MEMORANDUM

EUGENE WATER & ELECTRIC BOARD

Rely on us.

TO: Commissioners Simpson, Brown, Helgeson, Manning and Mital

FROM: Cathy Bloom, Finance Manager
Susan Eicher, General Accounting and Treasury Supervisor

DATE: July 26, 2013

SUBJECT: 2012 Audit Management Letter Update

OBJECTIVE: Information only

As part of our annual process, attached is a mid-year status report on the comments from the 2012 Audit Management Letter. Please contact any of us if you have any questions.

Communication to Those Charged with
Governance and Internal Control Related Matters

Eugene Water & Electric Board

December 31, 2012

MOSS-ADAMS LLP
Certified Public Accountants | Business Consultants

**COMMUNICATION TO THOSE CHARGED WITH GOVERNANCE AND
INTERNAL CONTROL RELATED MATTERS**

To the Board of Commissioners
Eugene Water & Electric Board

Dear Commissioners:

We have audited the financial statements of Eugene Water & Electric Board (EWEB or the Board) as of and for the year ended December 31, 2012 and have issued our report thereon dated February 22, 2013. Professional standards require that we provide you with the following information related to our audit.

OUR RESPONSIBILITY UNDER AUDITING STANDARDS GENERALLY ACCEPTED IN THE UNITED STATES OF AMERICA

As stated in our engagement letter dated December 14, 2012, our responsibility, as described by professional standards, is to form and express an opinion about whether the financial statements prepared by management with your oversight are fairly presented, in all material respects, in conformity with U.S. generally accepted accounting principles. Our audit of the financial statements does not relieve you or management of your responsibilities.

Our responsibility is to plan and perform the audit in accordance with generally accepted auditing standards and to design the audit to obtain reasonable, rather than absolute, assurance about whether the financial statements are free of material misstatement. An audit of financial statements includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Board's internal control over financial reporting. Accordingly, we considered the Board's internal control solely for the purposes of determining our audit procedures and not to provide assurance concerning such internal control.

We are also responsible for communicating significant matters related to the financial statement audit that, in our professional judgment, are relevant to your responsibilities in overseeing the financial reporting process. However, we are not required to design procedures for the purpose of identifying other matters to communicate to you.

Planned Scope and Timing of the Audit

We performed the audit according to the planned scope and timing previously communicated to you in our planning meeting held during our interim fieldwork.

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Significant Accounting Policies

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by the Board are described in Note 1 to the financial statements. No new accounting policies were adopted and there were no changes in the application of existing policies during 2012. We noted no transactions entered into by the Board during the year for which there is a lack of authoritative guidance or consensus. There are no significant transactions that have been recognized in the financial statements in a different period than when the transaction occurred.

Accounting Estimates

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

Unbilled Revenue – Unbilled revenue is a measure of revenue earned through the end of the reporting period that has yet to be billed. This generally represents accounts with billing cycles that start in the reporting year and end in the subsequent year. We have evaluated the key factors and assumptions used to develop unbilled revenue in determining that it is reasonable in relation to the financial statements taken as a whole.

Allowance for Doubtful Accounts – This represents an estimate of the amount of accounts receivable that will not be collected. We have evaluated the key factors and assumptions used to develop the allowance in determining that it is reasonable in relation to the financial statements taken as a whole.

Recovery Periods for the Cost of Plant – This represents the depreciation of plant assets. Management's estimate of the recovery periods for the cost of plant is based on regulatory-prescribed depreciation recovery periods. We have evaluated the key factors and assumptions used to develop the recovery periods in determining that they are reasonable in relation to the financial statements taken as a whole.

Other Post-employment Benefit Obligations – This represents the amount of annual expense recognized for post-employment benefits. The amount is actuarially determined, with management input. No liability is recognized in EWEB's financial statements because the annual required contribution, as actuarially determined, is transferred to an external trust. We have evaluated the key factors and assumptions used to develop the annual expense in determining that it is reasonable in relation to the financial statements taken as a whole.

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Mark-to-Market Adjustment – Certain derivative instruments are marked to market at year end. However, the impact to the statement of revenues, expenses, and changes in net assets is deferred in accordance with GAAP. We have evaluated the key factors and assumptions used to develop year-end amounts and have determined that they are reasonable in relation to the financial statements taken as a whole.

