurement have not changed from those used in the prior period. The presentation has changed to add additional budget detail to comply with the requirements of the GFOA Certificate Program.
30. During the course of your audit, you may have accumulated records containing data that should be reflected in our books and records. All such data have been so reflected. Accordingly, copies of such records in your possession are no longer needed by us.

*Compliance Considerations*

In connection with your audit, conducted in accordance with *Government Auditing Standards*, we confirm:

31. We are responsible for:
    a. Compliance with the laws, regulations, and provisions of contracts and grant agreements applicable to the County.
    b. Establishing and maintaining effective internal control over financial reporting.
32. We have identified and disclosed to you:
    a. All laws, regulations, and provisions of contracts and grant agreements that have a direct and material effect on the determinations of financial statement amounts or other financial data significant to audit objectives.

b. Violations (and possible violations) of laws, regulations, and provisions of contracts and grant agreements whose effects should be considered for disclosure in the auditor's report on noncompliance.

33. We have taken timely and appropriate steps to remedy fraud, illegal acts, violations of provisions of contracts or grant agreements, or abuse that has been reported.

34. We have a process to track the status of audit findings and recommendations.

35. We have identified for you previous audits, attestation engagements, performance audits, or other studies related to the objectives of the audit being undertaken and the corrective action taken to address significant findings and recommendations.

36. We have provided you with our views on your reported findings, conclusions, and recommendations, as well as our planned corrective actions for the report.

37. Maria Mendoza, Director of Financial Reporting, who has sufficient skills, knowledge, and experience; has supervised, reviewed, and approved, and we take full responsibility for the financial statements and related notes and acknowledge the auditor's role in the preparation of this information.

Cook County, Illinois

Toni Preckwinkle

Toni Preckwinkle
President

Ivan Samstein
Chief Financial Officer

Lawrence L.

Lawrence L. Wilson
Comptroller

## Appendix A

**Summary of Uncorrected Misstatements**
**Opinion Unit: Governmental activities**

| | Effect - Debit (Credit) | | | | |
|---|---|---|---|---|---|
| Description | Assets | Liabilities | Net Position | Revenue | Expenses |
| Carryover impact from prior year uncorrected misstatements | $ - | $ - | $ - | $ 2,731,742 | $ 2,357,729 |
| Current year misstatements | | | | | |
| Non Title Use Tax - unearned revenue not deferred | - | (577,381) | 577,381 | 577,381 | - |
| Accrued liability understated | - | (4,817,657) | 4,817,657 | - | 4,817,657 |
| Home rule tax receivable understated - AJE not posted | 702,328 | - | (702,328) | (702,328) | - |
| Loans receivable overstated | (2,499,762) | - | 2,499,762 | - | 2,499,762 |
| Receivables overstated (not properly reversed from PY) | (1,935,223) | - | 1,935,223 | 1,935,223 | - |
| **Total Effect** | $ (3,732,657) | $ (5,395,038) | $ 9,127,695 | $ 4,542,018 | $ 9,675,148 |

**Opinion Unit: Business Type Activities and Enterprise Fund**

| | Effect - Debit (Credit) | | | | |
|---|---|---|---|---|---|
| Description | Assets | Liabilities | Net Position | Revenue | Expenses |
| Carryover impact from prior year uncorrected misstatements | $ - | $ - | $ - | $ 3,310,000 | $ - |
| Current year misstatements | | | | | |
| Accrued liability understated | - | (1,000,578) | 1,000,578 | - | 1,000,578 |
| Insurance receivable overstated | - | (2,112,012) | 2,112,012 | - | 2,112,012 |
| **Total Effect** | $ - | $ (3,112,590) | $ 3,112,590 | $ 3,310,000 | $ 3,112,590 |

