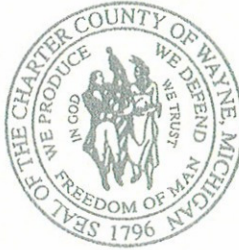


Office of Legislative  
**Auditor General**

**WILLIE MAYO, CPA, CIA, CICA**  
AUDITOR GENERAL



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April 5, 2012

**FINAL REPORT TRANSMITTAL LETTER**

Honorable Wayne County Commissioners:

Enclosed is our final copy of the Auditor General's Analysis of Cash Flow Projections prepared by the Department of Management and Budget. Our report is dated February 29, 2012; DAP No. 2012-57-001. The contents of this report did not change from the draft report previously issued. The report was accepted by the Audit Committee at its meeting held on March 27, 2012 and formally received by the Wayne County Commission on April 5, 2012.

You will be pleased to know that officials and staff in the Department of Management & Budget offered their full and complete cooperation during the review. If you have any questions, concerns, or desire to discuss the report in greater detail, we would be happy to do so at your convenience. This report is intended for your information and should not be used for any other purposes. Copies of all Office of Legislative Auditor General's final reports can be found on our website: <http://www.waynecounty.com/commission/lagreports.htm>

  
Willie Mayo, CPA, CIA, CGAP, CICA  
Auditor General

**REPORT DISTRIBUTION**

**Department of Management & Budget**

Carla E. Sledge, Chief Financial Officer  
Stacie Durant, Deputy Chief Financial Officer  
Lyn Roberts, Director, Financial Reporting  
Terry L. Hasse, Director, Grants Compliance and Contract Management

**Office of the Wayne County Treasurer**

Honorable Raymond J. Wojtowicz, County Treasurer

**Wayne County Executive**





**WAYNE COUNTY OFFICE OF LEGISLATIVE  
AUDITOR GENERAL**

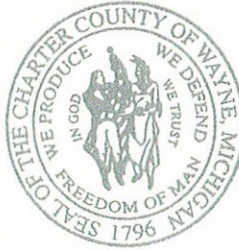
**Auditor General Analysis  
of Cash Flow Projections  
Prepared by the Department of  
Management & Budget**

**February 29, 2012**

**DAP 2012-57-001**

Office of Legislative  
**Auditor General**

**WILLIE MAYO, CPA, CIA, CICA**  
AUDITOR GENERAL



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February 29, 2012

DAP No. 2012-57-001

Honorable Ilona Varga  
Chairwoman, Audit Committee  
Wayne County Commission  
County of Wayne  
500 Griswold Street, 7<sup>th</sup> Floor  
Detroit, MI 48226

Re: Auditor General's Analysis of Cash Flow Projections

Chairwoman Varga:

**Engagement objective, scope, and methodology**

This is an analytical review engagement performed under Generally Accepted Government Auditing Standards (GAGAS) - Attestation standards. It is being prepared to adhere to the Wayne County Charter provisions and ordinances related to financial solvency and perceived risk. The purpose of this engagement is to provide constructive criticism and add value.

The objective of this engagement is to evaluate how county leadership is identifying, analyzing, monitoring, and addressing cash projection needs and risks of borrowing to pay general fund operating expenses.

The scope of this engagement is classified as a special report and is limited to an analytical analysis of the cash flow projections of general pooled cash prepared by the Department of Management & Budget (M&B) dated December 2011, and provided to the Office of the Auditor General (OAG) on February 20, 2012. This is the latest cash flow projection issued by M&B as of the date of our report. (See Appendix A Schedule of Cash Flows – General Pooled Cash).

The methodology used for this engagement included observations, inquiries and discussions with M&B officials, as well as analyses of financial data and review of other supporting documents to validate certain statements and conclusions reached in this report.





## **Background**

The cash flow projections prepared by M&B for December 2011 anticipates borrowing \$100 million in a short-term note on or about March 27, 2012. Based on the December 2011 cash projections, this will place the general fund pooled cash at more than \$123 million in deficit spending by the end of February 2012.

The commissioners were informed by the administration that the borrowing was necessary to avoid not being able to meet payroll and pay other obligations. Based on our review of the cash flow projections for the month of December 2011, we concur with that assessment made by M&B.

## **Auditor General Analysis**

### **Tax Anticipation Notes (TAN)**

Under the state statute, the county can issue tax anticipation notes (TAN) for the purpose of providing a mechanism to manage periodic cash flow shortfalls that occur throughout the year. As a result of the most recent borrowing approved by the commission, the county will now have spent more than \$8 million related to short-term borrowing.

According to the CFO, the interest rate for the TAN issued in December 2010 should be 3.50% and not the 4.00% as previously stated. The OAG has made this correction to the report. The CFO also stated Tax Anticipation Notes have become necessary to meet the county's cash needs and is an inexpensive method of financing short term cash shortfalls. The bulk of the county's revenue is received in the months of August through November while expenditures are made almost daily. See Appendix B for the CFO's full response to this concern.

### **Cash Flow Projections – General Pooled Cash**

In the cash flow projections, total general pooled cash balances as of February 2012 is projected at \$109 million and the general fund pooled cash is projecting a negative cash position of \$123 million. In a report to management and the audit committee in 2010, the external auditors expressed a concern regarding the use of restricted cash to pay general operating fund obligations. The implementation of GASB 54, effective June 15, 2010, will also help the county better clarify funds that are restricted for general purpose and use.

The county CFO responded that there has never been an instance where special revenue programs were impaired or delayed. Also, the CFO believes that the development of a county pooled cash policy is critical. See Appendix B for the CFO's full response to this concern.

### **Monthly Cash Needs**

Based on our review of the cash flow projections it appears that the general fund needs approximately \$54.8 million to meet its monthly cash requirements which approximates



\$658 million annually. Conversely, the cash inflows are approximately \$49.6 million on a monthly basis and \$596 million annually.

Consequently, cash outlays are exceeding expenditures by approximately \$5.2 million on a monthly basis and \$62.4 million annually. Needless to say, unless strategies are implemented to reduce the structural deficits the general fund will continue to accumulate deficits of \$60 million or more on an annual basis.

On the other hand, exploring methods to minimize the cash requirement outlay by \$10 million per month could minimize the necessity for short-term borrowing and generate an operating surplus of \$60 million annually.