Financial Statement Disclosures
The disclosures in the financial statements are consistent, clear, and understandable. Certain financial statement disclosures are particularly sensitive because of their significance to financial statement users. Significant disclosures include: Note 2 – Power Risk Management and Note 16 – Commitments and Contingencies.

Audit Adjustments/Reclassifications/Passed Adjustments

Audit Adjustments – For purposes of this letter, professional standards define an audit adjustment as a proposed correction of the financial statements made subsequent to the start of audit final fieldwork. An audit adjustment may or may not indicate matters that could have a significant effect on the Board's financial reporting process (that is, cause future financial statements to be materially misstated).

Audit adjustments are as follows:

- Electric Adjustments –

  o To correct derivatives balances based on corrections made to the mark-to-market calculation - $1.3 million

- Water Adjustments –

  o None

Reclassification adjustments are as follows:

- Electric Adjustments –

  o None

- Water Adjustments –

  o To reclassify a portion of the restricted component of net position to the net investment in capital assets component - $12.9 million

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Passed Adjustments – Passed adjustments are those entries found during the course of the audit that management has decided to not post to the financial statements of the Board. It has been concluded by management, and agreed upon by Moss Adams, that the adjustments are immaterial to the financial statements as a whole.

Passed adjustments are as follows:

- Electric Passed Adjustments –

    o None

- Water Passed Adjustments –

    o To reclassify open jobs that were in service at year end and should be closed to plant in service – $250,924

Significant Difficulties Encountered in Performing the Audit
We encountered no significant difficulties in dealing with management in performing and completing our audit.

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

Management Representations
We have requested certain representations from management that are included in the management representation letter dated February 22, 2013.

Consultation with Other 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 Board's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Independence
Moss Adams is independent in appearance and fact with respect to Eugene Water & Electric Board.

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COMMUNICATION OF INTERNAL CONTROL RELATED MATTERS

In planning and performing our audit of the financial statements of EWEB as of and for the year ended December 31, 2012, in accordance with auditing standards generally accepted in the United States of America, we considered the Board's internal control over financial reporting (internal control) as a basis for designing our auditing procedures 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 Board's internal control. Accordingly, we do not express an opinion on the effectiveness of the Board'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 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 did not find any material weaknesses through the course of our audit.

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 deficiencies, significant deficiencies, or material weaknesses. However, we identified a deficiency in internal control that we consider to be a significant deficiency. A significant deficiency is a deficiency, or 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. We consider the following deficiency in the Board's internal controls to be a significant deficiency:

>*Customer Adjustment Access Controls*
>During our review of the controls surrounding customer adjustments and through our IT testing procedures, we noted that anyone with read-write access to the CIS system could record adjustments. We also noted that a listing of personnel who has access to the CIS system is not routinely reviewed and therefore personnel that moved from the customer service department to another department still may have access to post adjustments to customer accounts. Our IT procedures revealed that over 200 users have access to the billing system and most have the ability to record adjustments. We recommend that management implement controls to review current access to the billing system and restrict read-write access to only the individuals authorized to record adjustments in the billing / customer service department or other authorized departments. Access to the system should be reviewed on a periodic basis to ensure that access to the system is appropriate.

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> ***Management's Response – Mark Freeman, Customer Service and EMS Manager***: EWEB and City of Eugene (COE) employees with established Customer Information System (CIS) Customer Service Analyst (CSA) or Cash Accounting roles have the ability to process adjustments. These roles are added or removed by the Help Desk at the request of transitioning employees' supervisor. Supervisors are not consistent in assessing whether staff continues to require access to the CIS to perform work and or in notifying C IS to process role changes.
>
> - Management will create an "Adjustment" class, removing the adjustment component from staff where this function is not needed or a requirement of their job.
>
> - To further ensure that Supervisors are accountable for appropriate assignment of CIS roles, and that the ability to process adjustments moves appropriately as employees transition between workgroups or out of the workplace, a CIS review of EWEB staff transitions could be monitored monthly for an "Adjustment" class of employees, and quarterly for all other EWEB staff transitions. COE should follow same format but EWEB cannot monitor COE staff transitions.
>
> ***Mid-year update – Mark Freeman, Customer Service and EMS Manager***: An "adjustment" class was created and the adjustment component was removed from non-essential staff as of July 2013. A report to monitor adjustments has been written and a review schedule established as of July 2013.