**Opinion Unit: General Fund**

| | Effect - Debit (Credit) | | | | |
|---|---|---|---|---|---|
| Description | Assets | Liabilities | Net Position | Revenue | Expenses |
| Carryover impact from prior year uncorrected misstatements | $ - | $ - | $ - | $ 2,643,605 | $ (3,429,289) |
| Current year misstatements | | | | | |
| Non Title Use Tax - unearned revenue not deferred | - | (577,381) | 577,381 | 577,381 | - |
| Accrued liability understated | - | (4,817,657) | 4,817,657 | - | 4,817,657 |
| Home rule tax receivable understated - AJE not posted | 702,328 | - | (702,328) | (702,328) | - |
| Receivables overstated (not properly reversed from PY) | (1,935,223) | - | 1,935,223 | 1,935,223 | - |
| **Total Effect** | $ (1,232,895) | $ (5,395,038) | $ 6,627,933 | $ 4,453,881 | $ 1,388,368 |

**Opinion Unit: Debt Service Fund**

| | Effect - Debit (Credit) | | | | |
|---|---|---|---|---|---|
| Description | Assets | Liabilities | Net Position | Revenue | Expenses |
| Carryover impact from prior year uncorrected misstatements | $ - | $ - | $ - | $ (1,016,688) | $ - |
| Current year misstatements | | | | | |
| None | - | - | - | - | - |
| **Total Effect** | $ - | $ - | $ - | $ (1,016,688) | $ - |

**Opinion Unit: Capital Projects Fund**

| | Effect - Debit (Credit) | | | | |
|---|---|---|---|---|---|
| Description | Assets | Liabilities | Net Position | Revenue | Expenses |
| Carryover impact from prior year uncorrected misstatements | $ - | $ - | $ - | $ (232,324) | $ - |
| Current year misstatements | | | | | |
| None | - | - | | | - |
| **Total Effect** | $ - | $ - | $ - | $ (232,324) | $ - |

**Opinion Unit: Aggregate Nonmajor Funds**

| | Effect - Debit (Credit) | | | | |
|---|---|---|---|---|---|
| Description | Assets | Liabilities | Net Position | Revenue | Expenses |
| Carryover impact from prior year uncorrected misstatements | $ - | $ - | $ - | $ 4,164,174 | $ - |
| Current year misstatements | | | | | |
| Loans receivable overstated | (2,499,762) | - | 2,499,762 | - | 2,499,762 |
| **Total Effect** | $ (2,499,762) | $ - | $ 2,499,762 | $ 4,164,174 | $ 2,499,762 |

# Exhibit B—Recorded Audit Adjustments

**Cook County**
**Year End: November 30, 2013**

| Description | Debit | Credit |
|---|---|---|
| Cash - Cook County | | $ (402,456.80) |
| Outstanding warrants | $ 402,456.80 | |
| (Adjust for escheatment liability) | | |
| Cash - Cook County | | (1,153,413.70) |
| Due from others | 1,153,413.70 | |
| (Reclassify DIT to AR) | | |
| State Government | 225,610.00 | |
| Grants | 6,427,594.00 | |
| Federal Government | | (6,526,125.00) |
| Grants Rev - State | | (127,079.00) |
| (To make corrections to grant revenue/deferrals) | | |
| Property taxes | 2,500,649.96 | |
| Annuity and benefit allocation | | (2,500,649.96) |
| (Adjust the annuity and benefit property tax revenues) | | |

# Exhibit C—Material Weaknesses and Significant Deficiencies Letter

McGladrey

The Honorable Toni Preckwinkle, County Board President
and Members of the County Board of Commissioners
Cook County, Illinois

In planning and performing our audit of the financial statements of Cook County, Illinois (the “County”) as of and for the year ended November 30, 2013, in accordance with auditing standards generally accepted in the United States of America, we considered the County's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our 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.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as discussed below, we identified certain deficiencies in internal control that we consider to be material weaknesses and 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. 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. We consider the following deficiencies in the County’s internal control to be material weaknesses:

## I. MATERIAL WEAKNESSES:

### Finding 2013–01: *Financial Accounting and Reporting*

Cook County, Illinois (County) continues to have difficulties in the execution of the County’s financial accounting and external financial reporting process.

The County has made significant improvements in this area since last year and although the County was able to meet its May 31 reporting deadline, which is a significant accomplishment, the process continues to have major concerns due to the inadequacy of the County’s accounting software which is inadequate for a governmental entity the size of Cook County.

