

PORT OF OAKLAND

Report to Board of Port Commissioners
Year Ended June 30, 2016



Certified
Public
Accountants

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Board of Port Commissioners
of the City of Oakland, California

In planning and performing our audit of the financial statements of the Port of Oakland (Port) as of and for the year ended June 30, 2016, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Governmental Auditing Standards*, issued by the Comptroller general of the United States, we considered the Port's internal control over financial reporting (internal control) as a basis for designing our 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 Port's internal control. Accordingly, we do not express an opinion on the effectiveness of the Port's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency or combination of deficiencies in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. In addition, because of inherent limitations in internal control, including the possibility of management override of controls, misstatements due to error or fraud may occur and not be detected by such controls. Given these limitations during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

During our audit, we became aware of a matter that is an opportunity for strengthening internal controls and operating efficiency. The accompanying schedule of current year comment and response discusses this matter. This report does not affect our report dated November 29, 2016, on the financial statements of the Port.

The Port's response to the comment identified in our audit are described in the accompanying schedule of current year comment and response. We did not audit the Port's response and, accordingly, we express no opinion on it. We will review the status of the comment during our next audit engagement. We have already discussed the comment and suggestion with various Port personnel, and we will be pleased to discuss it in further detail at your convenience, to perform any additional study of the matter, or to assist you in implementing the suggestion.

We have also provided a status of our prior year comments beginning on page 8 of this document.

Additionally, we have included in this letter a report on communications with the Board of Port Commissioners as required by auditing standards generally accepted in the United States of America.

This communication is intended solely for the information and use of the Board of Port Commissioners, management and others within the Port, and is not intended to be and should not be used by anyone other than these specified parties.

Macias Gini & O'Connell LLP

Oakland, California
November 29, 2016

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REQUIRED COMMUNICATIONS

We have audited the financial statements of the Port of Oakland (Port), as of and for the year ended June 30, 2016. Professional auditing standards require that we provide you with information about our responsibilities under generally accepted auditing standards, *Government Auditing Standards* and the Uniform Guidance, as well as certain information related to the planned scope and timing of our audit. We have communicated such information in our engagement letter dated July 7, 2016 and our audit plan dated July 6, 2016. Professional standards also require that we communicate to you the following information related to our audit.

Significant Audit Findings

Qualitative Aspects of Accounting Practices

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by the Port are described in Note 2 to the Port's financial statements. As described in Note 2 to the financial statements, the Port changed its accounting policies related to the following:

- ***Governmental Accounting Standards Board (GASB) Statement No. 72 – Fair Value Measurement and Application***
This statement enhances the comparability of financial statements among governments by requiring measurements of certain assets and liabilities at fair value using a consistent and more detailed definition of fair value and accepted valuation techniques. This statement requires additional disclosures and did not have a significant impact to the Port's financial statements. Please refer to Note 3 of the Port's financial statements for more information.

- ***GASB Statement No. 73, Accounting and Financial Reporting for Pensions and Related Assets That Are Not Within the Scope of GASB Statements 68 and Amendments to Certain Provisions of GASB Statements 67 and 68***
This statement establishes requirements for defined benefit pensions that are not within the scope of GASB Statement No. 68, as well as for the assets accumulated for the purposes of providing those pensions. GASB Statement No. 73 amends certain provisions of GASB Statement No. 67, *Financial Reporting for Pension Plans*, and GASB Statement No. 68 for pension plans and pensions that are within their respective scopes. GASB Statement No. 73 addresses the recognition of the total pension liability of such plans and the disclosures necessary for the plans that did not meet the definition of GASB Statement No. 68. This statement did not have a significant impact to the Port's financial statements.

- ***GASB Statement No. 76, The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments***
This statement clarifies the hierarchy of Generally Accepted Accounting Principles (GAAP) and reduces the GAAP hierarchy to two categories of authoritative GAAP and addresses the use of authoritative and nonauthoritative literature in the event that the accounting treatment for a transaction or other event is not specified within the scope of authoritative GAAP. This statement did not have a significant impact to the Port's financial statements.