### **Property Tax Revenues**

Property tax revenues have decreased by more than \$154 million over the last six years and the county has yet to convey a comprehensive county-wide strategic plan to reduce short-term borrowing and eliminate deficit spending. The \$154 million decrease in property tax revenue represents close to a 30% reduction in general fund revenue.

The CFO stated this concern was being addressed in the county's long term financial planning implemented by the administration a couple of years ago but the project lost momentum in 2011. See Appendix B for the CFO's full response to this concern.

### **Overstating Revenue Projections**

We found instances where the Food Safety and Jail Medical programs revenue budgeted in the general fund were overstated for fiscal years 2010 and 2011 by as much as \$7.5 million over the two year period. In a previous report, we also found instances in which overstating budgeted revenue resulted in allowing expenditures to be incurred in excess of funds available to pay for them. Needless to say, expenditures made in excess of revenue collections leads to deficit spending.

The CFO agrees with the Auditor General that revenue projections for both the Food Safety and Jail Medical programs appear to be overestimated. According to the CFO, once it becomes clear that certain revenues are not going to be achieved, the revenues should be decertified and corresponding expenses should not be allowed. The CFO intends to put together a forecasting team to start to address these issues. See Appendix B for the CFO's full response to this concern.

### **Decrease in Accumulative Deficits**

All is not gloom, based on a preliminary review of the most recent audited financial statements, the general fund generated an operating surplus of \$9 million for the FY 2011, and the county-wide cumulative fund balance deficits have decreased by \$55 million bringing the total deficits down to \$198 million. This is very encouraging and an indication that some cost saving measures employed by the CEO and Commission are working. The OAG is performing a separate engagement on the analysis of the fund deficits.



According to the Wayne County Enrolled Ordinance 2010-515: “a department or office with a projected deficit shall develop and submit a deficit elimination plan, in line-item form, to the Commission and the CEO within seven (7) business days of receipt of written notice from M&B.”

However, the CFO informed us that there is an annual deficit of \$45 million expected for the general fund for the FY 2012. We contacted the budget director and he stated that at the end of the first quarter of each year, departments with operating deficits are required, within 10 days after the end of the quarter, to submit a deficit elimination plan to M&B. See Appendix B for the CFO’s full response to this concern.

### **Assessment of Capital Projects – Cash Outlay**

Over the last three fiscal years, the county has issued bonds to fund such projects as the purchase of the Guardian Building, infrastructure improvement for the Pinnacle Race Track, and most recently, the construction of a new jail facility. For a grand total of \$277 million in additional debt issued since 2008. It is costing the county \$16.5 million per year to service these new debts over the next thirty years.

### **Erosion of Institutional Knowledge**

Within the last two years, M&B and the CEO have lost two financial reporting directors, a budget director, two personnel directors, Chief Information Officer, and the Deputy CEO, as well as a host of other key personnel in key administrative positions. The loss of such human resource talent appears to have negatively impacted the county’s ability to timely complete cash flow projections, revenue and expenses reports related to the Guardian Building, and the annual CAFR. Although the incoming key personnel appear to be quite competent and capable, it will still take time to regain the institutional knowledge that has been lost.

The CFO stated, although it is in its infant stage, the personnel department is working on a county-wide succession plan that is to outline strategies to address key personnel turnovers. Phase I of this plan is anticipated to be completed by June 2012.

### **New Commission Ordinances**

Adding standard language into new ordinances would establish the criteria for management to develop appropriate business processes to fulfill the goals and objectives of a particular ordinance. In addition, the development of policies and procedures by management provides for uniformity and consistency in carrying out a particular ordinance.

The suggested language that can be included in new ordinances, when warranted, could read: “The chief executive officer or his or her designee shall prepare and implement policies and procedures to provide for concurrence, uniformity and consistency in the application of this ordinance as well as establish criteria for the existence and effectiveness of a defined process.”



The CFO does not object to the auditor general's belief that including standardized language to certain ordinances adds value.

### **CFO Authority**

The CFO is granted authority under Section 5.143 of the Wayne County Charter to only allow expenditures that are appropriated in the budget and it further states that expenditures made in excess of the amount appropriated is a violation of this section and is void.

The CFO stated some of the obstacles in carrying out this mandate have been because of the proliferation of lawsuits filed by county elected officials to restrict the administration's efforts to reduce deficit spending. See Appendix B for the CFO's full response to this concern.

### **Suggested Action**

- ❖ M&B should closely monitor and accelerate the collection of general fund cash in order to maximize general pooled cash balances on a monthly basis.
- ❖ M&B should review monthly revenue and expenditure projections county-wide to make sure they are on target to equal the revenue and expenditures appropriated in the budget. A significant portion of their effort should concentrate on actual revenue collections because it drives expenditures.
- ❖ There is an urgent need for management to address the general fund structural deficits in the general fund and explore ways to at least reduce the cash requirement outlay by \$5 million a monthly basis.
- ❖ The commission needs to enforce Enrolled Ordinance No. 2010-515, which requires departments that are incurring deficits to develop and timely submit a DEP to M&B and the Commission for acceptance and approval.
- ❖ The CEO and Commissioners could develop a joint crisis management team composed of Commissioners, CFO, representatives from the Treasurer, PAO, Sheriff, Clerk, and Courts for the purpose of analyzing and monitoring the cash flow projections and deficits over the next two – five years and continue to make suggestions as needed to eradicate deficit spending.
- ❖ The commission could request the CEO to provide an assessment of all planned and proposed capital projects borrowing against the cash outlay that will be required by the general fund to service the debt.
- ❖ The CEO could develop a viable succession and recruiting plan for key employees that are expected to leave the county and provide it to the commission for acceptance. The CFO stated the personnel department is currently working on a succession plan that is to be implemented county-wide.
- ❖ Finally, the CFO and CEO must exercise the authority granted to them in the

charter and disallow all expenditures that are not included in the appropriated budget adopted by the commission.

Since this is a review engagement intended to add value, the OAG will not be requesting a corrective action plan for this engagement.

### **Views from Responsible Officials**

The CFO provided a detail response to the comments and observations being raised in this report and in some instances provided a plan of action going forward. We found the CFO responses to be very positive, encouraging and forward thinking. For a detail narrative of her responses see - Appendix B - Views from Responsible Officials.