The current system does not properly accommodate accrual based accounting, requires a massive amount of manual entries, and is not integrated with all fee offices.

With regards to the financial reporting process, we noted the following additional issues:

- Certain special revenue funds that receive resources that are restricted to a special purpose do not have sufficiently detailed supporting information in each individual fund’s general ledger detail, supporting the expenditures. Certain Chief Judge Funds report significant expenditures that are “allocations” from the public safety fund. As such, there is not a sufficient audit trail to support that all expenditures are specific to an allowed purpose.

- Demand bond related footnotes were not complete in the draft financial statements. In the footnote for demand bonds, information on the terms of liquidity/takeout agreements was lacking.

- Certain payroll clearing balances (mostly liabilities) are not sufficiently reviewed at year. As such, there are liability accounts that are reporting balances established in prior fiscal years for which there is no support. These accounts should be reviewed annually and adjusted.

- Due to the manual nature of the County's year-end closing process and due to the fact that many records are not maintained on the Comptroller's general ledger system, numerous adjustments, including material adjustments, were prepared by the County ($140 million) after the initial trial balances were provided to the auditors.

- The County does not have a process to estimate and record probable liabilities for retro-pay under union contracts.

- Loans receivable under the HOME loan program are not properly reviewed for accuracy and valuation within the financial statements. Auditors detected a duplicate loan balance within the listing and an adjustment of $2.5 million was proposed to correct the financial statements. Additionally, principal collections on the loans are recorded as revenues instead of as a reduction of the loan receivable balance throughout the year. At year-end, the loan receivable balance is adjusted by making an entry to expenditures. This process causes revenues and expenditures to be overstated. Finally, the County does not have an adequate process for evaluating the allowance for loan losses. The current process is to review all loans with balances delinquent for over 120 days. Some of the balances are allowed for while other are not. The County should also consider historical collection rates and other facts and circumstances impacting the collectability of these types of loan balances.

- Prior year receivables were not properly reversed ($1.9 million).

- Property tax entries were not reconciled to the supporting documentation resulting in an adjustment to reduce property tax revenue in the Annuity and Benefit Fund ($2.5 million).

- Adjustments were made to reclassify amounts from cash to accounts receivable ($1.2 million) and to properly reflect escheatment liabilities ($400,000).

The accounting software used by the County should be capable of meeting reporting needs including the proper basis of accounting, budgetary and other controls, and an "adjusting period" to post, close and roll-up year-end entries. Software should minimize the need for manual entries and allow integration with other departments. Statements should be prepared in draft form with adequate time for the auditors and upper management to thoroughly review the statements and resolve any questions or concerns.

All expenditures charged to special revenue funds should be reviewed to ensure they are a legitimate charge against the restricted, committed and assigned resources as applicable.

Although the County has several individuals that are trained and highly qualified, the amount of work is immense and the hours required to meet reporting deadlines are excessive due to the system limitations. Lack of sufficient time to prepare, record and review entries and supporting files has led to adjustments that are missed, and documentation that is not accurate. Finally, the County's general ledger system is old and outdated. It is no longer sufficient to meet the reporting needs of the County.

Under the present system, the County will continue to struggle with its financial reporting requirements and is at great risk of missing future reporting deadlines. Errors and adjustments will continue to occur and misstatement of the financial statements will continue to be a huge concern for the County and the auditors.

and misstatement of the financial statements will continue to be a huge concern for the County and the auditors.

**Recommendation**

In order to improve the County's year end reporting process which includes improving the quality and timeliness for preparing the year end CAFR, we recommend the following:

- The County has begun the process to purchase and implement an ERP (Enterprise Resource Planning) system. The County needs to ensure its most technical accounting staff are involved in the product selection and implementation process so that this significant investment will enhance the year-end financial reporting process.

- Regardless of the software used (current system versus a new system) the County should begin recording all of its funds and accounts in its general ledger system, including Agency Funds maintained by the fee offices. Until an ERP system is established, the County should consider obtaining the necessary information quarterly, and recording it in the general ledger in at least summary form. This will significantly reduce the amount of work that is required to be performed at year-end. Additionally, this will ensure all funds get reviewed on a regular basis by those individuals responsible for the County's financial reporting at the entity-wide level.