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REQUIRED COMMUNICATIONS (Continued)

Qualitative Aspects of Accounting Practices (Continued)

We noted no transactions entered into by the Port during the year for which there is a lack of authoritative guidance or consensus. All significant transactions have been recognized in the financial statements in the proper period.

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

- Claims liabilities;
- Pollution remediation costs;
- Allowance for losses on customer accounts receivable;
- Workers' compensation liability;
- Pension contributions and Postemployment benefits other than pensions (OPEB) liability;
- Depreciation for capital assets;
- Allocation of costs to construction projects;

Management's estimates were based on the following:

- Estimated claims liabilities and pollution remediation costs are based on independent consultant valuations as well as internal valuations;
- Allowance for losses on customer accounts receivable is based on historical collection activity;
- Workers' compensation liability is based on an actuarial valuation;
- For the pension and OPEB plans, the contributions and liabilities are based on actuarial valuations;
- Depreciation estimates for capital assets are based on estimated useful lives of assets; and
- Allocation of costs to construction projects is based on a methodology in accordance with the Uniform Guidance.

We evaluated the key factors and assumptions used to develop these accounting estimates in determining that they are reasonable in relation to the Port's financial statements.

Certain financial statement disclosures are particularly sensitive because of their significance to financial statement users. The most sensitive disclosures affecting the financial statements have been noted above.

The financial statement disclosures are neutral, consistent and clear.

Difficulties Encountered in Performing the Audit

We encountered no significant difficulties in dealing with management in performing and completing our audit.

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Corrected and Uncorrected Misstatements

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management. Management has corrected all such misstatements. In addition, none of the misstatements detected as a result of audit procedures and corrected by management were material, either individually or in the aggregate to the financial statements taken as a whole.

Disagreements with Management

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

Management Representations

We have requested certain representations from management that are included in the management representation letter dated November 29, 2016.

Management Consultations with Other Independent Accountants

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

Other Matters

Other Audit Findings or Issues

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the Port's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

Other Information in Documents Containing Audited Financial Statements

We applied certain limited procedures to the management's discussion and analysis and the schedule of funding progress – other postemployment benefits, which are required supplementary information (RSI) that supplements the financial statements. Our procedures consisted of inquiries of management regarding the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the financial statements, and other knowledge we obtained during our audit of the financial statements. We did not audit the RSI and do not express an opinion or provide any assurance on the RSI.

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Other Information in Documents Containing Audited Financial Statements (continued)

We were not engaged to report on the Introductory Section and the Statistical Section, which accompany the financial statements but are not RSI. We did not audit or perform other procedures on this other information and we do not express an opinion or provide any assurance on it.

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CURRENT YEAR COMMENTS AND RESPONSES

**Comment 2016-001 – Informational Comment
GASB Exposure Draft on Leases**

In January 2016, the GASB issued an exposure draft that proposes a single approach for lease reporting. The proposal would provide guidance for lease contracts for nonfinancial assets, such as vehicles, heavy equipment, infrastructure, and buildings. The proposed guidance would not apply to grants, donated assets, or leases of intangible assets such as patents and software licenses.

The exposure draft, *Leases*, would require a lessee government to recognize a lease liability and an intangible asset representing its right to use the leased asset. A lessor government would be required to recognize a lease receivable and deferred inflow of resources.

Under the proposal, a lessee would also report:

- Amortization expense related to the lease asset, recognizing the asset amount as an expense over the term of the lease.
- Interest expense related to the liability.
- Note disclosures with information about the lease, including a general description of the leasing arrangement.

The proposal also would require a lessor to report:

- Lease revenue and a corresponding reduction in the deferred inflow over the term of the lease.
- Interest revenue related to the receivable.
- Note disclosures with information about the lease, including a general description of the leasing arrangement.

This exposure draft will have a significant impact on the Port's system of internal controls and accounting policies and practices in tracking the various leases entered into by the Port with its customers. We recommend management to evaluate the impact of this exposure draft on its internal controls and accounting systems and implement changes as necessary.