In addition to the required communications, we have identified the following matters for your consideration. Our recommendations are based on observations and testing during the course of our audit. These recommendations should be evaluated by management and the Commissioners for implementation and EWEB should conduct a cost benefit analysis including consideration of the risks for the recommended action.

Internal Control Structure

> ***Review of meter setup***
> During our discussions with management, we noted that upwards of $300,000 in new loans had been issued to commercial customers as a result of under-billings to 10-15 commercial accounts. The under-billings were caused by improper meter setup that resulted in a multiplier being used that was much lower than what was required for the type of account being serviced. The setup of these meters was not reviewed for accuracy in a timely manner and months passed without management detecting the underlying issue. The lack of a timely review of the installation and proper setup of these meters resulted in additional loans that the customers have agreed to pay back in the future. We recommend that a policy be established and implemented to require someone other than the person installing the meter, to review the work performed and the attributes setup in the billing system to ensure the appropriate usage is being calculated.

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Management's Response – Todd Simmons, Electric T&D Operations Manager: Following the retirement of the Meter Shop Crew Leader July 2011, management determined the position was no longer needed and the loaded salary could be saved. Double checking the meter count settings was a task performed by the Crew Leader but not listed on the task list created by the Crew Leader and Supervisor prior to the retirement. After the under-billings were discovered by the Meter Shop, a procedure was put in place to check all CT meter (current transformer meters that require a multiplier in our billing system) activity to confirm the correct settings were recorded in the system. Each month there is a rotation of the job duties the Meter Technicians perform with one Meter Tech assigned to inventory all meters, re-stock Meter Shop supplies, and check all CT meter install information from the previous month.

Mid-year update – Todd Simmons, Electric T&D Operations Manager: The Meter Technicians in the Meter Shop have been performing this CT meter installation check with excellent results. No further under-billings have taken place. The Meter Shop Supervisor has performed spot audits to confirm the success of the new process.

Anonymous whistleblower hotline

During several of our discussions with personnel at varying levels throughout the organization, we noted a perceived apprehension regarding the willingness to communicate internal control and ethics concerns for fear of having personal repercussions if the information is leaked to the wrong person. We also noted that the organization does not have a method in place for employees to safely, and anonymously report suspicious activity occurring inside the organization. We recommend that a whistleblower hotline service be utilized so that employees feel comfortable reporting issues in a safe and anonymous manner. Using a third party vendor for this service will help improve the likelihood of anonymity and employee's perceived safety.

Management's Response – Roger Gray, General Manager : This finding and recommendation is one that is both complex in conclusion and possible solutions. Unlike a "simple" procedural finding that can be fixed with straight-forward policy or system changes this one is a matter of culture and both reality and perception. At a starting point, we believe that the finding is somewhat overstated in terms of EWEB not having a method in place to safely and anonymously report suspicious activity. The question about whether anonymity is necessary for safety is one that is open to opinion and perspective. EWEB does have policies and management does promote and reinforce that there are options to report concerns of any kind. The most effective organizational culture is one that reinforces open communication and feedback. Safety is also promoted by policy and practice through clear policies against retaliation and such. Whistleblower hotlines that lean in to anonymity may promote certain kinds of "safety" but they also can create other organizational issues that are counter to an organizational culture that is open to feedback.

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Anonymous tools recommended by Moss Adams such as a whistleblower hotline can help protect anonymity, but there are a variety of pros and cons associated with such an approach. Some members of EWEB Management have past experience with such tools and understand these pros and cons and will explore possible adoption of a hotline. As a preliminary response, perhaps the most significant "pro" of a hotline is the anonymity of the hotline to protect the "safety" of the person making a complaint or allegation. However, that "pro" can also be a significant "con" in that the anonymity of hotline can be potentially abused by the launching of false complaints or allegations against others. EWEB has a responsibility to promote and protect the "safety" of accuser and accused in these matters. Whistleblower hotlines clearly protect accusers by preserving anonymity. However, the safety of accused can be jeopardized by such methods. This particular issue regarding protection of accuser and accused is so important that the 6th Amendment of the U.S. Constitution even addresses it. While EWEB clearly does not try civil or criminal cases, we must manage various human resource matters that pertain to allegations and complaints that involve accusers and accused.