### **Conclusion**

According to M&B, the county is in a cash position, where if they did not request the short-term borrowing, they would not be able to make payroll and pay its vendors. Because of this tenuous position, the administration and the commissioners have no alternative but to seek short-term borrowing.

It is good that the deficits are decreasing and cash projections are being performed and it affords the county the opportunity to forecast ahead, as well as develop strategies to limiting the amount of borrowing in the future.

If the county is successful in tackling the causes of the cash flow problems, it will lead to adopting an achievable DEP in eliminating the county-wide deficits that are currently reported at \$198 million as of September 30, 2011.

Finally, we believe a succession plan for the turnover in managerial personnel is one of the keys to the county's future survival. In addition, unless the commissioners require policies and procedures to be established for critical ordinances being adopted, it could fail to assist management in meeting the goals and objectives desired by the commissioners.

We have generally concluded that county leadership is identifying and monitoring the cash projection needs of the county. This became evident by the preparation of cash flow projections on a monthly basis and through submission to the committee on Ways and Means.

However, we believe more can be done by the administration and commission to alleviate the necessity of borrowing restricted funds to pay general fund operating expenses. This practice is precariously risky and could lead to violations being imposed by certain regulatory agencies.



## **Detail Report**

## **Purpose**

This special report is being prepared to adhere to the Wayne County Charter provisions and ordinances that require the Auditor General to perform engagements under Generally Accepted Government Auditing Standards (GAGAS) as it relates to the financial solvency and the perceived risks and challenges Wayne County could be facing.

The purpose of this engagement is to provide constructive criticism and add value.

## **Objective**

The objective of this engagement is to evaluate how county leadership is identifying, analyzing, monitoring, and addressing cash projection needs and the risks of borrowing to pay general fund operating expenses.

## **Scope**

The scope of this engagement is classified as a special report and is limited to an in-depth analysis of the cash flow projections of general pooled cash prepared by Management & Budget (M&B) as of December 2011. This is the latest cash flow projection issued by M&B as of February 20, 2012. (See Appendix A Schedule of Cash Flows – General Pooled Cash).

This engagement is classified as a review under GAGAS - Attestation engagements. The work was primarily performed in the Wayne County Legislative Auditor General's Office (OAG) and was substantially completed on or about February 20, 2012.

## **Methodology**

The methodology used for this engagement is based on observations, inquiries and discussions with M&B officials, as well as a review of financial data and other supporting documents to validate certain statements and conclusions reached in this report.

## **Background**

The cash flow analyses prepared on a monthly basis and submitted to the Committee on Ways and Means, serves as an excellent planning tool for the administration and the commission to assist them in making assessments and determinations as to the short-term cash needs of county operations.

More specifically, the cash flow projections prepared by M&B for December 2011 anticipates borrowing \$100 million in short-term note proceeds on or about March 27, 2012. Based on the December 2011 cash flow projections, this will place the general fund pooled cash at more than \$123 million in deficit spending by the end of February 2012.

The commissioners were informed by the administration that the borrowing was necessary to avoid not being able to meet payroll and pay obligations. Based on our



review of the cash flow projections for the month of December 2011, we concur with that assessment made by M&B.

This is the third consecutive year that the county has had to borrow \$100 million to avoid not being able to pay its employees and vendors.

State of Michigan Public Act No. 34 of 2001, allows a county, by commission resolution, to issue short-term municipal securities in anticipation of property taxes to be collected by the county for its current fiscal year or the taxes for its next succeeding year to cover operating expenses.

The State of Michigan Act, among other things, limits the amount of the borrowing not to exceed 50% of the tax levy made for operating expenditures, and the note is payable at the time that collections are sufficient to repay the loan.

## **Auditor General Analysis**

### **Tax Anticipation Notes (TAN)**

Under the state statute, the county can issue tax anticipation notes (TAN) for the purpose of providing a mechanism to manage periodic cash flow shortfalls that occur throughout the year. Listed below are dates and costs of Wayne County's TAN borrowing over the past four years:

Schedule of Short-Term Borrowing			
Date	Amount	Interest (%)	Total Borrowing Cost
August 2009	\$60 million	3.00	\$ 664,045
January 2010	\$100 million	3.75	2,908,876
December 2010	\$100 million	3.50	2,938,154
March 2012	\$100 million	4.00	1,767,278 Est.
<b>Total TAN Borrowing Cost</b>			<b>\$ 8,278,353</b>

As illustrated in the above schedule - we estimate it will cost the county more than \$8.2 million in borrowing costs for the period – August 2009 thru November 2012.

We also observed that it is becoming more expensive to borrow because the annual interest rate on the short-term borrowing will increase in March 2012 from 3.50% to 4.00%.

### **Cash Flow Projections – General Pooled Cash**

General pooled cash is where management, with the assistance of the county treasurer, engages in the practice of consolidating all county-wide cash into one large interest bearing account in order to maximize the collection of interest income. The pooled cash account consists of monies belonging to the General Fund, Roads, Mental Health, Health



and Human Services, Juvenile Justice, and others. The tracking of the transactions and balances in these funds are accounted for by recordings in ledger accounts.

In the cash flow projections, total general pooled cash balances as of February 2012 are projected at \$109 million and the general fund pooled cash is projecting a negative cash position of \$123 million.

In other words, the general fund is projecting to use funds from other governmental funds, including special revenue funds, such as Roads, Mental Health, Health and Human Services, Juvenile Justice and others that are restricted in their use, in the amount of \$123 million.

According to GASB 54, "special revenue funds may only be established around one or more revenue sources that are restricted or committed to purposes other than capital projects or debt service."

Aside from being prohibited, it is beyond the scope of this engagement to determine the impact, if any, of the use of these funds to pay general fund obligations and impact on these restricted funds in carrying out their program goals and objectives.

Recently, we have been informed through the news media that the State of Michigan Attorney General's Office is investigating allegations that Medicaid funds may have been used by the county to pay employees that were not performing mental health functions.

In a report to management and the audit committee in 2010, the external auditors also expressed a concern regarding the use of restricted cash to pay general operating fund obligations. The implementation of GASB 54, effective June 15, 2010, will also help the county better identify funds that are restricted for general purpose and use.