- The County should not allocate expenditures from the Public Safety Fund to Special Revenue Funds. Due to the restricted nature of those funds, expenditures should be based on identified individual transactions recorded directly in the funds.

- The County should develop a new process for recording HOME loans including a comprehensive analysis of the collectability of the loans and proper financial reporting of annual loan activities such as collections of loan principal.

- The County should develop a bond note disclosure checklist to assist with the development of the footnote each year. The County has complex debt arrangements that require numerous disclosures and a checklist would be helpful for identifying the needed disclosures each year.

- The County should review all balance sheet account balances each year-end for accuracy and record any necessary adjustments.

- All liabilities pertaining to past employee service should be estimated and recorded in the financial statements.

**Management Response –**

Management agrees with the recommendations and will continue its strategic plan to implement process improvements that will ensure effective business systems exist when an ERP system is selected and implemented. During FY2013, the Comptroller's Office made significant improvements to its year-end reporting in the areas of bank reconciliations, investments, agency funds, accounts payable, grants and preparation of Prepared by Client (PBC) schedules.

- Communications to agency and fee offices were done on a regular basis and as a result, most agency and fee offices submitted their information by the requested date of January 31st. Therefore the agency schedules were prepared and provided to McGladrey earlier compared to the prior year.
- Bank reconciliations were prepared on a timely basis.
- The grant related PBC schedules did not need to be revised several times as in the past, due to a better review process.
- Additional procedures were performed to properly capture expenditure accruals.

- Investments were recorded at market value in the general ledger for the first time and the GASB 40 workpaper was properly reconciled to the general ledger.

Although significant improvements were made in the prior year, the Comptroller's Office recognizes that other areas still require improvements and is committed to take the necessary steps to achieve best practice processes that ensure the financial statements continue to be issued within six months.

The County is in the final steps of the procurement process to select an ERP software vendor. An ERP executive committee has been established as well as subject matter expert teams. The County is in the planning phase of issuing an RFP to select a vendor to implement the new ERP software.

The Comptroller's Office will provide a checklist to the individuals responsible for debt disclosures to ensure a complete and accurate disclosure is included in the draft provided to McGladrey.

The Comptroller's Office will review balance sheet account balances to determine accurate balances and write-off balances if necessary. An analysis of fund 2040 Payroll will also be performed to adjust/write-off old balances.

The County has recently contracted Amerinational Community Services, Inc. to service the Home Program loans and issue fiscal year-end financial reports on annual loan activities, including the collections of loan principal and interest. The financial reporting by Amerinational Community Services will allow management to do a better evaluation for loan losses.

**Finding 2013-02: *Workers' Compensation and Other Claims***

Cook County did not accurately track, coordinate, and report a portion of litigated claims related to workers' compensation.

The County's actuary was advised by the County in December 2013 that a portion of litigated workers' compensation claims were closed in the Risk Management Department (RM) and administratively reassigned to the State's Attorney's Office (SAO). This reassignment process began in May 2011. The potential value, or case reserve, of the reassigned claims was not accurately tracked by the County and thus not accurately reported to and included in the actuary's analyses as of November 30, 2011 and 2012. The 2013 actuarial analysis included the potential value of all open workers' compensation claims. These claims, net of duplicate amounts (see below) increased the actuarially calculated liability by approximately $17 million.

Because the information regarding potential liability reported to the actuary was found to be incomplete, the actuary used a different generally accepted valuation model based on developed paid claims.

Below is additional detail on the issues noted:

**Workers' Compensation Claims**

- The potential value of claims established as of November 30, 2013 by Risk Management was incomplete due to the understatement of settlement valuations for certain litigated claims. The discrepancy arose because 1) SAO included certain claims not provided to RM; 2) SAO report included settlement valuations totaling $22.2 million; however, the RM system only included $5.7 million of those reserves. The actuary made an allowance for all claim reserves, including SAO, as part of the final FY13 analysis.