Again, the implementation of an anonymous whistleblower hotline is something that merits exploration. There may be an appropriate opportunity for EWEB to utilize a hotline or online reporting system. However, prior to the implementation of any such system, there is foundational and cultural work that must be done. Additionally, EWEB Management believes there are several other logical steps to be taken prior to final consideration or adoption of a hotline.

At present, EWEB's Open Communications Policy was recently amended (prior to this audit finding) to better address the matter of surfacing employee concerns and protecting employee safety. While the policy encourages employees to file complaints through internal means, it does offer the option to report complaints directly to outside agencies (e.g Oregon Ethics Commission). In some respects, EWEB already has a form of an outside option although not a "whistleblower" hotline per se. Clearly, there is the opportunity to strengthen the language with respect to these outside avenues and specifically regarding reports of ethics violations, fraud or malfeasance. To that end, the policy will be revisited and revised appropriately. In addition to policy review, EWEB will also improve communication, awareness and training on this important matter.

The policy information will be communicated through various channels across the organization. Obviously, EWEB's internal process or that of filing a complaint with the appropriate outside body does not provide the option of anonymity. While not anonymous, these processes are strictly confidential and there are public agencies in place to receive and investigate complaints including the Bureau of Labor and Industries, the Oregon Government Ethics Commission and the Equal Employment Opportunity Commission, for example.

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EWEB recognizes the element of anonymity may be a critical factor that enables an individual to report concerns when otherwise they may not. Another critical factor for any complaint filing process – anonymous or otherwise - is the need for awareness and understanding surrounding public ethics, malfeasance and internal controls. Without this understanding, the purpose of an anonymous reporting system could be misunderstood and could become a vehicle for disgruntled employees to report complaints that do not begin to rise to level of those an anonymous system is designed to address. At this writing, there has been little training for EWEB managers, supervisors and the general workforce. Education on these topics will go far to enable employees to recognize potential violations and strengthen their confidence to report concerns. Some training is planned for 2013 and there is work under way to introduce new employees to their obligations as public employees at the time of their hire and orientation to EWEB.

Beyond understanding the concepts and requirements that support ethical conduct, EWEB's workforce would have to be educated about EWEB's legitimate intent surrounding such a system. An anonymous reporting system might be met with suspicion and be viewed as EWEB's attempt to encourage employees to spy on each other. This is particularly important considering EWEB's present employee culture which is challenged by organizational change, limited financial resources, recent staff reductions and the fear that future reductions may occur. Union organization efforts are underway and employees are being asked to work harder and at times, take on new and unfamiliar work. These are all conditions that escalate stress, dissatisfaction and understandable apprehension in employees to surface concerns.

EWEB acknowledges that anonymous whistleblower reporting systems offer protections to the complainant. A hurdle for EWEB that must be addressed as we investigate such a system is that as a relatively small employer, the cover of anonymity is often diminished as complaints are investigated.

Clearly EWEB has opportunities to strengthen its processes with regard to complaint reporting and to raise awareness and create a sense of responsibility for reporting misconduct or irregularities in internal controls. The implementation of an anonymous reporting system is one of several avenues that should be contemplated; however, EWEB Management believes that the steps and plans articulated above (i.e. policy reviews, improved training, communication and awareness and clear outside options for complaints and allegations) are logical first steps. Management will monitor this issue and if similar "tone" issues arise in the audit next year, then Management would consider a hotline as a possible logical next step. Management does not believe that a hotline is the logical first step.