Based on a review of the cash flow projection prepared by M&B dated December 2011, there are some alarming indicators that require closer scrutiny. The fact that even after the approval by the commission for the county to borrow \$100 million, the cash position of the county is so deficient, it still leaves the general fund pooled cash in a negative cash position for all twelve (12) months in the cash flow projection. In fact, it is projected by November 2012 the general fund pooled cash will be in a negative cash position of more than \$185 million.

This will again necessitate the need to immediately float another short-term loan for another \$100 million on or before November 2012, or render the county unable to meet its general fund obligations.

The projection further supports the fact that the county is currently using restricted cash to meet its general fund operating expenses; therefore, it could create a burden on the county's ability to meet restricted funds program objectives. In essence, this cash flow projection reports that restricted cash is being used to fund the general fund's daily operations.

Restricted cash are monies that are earmarked for specific purposes and generally cannot



be used for general governmental operating expenses. For example, restricted funds are those grants and other support funds that are received from the state and federal government earmarked or designated for specific purposes.

Further, this cash flow projection reflects that the county is unable to meet its operating expenses without this short-term borrowing now, as well as going forward into the next fiscal year.

### **Monthly Cash Needs**

Based on our review of the cash flow projections it appears that the general fund needs approximately \$54.8 million to meet its monthly cash requirements which approximates \$658 million annually. Conversely, the cash inflows are approximately \$49.6 million on a monthly basis and \$596 million annually.

Consequently, cash outlays are exceeding expenditures by approximately \$5.2 million on a monthly basis and \$62.4 million annually. Needless to say, unless strategies are implemented to reduce the structural deficits the general fund will continue to accumulate deficits of \$60 million or more on an annual basis.

On the other hand, exploring methods to minimize the cash requirement outlay by \$10 million per month could minimize the necessity for short-term borrowing and generate an operating surplus of \$60 million annually.

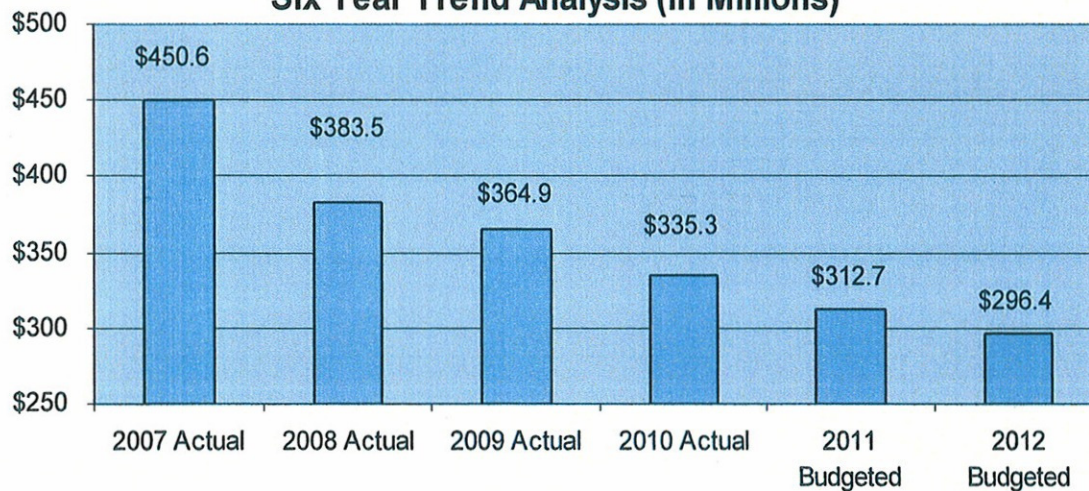
### **Property Tax Revenues**

Property tax revenues have decreased by more than \$154 million over the last six years and the county has still yet to introduce a county-wide viable strategic plan to avoid cash flow shortfalls and eliminate deficit spending. The \$154 million decrease in property tax revenue represents close to a 30% reduction in general fund revenue.

A recent newspaper article stated: "Property tax values in Wayne County are continuing to decrease at a rate of 6% in Wayne County based on a 2011 assessment." Therefore, one could conclude that property tax revenues will probably continue to decline until there are some significant economic improvements in Southeastern Michigan.

It would be prudent for the CEO, among other things, to submit a budget to the commission with corresponding decreases in general fund expenditures of 30% or more in order to align expenses with revenue.

### General Fund Property Tax Revenue Six Year Trend Analysis (in Millions)



**Source:** The Wayne County CAFR and budget book.

Based on historical statistics reported in the 2010 CAFR, approximately 72% of total property taxes are collected in the summer months of August and September and 28% in the winter months of December and January of each year. However, a percentage of the summer and winter taxes collected are earmarked and restricted for the jails, parks, and soldier's relief fund.

Under the statute, short-term borrowing is expected to be paid when the taxes are actually collected each year. Based on this criteria, the TAN practically fully paid off in September 2012, but it leaves the general fund pooled cash in (\$171) million deficit. This means the county will have to turn around and borrow again before the end of the calendar year.

#### **Overstating Revenue Projections**

Based on our review of the budget to actual revenue for fiscal years 2008 – 2010 revenues, we determined that actual revenue fell short of the budgeted amount by more than \$300 million. Additionally, we found instances where the Food Safety and Jail Medical programs revenue budgeted in the general fund are overstated for fiscal years 2010 and 2011 by as much as \$7.5 million.

The overstatement of revenue has resulted in allowing expenditures to be incurred in excess of funds available to pay for them. Needless to say, expenditures made in excess of revenue collections leads to deficit spending.

#### **Decrease in Accumulative Deficits**

All is not gloom, based on a preliminary review of the most recent audited financial statements, the general fund generated a surplus of \$9 million for FY 2011 before an



offset of \$43 million related to a lawsuit settlement with the Third Circuit Court, and the county-wide unassigned/unrestricted deficits decreased by \$55 million (\$253 million - \$198 million) as of September 30, 2011. This is very encouraging and an indication that some cost saving measures employed by the CEO are working. The OAG is performing a separate engagement on the analysis of the fund deficits.

However, the CFO informed us that there is an annual deficit of \$45 million expected for the general fund for the FY 2012. We contacted the budget director and he stated that at the end of the first quarter of each year, departments with operating deficits are required, within 10 days after the end of the quarter, to submit a deficit elimination plan to M&B.