The duplicates and omissions occurred due to a lack of internal departmental communication over the tracking and reporting of claims.

**Non-Worker's Compensation (Non-WC) Claims**

- Reserves outlined in the SAO reports as of April 2014 were $10.4 million greater than the corresponding RM reserve records as of November 30, 2013 for the same litigated claims.

Tracking and reporting the potential value of claims is a complex process. The Risk Management Department and State's Attorney's Office should meet on a regular basis to reconcile known claims and reserve amounts, and develop claims management strategy. This reconciliation would improve the claim tracking and reporting process and minimize the possibility of duplicate claimants, inappropriate reserves and missing claims. The Risk Management Department and the State's Attorney's Office should have a congruent understanding of the County's exposure for claims. The State's Attorney's Office should provide timely notice to Risk Management regarding any litigated activity related to workers compensation claims.

Due to the omission of workers' compensation claims transferred to the SAO, the actuary was required to perform additional work to determine the impact they had on the actuarial valuation.

**Recommendation**

We recommend that the County revise its policies and procedures for tracking claims and setting the potential value of each claim. These procedures should include:

- A schedule which outlines how frequently Risk Management and the State's Attorney's Office meet to annually reconcile all known claims and reserve amounts, and develop claim management strategy.
- Development of a uniform protocol for establishing and adjusting reserve amounts consistent with industry standards.
- Utilization of the same fields (for example Name, Date of Loss, Illinois Workers' Compensation Claim # if applicable, and County Risk Management claim #) for identifying and tracking claims.

**Management Response –**

Management accepts the recommendations.

Upon Risk Management's discovery that there was an inconsistency between the Risk Management claims system and the SAO tracking of workers compensation claims and other claims, RM adopted a corrective action plan to ensure accurate reporting of estimated claims liabilities that includes:

1. Hiring an experienced Workers' Compensation Manager to its team of five professional workers compensation staff and requiring on-going continuing professional education. Complete as of 11/30/2013.
2. Ceasing the previous practice of "closing" claims that are reassigned to the SAO. Complete as of 11/30/2013.
3. Issuing the Workers' Compensation policies and procedures manual that includes management control over related adjuster functions including the justification of set reserves. Complete as of 11/30/2013.
4. Conducting a comprehensive and systematic review of all cases, including determination of case status (open or closed), establishment of appropriate indemnity and medical reserves, and assignment of a Risk Management adjustor to monitor and manage cases with the SAO. On-going.
5. Incorporating SAO information into RM's David system by conducting periodic file review sessions with the SAO to review outstanding claims. On-going.

## II. SIGNIFICANT DEFICIENCIES:

### Finding 2013-03: *Accounting for Capital Assets*

The County does not have sufficient controls over capital asset accounting and inventory tracking.

The schedule supporting the capital asset required disclosures (beginning balances, additions, deletions and ending balances) was revised several times by County personnel after first being provided to the auditors. The final changes were not provided until May 8, 2014. Also, the capital asset detailed listing was missing required asset identification information for most of our sample items. The missing and/or incorrect information included the asset #, vendor name, serial #'s, asset descriptions, correct locations, etc.

During our audit we found:

- Deletions totaling $11 million were omitted from the initial schedules.
- Of the 20 inventory items selected from the fixed asset listing, 4 of the assets could not be located because the listing was missing unique identifiers making it impossible to identify the specific asset.
- Of the 20 inventory items selected from the floor, 8 assets could not be traced into the capital asset listing as the asset's unique identifiers were not captured on the capital asset listing at inception.
- Detailed records continue to be maintained in excel which is prone to error.

Good internal controls over the custody of capital assets should include assets recorded at the proper historical cost and depreciated using the proper useful life. Construction in process should be recorded in the year that the work is performed. When an asset is tagged for disposal, it should be removed from service and properly disposed. Assets should be recorded as disposals in the year that they are disposed. Supporting documentation for every disposal should be maintained. Each asset should be recorded individually. The capital asset listings should be updated with each new asset purchase.