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Mid-year update – Roger Gray, General Manager : As stated in our response to the auditor recommendation, EWEB Management committed to several improvements to address the underlying issues that drove this recommendation.   Here is what has been accomplished in the past several months:

1) EWEB Management updated, refined and improved its Internal Dispute Resolution and Whistleblower policy. http://intranet.ewebnetwork.net/HR/Policies/Images/June%202013/DisputeResolutionWhistleblowingHRSubcommitteeEdits0613.pdf   Among other things, the policy addresses the importance of raising issues and provides specific internal and external resources for any employee to effectively raise issues.   The policy even provides a "flow chart" of where to go depending on the nature of the issue an employee might have (e.g. safety, ethics, other).
2) The policy reaffirms that retaliation against an employee reporting an issue is strictly prohibited.
3) Senior Management (GM and Leadership Team), have required mandatory training and attendance on the revised policies and ethics in general for all managers, supervisors and leads. This initial training is nearly complete with some follow-up necessary due to vacations.
4) The General Manager is reinforcing "tone at the top" about the importance of ethics and all decisions and actions by EWEB.
5) Senior Management (GM and Leadership Team) have adopted a regular "ethics moment" agenda item as part of the LT agenda to reinforce tone at the top.
6) Employee surveys that will be conducted later in 2013 will attempt to assess this area and compare to past baseline data.
7) Depending on survey data, the 2013 audit finding and other factors, Senior Management will assess the situation again in early 2014 to determine if the additional policies and practices are improving or not. Depending on that assessment, Senior Management will then assess whether any further steps, up to and including a whistleblower hotline, are necessary.

EWEB Credit Cards
During our discussions with EWEB personnel and through review of credit card statements, we noted one case in which a supervisor was using an employee's credit card to make purchases, and then approving that employee's credit card statement. We recommend that each employee's credit card be used only for purchases made by that specific employee, as required by current policy, and that a supervisor or manager review and approve the charges before being submitted for payment. Any purchases should also be made by the appropriate personnel and go through the normal process to ensure compliance with EWEB policy.

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> ***Management's Response – Todd Simmons, Electric T&D Operations Manager:***
> Management has investigated the credit card activity and will put appropriate measures in place that ensure compliance with policies for use of purchase cards, as well as purchasing laws and policies and ethics standards.

> ***Mid-year update – Todd Simmons, Electric T&D Operations Manager:*** All invoices paid with credit cards that are required to be paid with purchase orders have been corrected and supervisors needing additional assistance have received Technical Assistant or Utility Coordinator support to develop purchasing plans consistent with all EWEB policies. All credit card reconciliation reports generated by assistants and coordinators are approved by direct supervisors and the manager.

Customer Service Billing System

Customer Adjustments Report
During our review of the controls surrounding customer adjustments and review of those adjustments, we noted that a listing of customer adjustments is run on a monthly basis and reviewed by someone other than the person making the adjustments. However, we noted that the listing was large and contained much more information than is needed to verify adjustments. The person reviewing the listing stated that she is not able to thoroughly review all the adjustments to determine that they were appropriate and booked by authorized personnel. In addition, we noted that any adjustments recorded by the City of Eugene are not reviewed during this process. We recommend that the format and parameters used to run the adjustments report be revisited to ensure that a more streamlined user-friendly report is produced that can be reviewed in a more efficient and effective manner. We also recommend that the review of the adjustments report include the City of Eugene adjustments to ensure that they are appropriate and restricted to the sewer portion only.

> ***Management's Response – Mark Freeman, Customer Service and EMS Manager:***
> The "Customer Adjustment Report" is a CIS-generated report and as such, is not alterable for EWEB's specific needs. A separate report was created to include User ID information and to remove unnecessary data, however the critical adjustment data (CIS notes) needed to validate adjustments cannot be captured in an electronic report and must be reviewed manually, which recent staffing reductions no longer consistently permit.
>
> - EWEB will dedicate staff to consistently monitor the report(s), however this may necessitate an FTE increase as manual review is time-consuming even with random, spot checking.

11

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- EWEB cannot determine the validity of adjustments made to its CIS by the COE. EWEB will re-train COE employees on appropriate documentation of adjustments that COE makes to EWEB's billing system. EWEB will monitor and forward a further refined COE adjustment report to COE for its review and internal control implementation. EWEB will continue to monitor report(s) for COE adjustments by service to ensure only sewer and wastewater adjustments are processed by COE.