According to the Wayne County Enrolled Ordinance 2010-515: "a department or office with a projected deficit shall develop and submit a deficit elimination plan, in line-item form, to the commission and the CEO within seven (7) business days of receipt of written notice from M&B."

### **Assessment of Capital Projects – Cash Outlay**

Another area that impacts the county's cash flow projections results from the payments of debt service for capital improvement projects. Management must take into consideration, in its fiscal strategic plan, its ability to fund capital projects against the county being able to ensure mandated and vital county services and general fund obligations are met.

Over the past fiscal years, the county has issued bonds to fund such projects as the purchase of the Guardian Building - \$51 million, infrastructure improvement for the Pinnacle Race Track - \$26 million, and most recently, the construction of a new jail facility - \$200 million. For a grand total of \$277 million in additional debt issued since 2008. Another factor for consideration is the interest rates charged to obtain the bond funds.

As of the date of this memo, for the identified projects, they either do not generate sufficient revenue or never were intended to annually pay the debt service on the bond issuance that funded the capital project. We determined, for fiscal years 2009-2011, the annual average principal and interest debt service payments for these three projects are \$16.5 million. The debt service will be required to be repaid over the next thirty years. As the payer of last resort, the county's general fund is responsible to make the requisite debt payments.

### **Erosion of Institutional Knowledge**

There have been several changes in key positions within M&B. These turnovers have resulted in the delaying of the issuance of the CAFR for 2011, and other internal reports, primarily due to the loss of individuals with key institutional knowledge and experience about county operations.

Over the last two years, M&B and the CEO have lost two financial reporting directors, a budget director, personnel director, Chief Information Officer, and Deputy CEO, as well as a host of other key personnel in managerial positions. The loss of key personnel and human resources appears to have impacted the county's ability to timely complete cash



flow projections, the deficit elimination plan, revenue and expenses reports related to the Guarding Building, and the annual CAFR. Although the replacement of key personnel appears to be quite competent, it will still take time to regain the institutional knowledge that has been lost.

According to a recent article in the Internal Auditor journal the loss of key individuals poses high risk to an organization's operations; it state's "knowledge management encompasses the ways in which information and the interpretation of information is handled. It involves the ways an organization's employees - individually and collectively – learn, sort, analyze, understand, distribute, represent, and use information to achieve organization objectives." It further states a "comprehensive transfer of knowledge from departing to new and existing personnel is impossible."

The CEO should consider initiating succession planning and recruitment actions to address the anticipated separation of personnel in important functions. Best practices advocate that a good succession plan would better position the organization to deal with turnover in the workforce. For example, management may want to consider negotiating staggered retirement dates to avoid a mass turnover in experienced employees. This also includes defining job descriptions and operational and administrative duties for key employees.

We were informed by the CFO that the personnel department is in the process of developing job duties and responsibilities for key positions and succession planning.

### **New Commission Ordinances**

Over last few months the commissioners are in the process of establishing new ordinances to address county-wide ethics, appointment confirmations, and limitation on benefits being offered to county employees, as well as others that was recently adopted within the last year.

We believe ordinances are needed and will serve to make county government more transparent and accountable. However, I believe the ordinances are missing a key element which requires the executive branch to establish policies and procedures to outline the business processes that are necessary to implement particular ordinances.

For example, we noted there is an ordinance adopted in 2010 pertaining to deficit spending but there was no requirement for the CEO to develop or revise their policies and procedures to comply with the new ordinance.

To leadership's credit, we noted the procurement ordinance adopted in December 2006 does have a provision that requires the purchasing director to establish policies governing the procurement, and management of the purchasing processes.

Adding standard language into complex ordinances, when warranted, could read: "The chief executive officer or his or her designee shall prepare and implement policies and procedures to provide for concurrence, uniformity and consistency in the application of this ordinance" as well as establish criteria for the existence and effectiveness of a



defined process.

Adding such language to each applicable new ordinance will establish the criteria that are necessary that are necessary to implement and evaluate compliance with a particular ordinance. In fact, this would also enhance management's ability to adhere to the adopted ordinance.

### **CFO Authority**

The CFO is granted authority under Section 5.143 of the Wayne County Charter to only allow expenditures that are appropriated in the budget and it goes on to state that expenditures made in excess of the amount appropriated is a violation of this section and is void.

Based on a discussion with the CFO it was stated that whenever attempts have been made to control expenditures departments, such as the Sheriff and 3<sup>rd</sup> Circuit Court, have filed litigation to stop such action, and often time they have won lawsuits to block the CEO's effort to control costs.

From a legal view point, a closer review of the decisions made by the courts in the above referenced litigations now provides opportunities for the administration to revise its strategy to assist them in accomplishing the mandate as stated in Section 5.143 of the charter.

Additionally, the CFO believes a unified effort by commission and administration, as well as the adoption of the long range strategic plan introduced by M&B a couple of years ago would bring about some positive results in limiting expenditures made in excess of the budget.

### **Overall Concerns:**

In reviewing the cash flow projections provided by M&B, there are several indicators that the commission should be concerned about:

1. The general fund's cash position immediately after the borrowing of the \$100 million will result in the general fund cash being projected at (\$49) million deficit and remains in a deficit position the remainder of the year.
2. Property tax revenues have decreased by more than \$154 million over the last six years. Property tax collections projected at \$296 million for FY 2012 are the lowest they have ever been.
3. It has cost the county over \$8 million over the last four years in interest and fees paid related to TAN borrowing; these funds could be better used for other purposes.
4. There is a concern that the county is using restricted cash to pay for general operating expenses during the year, which could limit the amount of cash available to carry out special revenue programs that are appropriated in the budget adopted by the commissioners.
5. Historically, revenue projections have been overstated in the past and the decertification of revenues has not always been made on a timely basis.

6. The reduction of the deficits in the general fund and county-wide is encouraging, but fiscal year 2008-2009 was the last time a DEP was submitted to the State Treasurer; a potential triggering device under the EFM act.
7. The turnover in key positions has exposed the county to the loss of institutional knowledge and impacted its ability to issue the CAFR and other internal reports on a timely basis.
8. The commissioners need to consider adding language to certain ordinances requiring the CEO to establish policies and procedures in order to promote to compliance.