Management's Response:

Port staff is aware of the proposed GASB on lease accounting and understands there may be significant changes to our financial statements and our reporting processes. The proposed GASB statement has not been issued; it is unclear when it will be issued and over what time period the implementation of these changes will occur. Over the next year, Port staff will begin evaluating the inventory of current leases and estimating how the proposed GASB will change our financial statement presentation.

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STATUS OF PRIOR YEAR COMMENTS

**Comment 2015-001 – Informational Comment
Uniform Guidance for Federal Awards**

The Office of Management and Budget (OMB) published new guidance for federal award programs, *OMB Uniform Guidance: Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*, commonly referred to as the “Uniform Guidance,” on December 26, 2013. The new guidance is a key component of a larger federal effort to more effectively focus federal grant resources on improving performance and outcomes while ensuring the financial integrity of taxpayer dollars. By streamlining eight federal circulars into a single, comprehensive policy guide, governments can better administer grants and other types of financial assistance by decreasing the administrative burden for recipients and reducing the risk of waste, fraud and abuse.

We recommend that the Port analyze the Uniform Guidance and work closely with its grantor agencies to determine what compliance requirements have changed beginning on December 26, 2014. Because many individuals amongst multiple departments of the Port may be involved with the administration of federal grants, the Port may want to consider forming a central Uniform Guidance taskforce to assist in assessing the Port’s internal controls, policies, and procedures that may need to be amended to ensure compliance with Uniform Guidance requirements. The Council on Financial Assistance Reform (COFAR) and OMB have conducted webcasts about the Uniform Guidance, which are now archived at www.cfo.gov/COFAR. COFAR has also published *Frequently Asked Questions for New Uniform Guidance at 2 CFR 200*, which may provide additional guidance to the Port.

Status:

Port staff in the Finance department read the Uniform Guidance and attended several trainings discussing the changes brought on by the Uniform Guidance. Port staff addressed the significant changes primarily affecting the Port’s grants and issued a new Grant Administration and Accounting policy, on November 19, 2015. While several individuals throughout the Port participate on grant funded projects, the primary responsibility for compliance rests with a few project managers who work intimately with their respective granting agency. In accordance with the new Grant Administration and Accounting policy, Port finance staff reviews each grant award as they are received and continues to distribute information to the project managers as deemed necessary. Therefore, the Port does not feel it necessary to organize a formal Uniform Guidance taskforce.

Additionally, the Port maintains an open dialogue with our granting agencies to help ensure compliance with specific grant requirements and the Uniform Guidance. For example, during the last fiscal year the Port completed its first formal review of an indirect cost rate proposal (which was not subject to the Uniform Guidance). During this review, Port staff discussed with the approving agency what changes the Port needs to make to future proposals (which will be subject to the Uniform Guidance) in order to be compliant.

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Comment 2015-002 – Informational Comment
New Other Postemployment Benefit Accounting Standard

Postemployment benefits other than pensions (OPEB) principally involve health care benefits, but also may include life insurance, disability, legal and other services. In June 2015, the GASB issued GASB Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, and GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, which are intended to improve the accounting and financial reporting by state and local governments for postemployment benefits (hereinafter referred as “OPEB Standards”).

The OPEB Standards are designed to improve the information reported on OPEB for decision-making and accountability purposes, comparability across governments, and transparency for those who avail themselves to it. They also are designed to equip state and local government policy makers and all users of governmental financial reports with information that would allow them to obtain a more comprehensive understanding of a government’s financial position.

The provisions in GASB Statement No. 74 affecting OPEB plans are effective for the fiscal year ending June 30, 2017. The provisions in GASB Statement No. 75 affecting employers that provide OPEB benefits are effective for the fiscal year ending June 30, 2018. The Port should begin assessing the impacts of the new OPEB Standards and develop a plan to implement the new accounting and financial reporting requirements. In addition, the Port should work closely with its OPEB administrator, actuaries, and auditors to ensure that all relevant parties are involved in the process that ultimately affect its successful implementation.

Status:

Port management is aware of GASB 74 and 75, and continues to discuss with our actuary potential impacts to our actuarial study to ensure that we take proper steps leading up to the implementation of GASB 74 and 75. Additionally, we look forward to working with our external auditors and with CalPERs to plan and execute a smooth implementation.