Mid-year update – Mark Freeman, Customer Service and EMS Manager:
Completed July 2013 – this report is now in an electronic format for easier, more effective and efficient (streamlined with no extraneous data, user-friendly and sortable) review and is randomly audited monthly by an employee in a separate CS department with less time constraint. The electronic format also allows EWEB to segregate the City of Eugene adjustments for separate review by the City (as EWEB has no way to determine if the City's adjustments are accurate or not).

Customer Adjustments Policy
During our review of the process used to record adjustments, we noted that although a policy for recording adjustments is present, it is not followed on a consistent basis and therefore adjustments are not reviewed and approved prior to being recorded. We also noted that the policy does not include provisions for the dollar thresholds that each employee is allowed to record. We recommend that management update the policy to incorporate provisions for which employee positions are allowed to record adjustments. The policy should also establish thresholds for the amounts that each position can record and should also specify who is authorized to review and approve those adjustments prior to being recorded. These provisions should be implemented such that adjustments, over a specified dollar threshold, are prepared and approved by separate individuals to ensure the appropriate segregation of duties.

Management's Response - Mark Freeman, Customer Service & EMS Manager:
EWEB does not have a "Customer Adjustments Policy". Customer Service departments developed and now use a "Conflict of Interest Statement" which is annually covered and documented with all CS staff. Current CIS does not provide functionality for dollar thresholds or caps on adjustment processing.

- The "Conflict of Interest" statement will be widened to include all EWEB staff, and used for annual EWEB documented coverage of staff. The statement covers items such as: no access of employee's own, friends', or relatives' accounts, no discussion of customer accounts outside of workplace, etc.

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- Reiterate that all consumption adjustments must be done via Billing Control, however non-consumption adjustments can be processed by designated staff

- Explore subsequent versions of CIS to see if dollar thresholds or caps become functional, or ensure that such functionality exists in any subsequent acquisition of a different CIS.

- Continue to monitor reports to verify compliance with above.

Mid-year update – Mark Freeman, Customer Service and EMS Manager: Compliance with the customer adjustments policy is further controlled by the results of the Customer Adjustment Access Control changes noted above.

Work Order and Asset Management

Work Order Documentation Consistency
During our review of work orders, we noted that the documentation maintained to explain and support the reason for significant variances from budget / estimate differs significantly from job coordinator to job coordinator. Often, no documentation exists in the job packets to explain the reason for significant variances from budget / estimate, and only limited comments in the Work Tracking system are maintained to explain variances at the project level. As a best practice, we recommend working with the job coordinators to develop a close out sheet to document when the work was completed and why the job was over / under budget (if applicable). It may be helpful to set a threshold for when these controls need to be applied as not all jobs require this detailed level of monitoring.

Management's Response – Mel Damewood, Engineering Manager: The Engineering Department, which manages most capital improvement projects that generate work orders, is refining our project management processes to attain consistency between business units (generation, electric, water, telecom, etc.). As part of this refinement, standardization of forms linking financial management and controls will be developed; including authorization, change controls, and close-out accountability. Initially, both internally-driven and customer-driven jobs of $50,000 and more will be included in this process, which is scheduled for implementation by July 1, 2013.

Mid-year update – Mel Damewood, Engineering Manager: The recommended documentation for projects over $50,000 has been implemented and well be addressed for al projects initiated in 2013.

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Other Matters

Water Department Exception Reporting
During our walkthrough of exception/validity reports, we determined that the water department does not review the listing of zero-read meters. We did note that the billing department runs a zero-read report for the water department (approximately monthly). However, we believe the best practice recommendation below would improve the controls in this area and make them consistent with the practices of the electric department. As a best practice, the zero-read exception report should be run by the water department on at least a weekly basis similar to the treatment of zero reads for the electric department.

Management's Response – Brad Taylor, Water T&D Acting in Charge Manager: Water Operations spent much of 2012 improving our processes and have recently completed a change in reporting exceptions, including zero consumption reporting. We are prepared, and will implement immediately running the zero consumption report on a weekly basis. Water Operations, specifically Water Distribution Services, will adjust its work load and scheduling to accommodate this work.