### **Suggested Action**

- ❖ M&B should closely monitor and accelerate the collection of general fund cash in order to maximize general pooled cash balances on a monthly basis.
- ❖ M&B should review monthly revenue and expenditure projections county-wide to make sure they are on target to equal the revenue and expenditures appropriated in the budget. A significant portion of their effort should concentrate on actual revenue collections because it drives expenditures.
- ❖ There is an urgent need for management to address the general fund structural deficits in the general fund and explore ways to at least reduce the cash requirement outlay by \$5 million a monthly basis.
- ❖ The commission needs to enforce Enrolled Ordinance No. 2010-515, which requires departments that are incurring deficits to develop and timely submit a DEP to M&B and the commission for acceptance and approval.
- ❖ The CEO and commissioners could develop a joint crisis management team composed of commissioners, CFO, representatives from the Treasurer, PAO, Sheriff, Clerk, and Courts for the purpose of analyzing and monitoring the cash flow projections and deficits over the next two – five years and continue to make suggestions as needed to eradicate deficit spending.
- ❖ The commission could request the CEO to provide an assessment of all planned and proposed capital projects borrowing against the cash outlay that will be required by the general fund to service the debt.
- ❖ The CEO could develop a viable succession and recruiting plan for key employees that are expected to leave the county and provide it to the commission for acceptance. The CFO stated the personnel department is currently working on a succession plan that is to be implemented county-wide.
- ❖ Finally, the CFO and CEO must exercise the authority granted to them in the charter and disallow all expenditures that are not included in the appropriated budget adopted by the commission.



Since this a review engagement intended to add value, the OAG will not be requesting a corrective action plan for this engagement.

### **Views from Responsible Officials**

The CFO provided her views and assessments of the report contents and in some instances also provided a plan of action going forward. We found the CFO responses to be very positive, encouraging and forward thinking. For a detail narrative of her responses see - Appendix B - Views from Responsible Officials.

### **Conclusion**

According to M&B, the county is in a cash position where if they did not do any short-term borrowing they would not be able to make payroll and pay its vendors. This is a very tenuous position for the administration and the commissioners to be in and it leaves no alternative but to seek short-term borrowing.

It is good that the deficits are decreasing and cash projections are being performed and it allows the county to forecast ahead, as well as develop strategies to limiting the amount of borrowing in the future.

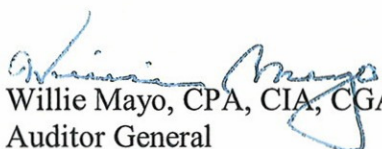
If the county is successful in tackling the causes of the cash flow problems, it will lead to adopting an achievable DEP in eliminating the county wide deficits that are currently reported at \$198 million as of September 30, 2011.

Finally, we believe a succession plan for the turnover in managerial personnel is one of the keys to the county's future survival. In addition, unless the commissioners require policies and procedures to be established for critical ordinances being adopted, it could fail to assist management in meeting the goals and objectives desired by the commissioners.

We have generally concluded that county leadership is identifying and monitoring the cash projection needs of the county. This became evident through the preparation of cash flow projections on a monthly basis and submission to the Committee on Ways and Means.

However, we believe more needs to be done by the administration and commission to alleviate the necessity of borrowing restricted funds to pay general fund operating expenses. This practice is precariously risky and could lead to violations being imposed by certain regulatory agencies.

Respectfully submitted,

  
Willie Mayo, CPA, CIA, CGAP, CICA  
Auditor General

Appendix A

Schedule of Cash Flows

General Pooled Cash



Charter County of Wayne, Michigan  
Schedule of Cash Flows  
General Pooled Cash

	Actual November 2011	Actual December 2011	Projected January 2012	Projected February 2012	Projected March 2012	Projected April 2012
<b>General Pooled Cash, Beginning **</b>	<b>172,126,575</b>	<b>143,091,972</b>	<b>142,189,156</b>	<b>140,099,720</b>	<b>158,636,720</b>	<b>217,305,219</b>
General Fund						
Operating Inflows†	32,770,821	26,512,781	44,366,097	69,367,414	35,195,118	23,601,589
Operating Outflows	(39,684,103)	(47,046,995)	(57,508,192)	(42,952,378)	(53,894,578)	(65,196,631)
Receipt of TANS (A)	-	-	-	-	100,000,000	-
Repayment of TANS**	-	-	-	-	(6,682,790) ††	(2,545,825)
Other Non-Trust Funds						
Inflows	148,032,303	125,887,634	145,549,352	125,986,783	135,395,066	136,902,909
Outflows	(159,036,143)	(123,551,743)	(128,621,548)	(132,569,462)	(154,640,213)	(141,956,788)
Net DTRF activity	1,015	(1,322,596)	(5,885,145)	(1,295,357)	3,295,896	725,471
Trust and Agency Funds						
Inflows	43,017,994	51,214,796	-	-	-	-
Outflows	(54,134,490)	(32,586,693)	-	-	-	-
Net Trust and Agency activity	(11,116,496)	18,628,103	-	-	-	-
Net clearing fund activity	-	-	-	-	-	-
General Pooled Cash, Ending	143,091,972	142,189,156	140,099,720	158,636,720	217,305,219	168,835,944
Less: Trust and Agency Balance	30,362,593	48,990,696	48,990,696	48,990,696	48,990,696	48,990,696
Remaining General Pooled Cash	112,729,379	93,208,460	91,109,024	109,646,024	168,314,523	119,845,248
General Fund position in pooled cash	(116,381,086)	(136,915,300)	(150,057,395)	(123,642,359)	(49,024,609)	(93,165,476)

\*\* This represents the pooled cash balance per the County's General Ledger. Cash at the bank will differ due to outstanding/uncleared items.

\*\*\* This line represents transfers to the TANS reserve pool. Payment is not made to the note holder until end of note term. This represents a projected statutorily required 45.55% set-aside of collections on the 2012 operating levies.

Δ The County anticipates issuing TANS in mid-March 2012 @ \$100,000,000 for FY 2012 operating purposes. The projections assume a 4% interest rate over 8.5 months.