The County's process for recording additions and deletions, as well as depreciating capital assets are highly manual and rely on multiple departments and individuals.

Over and understatement of capital assets, construction in process, depreciation expense, and accumulated depreciation as well as incorrect gain/loss calculations on sale/disposal transactions occurred and will continue to occur under the present system.

**Recommendation**

Although the County has significantly improved the capital asset records over the past few years, we continue to recommend that the County continue efforts to maintain accurate capital asset records. This includes recording capital asset additions and deletions monthly, reconciling additions to the capital outlay expenditure accounts monthly, updating capital asset descriptions in the system and implementing an automated system. Additionally, we believe the County should conduct a physical inventory of its capital assets. This process could be done one department at a time to better manage the process. Additionally, the County could use interns or other available employees as appropriate.

**Management Response –**

- Management agrees that some of the capital assets did not include the required information such as ID tag, location, serial number, quantity and unit value. To address this issue, the Comptroller's Office will send annual notifications to all County departments requesting that asset custodians perform an inventory of existing fixed assets and update their fixed assets listing to include the required information. In addition, the Comptroller's Office will work with at least five departments to ensure that all assets included in the listing contain all required information and can be physically identified.

- Management concurs that $11 million of asset disposals were not included in the initial roll-forward schedules provided to McGladrey. To address this issue, the Comptroller's Office will send notifications on a quarterly basis beginning July 2014, to all County Departments requesting that the departments report all disposals or transfers. Departments will need to submit all FY14 disposals by January 2015. The Comptroller's Office will follow up with non-compliant departments on a biweekly basis. In addition, the importance of reporting capital assets, including department disposals will be presented at the quarterly CFO round table meetings.

- To address the issues with internal control, cost analysis and depreciation calculations, the Comptroller's Office will continue its efforts to utilize the JD Edwards (JDE) fixed asset module. The system will compile cost data, description and serial numbers while tracking the locations of its capital asset inventory. The Comptroller's Office will also be the custodian department in charge of data integrity and maintenance. To ensure improvement of internal controls, assets will be manually created in the fixed asset module by the Comptroller's Office. The asset custodian for each department(s) will identify their new assets based on a quarterly expenditure transaction report. JDE depreciation reports will be processed and audited on an annual basis. The Comptroller's Office will continue to work with BOT to achieve its goal of tracking capital assets in the JDE fixed assets module.

- The JDE fixed asset module has system limitations and will serve as a repository for capital asset inventory records until a new ERP system is implemented. The future ERP system should incorporate an inventory and capital asset module to control financial reporting and inventory tracking.

- The County is in the final steps of the procurement process to select an ERP vendor. An ERP executive committee has been established as well as subject matter expert teams. The County is in the planning phase of issuing an RFP to select a vendor to implement the new ERP software.

**Finding 2013-04: *Grant Accounting***

The County does not adequately account for individual grants in accordance with GASB Statement No. 33. Instead, grants are analyzed in groups to estimate receivables and deferred amounts.

During our testing of grant transactions we noted the following:

- There is no documentation of a detailed analysis of individual grant agreements to support the proper classification of each grant as an expenditure driven grant, a grant with eligibility requirements, etc., all of which drive the proper accounting treatment.

- Program income is not separated from grant revenue for purposes of determining year-end receivable (deferred) balances.

- Revenues and expenditures are not always aligned into the proper business reporting unit or fund. This results in an overstatement of accounts receivable and deferred revenue.

- Our testing detected 14 errors and resulted in adjustments of approximately $6.5 million to the financial statements.

Under a good system of internal control for grants, a system should be in place to assess all significant grants, determine the appropriate accounting relating thereto, accurately track grant receipts and disbursements during the fiscal year, as well as throughout the life of the individual grant, and calculate and report grant receivables, revenue and deferred revenue, net of an allowance for uncollectable amounts.

The County has over 100 grants each year that it has to monitor and account for. The present system available to the County is not sophisticated enough for a grant program of the magnitude administered by the County. Additionally, those in charge of monitoring grant performance and reporting back to the funding sources are not the same individuals responsible for reporting grants in accordance with GAAP within the financial statements.