Mid-year update – Brad Taylor, Water T&D Manager: Initially over 3000 entries made up the "Zero Consumption" report that was generated monthly automatically. A new zero report was designed and implemented. The new report allows for a greater level of manipulation and reporting. We now have a process to remove entries off the list after a final determination has been made (stuck, vacant lot, snow bird etc.). We started the field work with approximately 1300 entries and quickly worked through 1000. We currently have less than 200 remaining from the initial list; we will have this done by the end of July 2013. Of those sites visited, very few were actually stuck (5%). Along with the new report, we have implemented a new procedure that will help us manage this work in the future.

Information Technology Matters

IT Financial Statement Active Directory
During the IT examination, a user extract of the Active Directory (AD) was compared against a listing of current employees. This comparison identified numerous AD accounts for persons not included on the current employee list. It was also noted that EWEB does not conduct formal access reviews on a regular basis. The goal of these reviews would be twofold: 1- to ensure that accounts for terminated employees have been disabled, and 2- to ensure that permissions and access rights are appropriate for each user's job responsibilities, and that the systems are configured to help ensure proper segregation of duties. It is recommended that EWEB distribute user listings to managers to verify the access rights of direct reports. This should happen at least annually, and it is recommended this be conducted semi-annually.

Management's Response – Matt Sayre, Information Technology Manager: There were five accounts identified that had not been removed from AD, however we believe these accounts had been disabled in the Novell environment, therefore access to the network would have been denied. We do see an opportunity to improve this process; see Management response in IT Other Matters below.

EWEB has recently allocated staffing resources to focus on the Audit function specifically in the domain of Cyber Security. As part of the scope of responsibility of the Cyber Security roll, AD account reviews will be conducted at least annually. Our Cyber Security Position Descriptions are currently being updated and will list that responsibility explicitly.

Mid-year update – Matt Sayre, Information Technology Manager: This work is on track to be completed in 2013.

IT Opportunities for Potential Business Process Improvement – Access Management
Discussion of the access management process included identification of some control improvements resulting from the HRIS implementation. Specifically, the system will send notifications to appropriate personnel regarding new hires and separations. From an access management perspective, this is efficient in ensuring that access is authorized and approved for new hires and access is disabled for terminations. Even though the new process has been in place for some time, the process documentation related to access management has not been updated to reflect the new process. EWEB has activated a task force that meets weekly to facilitate the project to review and update policy/procedure documentation. It is recommended that the materials related to access management be reviewed and updated as needed.

> ***Management's Response – Matt Sayre, Information Technology Manager:*** EWEB's IS Policy and Procedure Task force will update the Internal Controls Procedures for organizational review by Q3 2013

> ***Mid-year update – Matt Sayre, Information Technology Manager:*** This work is on track to be completed in 2013.

IT Other Matters
Access Management around Re-org/Reduction in Force: There was some concern over the re-organization activities that occurred during July 2012. Through inquiry and observation of tracking spreadsheets the following was noted:

    i. During the re-org, service desk tickets were created for all changed roles
    ii. In addition, a spreadsheet was prepared that listed all changes including lay-offs to ensure that access was managed appropriately

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Potential Issues: Given the active accounts noted for users not on the current employee list and the lack of formal reviews, it is possible that there may be some access rights that have not been managed appropriately. This risk is low given the effort put into planning the re-organization.

> ***Management's Response – Matt Sayre, Information Technology Manager:*** Access management will be automated via Service Desk workflows in 2013. We will model a corporate policy after our compliance process where, when notified of role changes, access rights are reviewed. See Management responses above in IT Opportunities for Potential Business Process Improvement – Access Management and IT Financial Statement Active Directory.

> ***Mid-year update – Matt Sayre, Information Technology Manager:*** This work is on track to be completed in 2013.

Prior Year Matters

> ***Federal Grant Management***
> Through our inquiries of management, we noted that no EWEB employee is currently responsible for managing all federal grant activity. While an additional FTE may not be appropriate at this point given the level of federal grant activity, it may be helpful to identify someone currently within the organization who could take on this task. The employee in charge of this process could ensure compliance with federal grant requirements and also track all of the grant activity for administrative and accounting purposes. We recommend that EWEB consider identifying an individual within the utility to take ownership of this task.