† Assumes renewal of Jail Millage

†† Represents 50% of the required set aside for the partial month of March

Trust and Agency Activity: Trust and Agency activity should, over time, be zero as this is money the County collects on behalf of others. As funds collected in a trust or agent capacity are not available for County use, no projections are presented for

Charter County of Wayne, Michigan  
Schedule of Cash Flows  
General Pooled Cash

	Projected May 2012	Projected June 2012	Projected July 2012	Projected August 2012	Projected September 2012	Projected October 2012
<b>General Pooled Cash, Beginning</b>	<b>168,835,944</b>	<b>162,962,689</b>	<b>228,969,422</b>	<b>116,577,745</b>	<b>99,217,841</b>	<b>111,386,401</b>
General Fund						
Operating Inflows	39,465,037	54,719,762	32,788,472	63,345,347	125,915,677	48,174,357
Operating Outflows	(44,696,790)	(65,594,820)	(38,409,369)	(52,002,007)	(83,255,300)	(48,008,243)
Receipt of TANS	-	-	-	-	-	-
Repayment of TANS***	(5,409,878)	(429,608)	(2,689,027)	(29,913,442)	(51,871,181)	(3,291,582)
Other Non-Trust Funds						
Inflows	161,549,030	138,247,789	134,032,301	161,135,406	286,034,153	147,996,980
Outflows	(156,993,650)	(133,081,419)	(123,216,096)	(160,512,143)	(269,401,060)	(157,667,300)
DTRF						
Inflows	23,063,008	681,354,040	20,613,158	49,832,946	56,696,735	37,880,164
Outflows	(22,850,013)	(609,209,011)	(115,511,115)	(49,246,011)	(51,950,464)	(17,078,561)
Net DTRF activity	212,995	72,145,029	(94,897,957)	586,935	4,746,271	20,801,603
Trust and Agency Funds						
Inflows	-	-	-	-	-	-
Outflows	-	-	-	-	-	-
Net Trust and Agency activity	-	-	-	-	-	-
Net clearing fund activity	-	-	-	-	-	-
General Pooled Cash, Ending	162,962,689	228,969,422	116,577,745	99,217,841	111,386,401	119,392,216
Less: Trust and Agency Balance	48,990,696	48,990,696	48,990,696	48,990,696	48,990,696	48,990,696
Remaining General Pooled Cash	113,971,993	179,978,726	67,587,049	50,227,145	62,395,705	70,401,520
General Fund position in pooled cash	(103,807,107)	(115,111,773)	(143,421,697)	(161,991,799)	(171,202,604)	(174,328,071)
Projected Tax Collections	8,500,000.00	675,000.00	4,225,000.00	47,000,000.00	81,500,000.00	30,000,000.00
Applicable Ratio	63.65%	63.65%	63.65%	63.65%	63.65%	63.65%
Set-Aside Amount	5,409,877.80	429,607.94	2,689,027.49	29,913,441.96	51,871,181.26	19,093,686.35



Charter County of Wayne, Michigan  
Schedule of Cash Flows  
General Pooled Cash

	Projected November 2012
General Fund	119,392,216
Operating Inflows	29,593,581
Operating Outflows	(40,483,688)
Receipt of TANS	-
Repayment of TANS***	-
Other Non-Trust Funds	
Inflows	152,762,293
Outflows	(148,661,530)
Inflows	17,731,577
Outflows	(17,730,562)
Net DTRF activity	1,015
Trust and Agency Funds	
Inflows	-
Outflows	-
Net Trust and Agency activity	-
Net clearing fund activity	-
General Pooled Cash, Ending	112,603,887
Less: Trust and Agency Balance	48,990,696
Remaining General Pooled Cash	63,613,191
General Fund position in pooled cash	(185,218,178)

## Appendix B

### Views of Responsible Officials





**Robert A. Ficano**  
County Executive

February 29, 2012

Willie Mayo  
Auditor General  
County of Wayne  
500 Griswold, 8<sup>th</sup> Floor  
Detroit, MI 48226

RE: Analysis of Cash Flow Projections

Dear Mr. Mayo,

I have reviewed the working draft of the above referenced document and would like to offer the following comments:

Tax Anticipation Notes (TANs)

The interest rate for the TANs issued in December 2010 is stated incorrectly. The interest rate stated is 4.00%; in fact the interest rate on the TANs was 3.50% with a yield of 2.50% (the TANs were issued at a premium). Tax Anticipation Notes have become necessary to meet the cash requirements of the County prior to the receipt of property taxes. They are low risk securities and appeal primarily to large investors. Each year since 2009, the County has issued TANs to finance its current operations in anticipation of future tax receipts. The collection of property tax receipts is cyclical in nature. The County receives the bulk of this revenue, over 73%, in the months of August, September, October and November while expenditures are made almost daily. Additionally, with the roll out of the State's "property tax shift" in 2005, the housing market conditions and the accumulated deficits, the need for this short term borrowing has become even more critical.

Although it has cost the County several million dollars in interest cost, it is still an inexpensive method of financing short term cash shortfalls. The working draft lists "Total Borrowing Costs." The breakout of these costs is interest, underwriter fees, and direct costs of issuance. Of the Total Borrowing Costs, interest costs were approximately \$6 million, underwriting fees were \$335,000 and Direct Costs of Issuance were \$183,200. No doubt a longer term approach is needed but there is no silver bullet. Fiscal sustainability is a long term concept. Therefore, it requires a long term plan, one that reduces deficits over an extended period and that, to the fullest extent possible, is credible, practical, and enforceable. In current circumstances, an advantage of taking a longer-term perspective in forming concrete plans for fiscal consolidation is that the County can avoid a sudden fiscal contraction that might put the still very fragile recovery at risk. At the same time, acting now to put in place a credible plan for reducing future

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deficits would not only enhance economic performance in the long run, but could also yield near-term benefits. We cannot expect to “cut” our way out of the fiscal imbalances. I urge the Legislative body to work with the Administration to quickly develop and implement a credible plan to achieve long-term sustainability. I hope, though, that such a plan can be achieved in the near term without resorting to or actions that would cast doubt on the creditworthiness of the Wayne County.