Insufficient reporting of grant transactions can result in forfeiture of funding or possible recoupment of grant funds already awarded. Additionally, the level of manual analysis of the grants could lead to financial statement misstatements of grant receivables, revenue, and deferred revenue.

**Recommendation**

We recommend the County continue to improve its grant reporting procedures to addresses year-end financial reporting needs as well as reporting requirements imposed by funding agencies. The County should enlist the individual grant administrators from throughout the County to assist in this process. These individuals are the most familiar with the individual grant program requirements and are best positioned to help the Comptroller's office identify the key grant requirements/attributes that impact GAAP basis accounting. At a minimum, the County should segregate the most significant grants for separate analysis. For these larger grants, the agreement should be analyzed to determine the grant type and the proper accounting treatment. Because the County has been receiving large grant advance payments under various programs, the County can no longer assume that all grants are reimbursement based grants.

As the County works towards selecting an ERP system, a detailed assessment of the grant reporting features of each prospective system should be a major consideration in the award process.

**Management Response –**

The County receives an average of 100 grants on an annual basis. The County has implemented reforms and continues to review best practices to help ensure that each grant receives proper review to allow for proper classification, budgeting, and expenditure of grant funds. In FY 2013, the Department of Budget and Management Services (DBMS) and Comptroller's Office, in collaboration with other central service and grant-funded departments, developed a Grants Manual to outline grant regulations, policies, procedures, eligible costs, reimbursement requests and deposits, closeout instructions, and other necessary information required to effectively manage grants throughout the entire lifecycle of a grant. The Grants Manual, supported with quarterly workshops, provides training and instruction on administrative, programmatic, and fiscal responsibilities regarding the management of federal, state, and private grants. In addition, each department is required to submit standard forms to the DBMS to assist in the review and establishment of all grant budgets in the County's financial system. The documentation required includes:

- A-133 Single Audit Questionnaire: Provides a summary of the grant period, funding agency details, funding agency type and pass thru entity, CFDA number (as necessary), schedule of reimbursement (advance or reimbursable), grant reporting schedule, in addition to other relative information.
- Application/Award Checklist: Provides a summary of information relating to the application or award including grant period, grant description, budget by category, number of personnel, Federal Funding Accounting & Transparency Act (FFATA) requirements, performance planned deliverables, certifications, matching requirements, indirect cost and justification, in addition to other relative information.
- Grant Agreement with detailed budget: Provides instruction into the execution and management of the grant including any special conditions, regulatory requirements, reporting requirements, and approved budget details.

- Budget Setup form: Provides detailed information regarding the approved budget by cost code and object account. This form may also include details into the personnel budget and associated personnel in alignment with the grantor approved budget.

In addition to the required documents and review of relevant information, DBMS monitors each department's grant performance by conducting a monthly spending analysis of each grant to review grant budget, expenses, and revenues. DBMS submits the grant performance analysis to each department for review and to provide justification or a corrective action to ensure that grant funds are properly expending funds; action is taken on a case by case basis. The Comptroller's Office will request that departments perform a reconciliation of the expenditures on the general ledger to the grant reports submitted to their grantors on a quarterly basis.

The County also implemented a SharePoint site in FY 2014 to facilitate the management of grants. The SharePoint site provides access into all required grant information and forms, allowing users to review and share information more effectively. The SharePoint site is being enhanced to allow for a more robust workflow, alert, and notification process capable of tracking grant reporting dates and other requirements and schedules, which is expected to be implemented in FY 2015.

In addition, the County is in the final steps of the procurement process to select an ERP software vendor. An ERP executive committee has been established as well as subject matter expert teams. The County is in the planning phase of issuing and RFP to select a vendor to implement the new ERP software. The County will work with the vendor and the spending departments to ensure the system can support grant reporting requirements.

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This communication is intended solely for the information and use of the County Board, the members of the audit Committee, management and others within the organization, and Federal and State granting agencies and is not intended to be and should not be used by anyone other than these specified parties.

McGladrey LLP

Chicago, Illinois
May 30, 2014