>> ***2012 Update:*** Management has identified staff to monitor grant activity and is in the process of training staff in this area. We believe management has appropriately addressed this prior year comment.

>> ***2013 Update– Cathy Bloom, Financial Services Manager:*** A draft grant policy has been prepared and during the course of the audit, grant activity was summarized and subjected to audit procedures. Staff identified for specialized training will receive training during 2013.

>> ***Mid-year update– Susan Eicher, General Accounting and Treasury Supervisor:*** Specialized Staff training has been completed and grant policy development is in process.

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Prior Year IT Matters

Although there were no new IT issues identified within the 2011 Communication to Those Charged with Governance, the following IT matters were noted as repeat comments in 2011 as they had not been satisfactorily addressed and cleared. We have included 2012 updates for each of these such IT comments below.

IT Opportunities for Potential Business Process Improvement - Network

It was reported that EWEB still maintains two distinct core network operating systems- Novell and Windows AD network operating systems. The organization has not completely migrated off of the Novell system and sets up user accounts in both domain controllers. Users login utilizing Novell which passes the credentials on to AD, where Outlook has replaced GroupWise as the email system. This situation requires the maintenance of multiple systems that do the same thing, but also poses risks when it comes to terminating users. Also, it was reported that password settings for the Novell operating system are somewhat weak, requiring only six characters minimum, no strength characteristics, and change every six months. It is recommended that the organization phase Novell out completely if there is not a strong argument to keep it, and that Active Directory group policy be used to enforce stronger password requirements. Best practices typically include 8-character minimums, strength characteristics pertaining to case or special characters, the forced change of passwords at initial login and every 90 days, and the maintenance of password history so that users cannot re-use prior passwords. In addition, access review processes should be examined to ensure that all systems where active user accounts had been created are addressed.

> **2012 Update:** A project listed on the current project listing for IT has been defined to retire Novell, but the project has not yet been completed. In addition, it was also noted that the current Active Directory group policy related to password configurations does not require a minimum age for passwords. It is recommended that EWEB modify this setting to require passwords to be used for a minimum period of time once the Novel retirement project has been completed. Otherwise, when prompted to change their passwords every 110 days, users could simply change their password repeatedly until they are able to use the same password again. While this scenario is not likely, the possibility that users can circumvent the forced password change still exists.

> **2013 Update – Matt Sayre, Information Technology Manager:** A project listed on the current project portfolio for IT to retire Novell is in-progress. The Novell project is scheduled to complete Q2 2013.

> **Mid-year update – Matt Sayre, Information Services Manager:** The Novell project was completed; EWEB is now standardized on Windows Active Directory.

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IT Opportunities for Potential Business Process Improvement – Electronic Commerce Transactions

EWEB processes electronic commerce transactions over the Internet. However, a recent project was completed to outsource the Electronic Bill Payments to a third-party. This will allow EWEB to offload significant risk associated with a bulk of the card transactions. However, there are still credit card transactions that EWEB manages directly themselves, particularly at the customer service center. Processing even a few credit card transactions exposes EWEB to the compliance requirements from the Payment Card Industry (PCI) Data Security Standards (DSS).

> ***2012 Update:*** Per inquiry with the IT Manager and review of the current project listing, PCI compliance has been defined as a project goal and is underway. It is recommended that EWEB continue with this process to identify all processes and functions wherein EWEB handles credit/debit card data of customers.

> ***2013 Update– Matt Sayre, Information Technology Manager::***EWEB will be PCI compliant or remove the need to be PCI compliant by 12/31/13.

> ***Mid-year update – Matt Sayre, Information Technology Manager:*** This work is on track to be completed in 2013.

Disaster Recovery Plan

In the current year, a more robust disaster recovery plan was developed and implemented. Management identified critical systems and have determined an off-site backup that is updated depending on the need of the individual system. We have reviewed this plan noting that critical systems and their frequency of back-up is reasonable.

Management's responses to the recommendations on other matters have not been subjected to auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on them.

This communication is intended solely for the use of the Board and members of management and is not intended to be and should not be used by anyone other than these specified parties. We look forward to discussing our report or any other matters of interest with you at the meeting.

Sincerely,

Portland, Oregon
February 22, 2013