#### Cash Flow Projections – General Pooled Cash

The County pools the cash balances from its various unrestricted, designated, restricted and agency funds to achieve economies of scale necessary for maximizing investment returns and creating internal operating efficiencies. This is a common practice for both the public and private sectors. Although the County has used its restricted cash to pay for general operating expense during the year, there has not been an instance where projects of a special revenue program was impaired or delayed. In fact, two of the County’s largest special revenue (Roads and Mental Health) ended fiscal year 2011 with healthy funds. In addition, there has been no instance where restricted dollars held by the County for other agencies were not available when required. Although this is not the preferred method of operation, there is no guidance to suggest that this practice is illegal.

Creating positive cash flow does not happen by accident. Ideally, an organization should have more cash inflow (or a surplus) than outflow in order handle its obligations. Among other things, the office of the CFO will designate a person from Management and Budget to work with the Treasurer’s office to form a cash management team. The full scope of the team cannot be fully determined at this time as they will involve input from the Treasurer’s office. Although the concept of pooled cash has been in existence in the County for years, there is no formal policy that one can point to. One of the items I see as critical is the development of a pooled cash policy. In addition, I would like for the team to explore the use of credit cards for payment County wide. This will help the County to get cash in the door sooner.

#### Property Tax Revenues

The Auditor General recommends that a county wide strategic plan be introduced to avoid cash flow shortfalls and eliminate deficit spending. There is already an initiative to deal with his concerns. In 2009, the County with the assistance of a consultant embarked upon a Long Term Financial Plan initiative. The Long Term Financial Plan (LTFP) is an annual process to address issues impacting the County's financial condition. The process begins by identifying critical areas which have, or are expected to have, an impact on the financial condition of the County over the next five years. Once the issues are identified, specific goals and objectives are developed for each project. Project teams are formed to prepare option papers with specific and practical recommendations. The issues and recommendations are presented to the County Executive and the Commission for direction on implementation. Nearly all of elected officials and departments participated in this project. The project lost its momentum in 2011. I recommend that the County revisit this initiative immediately rather than establishing another group.



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## Overstating Revenue Projections

There is no argument that revenue projections appeared to be overestimated with respect to the Food Safety and Jail Medical programs. Forecasting is—in part—dependent on observing past trends to predict future results. Because the recently-concluded economic recession and the County's policy responses to it were unprecedented, there are many open questions about how the economy and County revenues will react in the coming years as the recovery progresses. The need for caution in projecting future revenues is evident. The projections given to Management and Budget are the department's best estimate of what they believed the revenues will be. At the point, it becomes clear that certain revenues are not going to be achieved, the revenues should be decertified and thus the corresponding expenses should not be allowed. This action means this is not the time to consider major expansions of government programs. Departments will have to continue to find savings where they can and find ways to operate at less than full capacity. Likewise, elected officials need to show discipline. As we claw out of our deep budget hole and struggle to bring County finances back into balance, the Chief Financial Officer will put together a forecasting team. This team will consist of the following members:

The Directors of Assessments and Equalization, Economic Development and Growth Engine, Personnel/Human Resources, Budget and Planning, the Chief Financial Officer, the Office of the County Executive and possibly the Wayne County Treasurer. The role of this team is to provide the strategic input of the County in order to address future challenges.

## Deficits are Decreasing

While I appreciate the Auditor General for the accolades for generating a General Fund surplus at the end of fiscal 2011 and thus reducing our deficit, the need to stay within our budget is ever so great. The "surplus" was the result of the settlement with Third Circuit Court and the retained earnings generated by the County Treasurer's Revolving Fund Program. The County's General Fund still has an accumulated deficit of \$76.4 million. Additionally, first quarter projections for fiscal 2012 show a \$45 million deficit if no action is taken to avoid expenditure overruns. I cannot emphasize the need to revisit the long term financial plan. The long-term financial plan enables proactive management of government finances, rather than reactive responses to financial crises as they occur.

The Auditor General's report makes reference to the fact that the County has not provided a Deficit Elimination Plan (DEP) to the State since fiscal year 2009 and that this is a potential trigger under the Emergency Financial Manager Act (EFM). While it is true that the County has not submitted a new DEP we are in compliance with the 2009 plan. Additionally, the executive branch has been working very closely with the State Treasury since early 2011 to complete the County's 2010 plan. Many of the reasons for County's deficits are related to the way the State is funding the County. Preliminary there is an agreement between the two parties. We have not received any letter from the State to say that we are out of compliance with the requirement.

In addition to the above, the CFO is in the process of putting together a white paper that will provide an analysis of the EFM Act as it relates to Wayne County. That analysis is expected to be completed within the next thirty days and will be shared with the legislative branch.

#### Erosion of Institutional Knowledge

While it is true that the Department of Management and Budget has lost some key personnel, we have been able to fill these positions internally with qualified professionals. Many of these individuals had worked alongside the previous incumbents and therefore have significantly reduced the learning curve. Additionally, the Department of Personnel/Human Resources has begun a succession development effort for Directors, Deputy Directors, and Division Directors for the executive branch. Although it is in its infancy stages, it is anticipated that phase I will be completed by June 2012.

#### New Commission Ordinances

No comment. If the auditor general believes that adding language to certain ordinances adds value, I do not object.

#### CFO Authority

The Charter is clear about the CFO's authority as to allowing expenditures that are appropriated in the budget. However, there are many obstacles in carrying out this mandate. The proliferation of lawsuits by other elected officials is just one of them. In order to reduce deficits, the County must either reduce the amount of money it spends (through cutting programs or reducing costs) or increase the amount of money it takes in (through increased taxes or other revenue streams. In crafting last year's (FY 2012) budget, many difficult decisions were made. County services were eliminated, reduced, or delayed and funding of departments was reduced. With all of the tough decisions made, the current fiscal path of Wayne County is imprudent and unsustainable. Property tax receipts would have to rise considerably faster than our historical experience to enable the operating budget to remain in the historical range. It is no longer enough to balance the operations of departments. It is imperative that all departments make a consistent and deliberate effort to control costs by operating within its budget and with efficiency. Incentives need to be implemented for departments that come in under budget that result in savings that increase General Fund balance in the short term. This approach will result in implementing structural reductions sooner than later. The CFO will be meeting with all of the departments and elected officials in the month of March to discuss this concept among other items as the County prepares for the next budget cycle.

Sincerely,



Carla E. Sledge  
Chief Financial Officer