

East Bay Charter Township

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2007 Audit

Report to the Board

Plante and Moran

Response from Management

**East Bay Township Internal changes/progress in response to the auditor's report
on internal control issues for audit year ended 2007:**

Auditor's Notes:

1) Bank Reconciliations:

Auditor Issue: Bank reconciliation's are not prepared on a timely basis.

Auditor Recommendation: Prepare bank reconciliation on a timely basis, signed by responsible parties and copies given to the board.

East Bay Township internal response/change –

An Accountant was hired in February, 2008 who is proficient at completing bank reconciliations. Bank reconciliations are now being completed by the end of the month for the month prior. The reconciliations are also being signed by both Clerk and Treasurer and given to the board monthly.

2) Cash Processing:

Auditor Issue: There is no separation of duties from the Treasurer as she has the ability to accept money, receipt it into the system, make journal entries and prepare the bank reconciliations.

Auditor Recommendation: Remove the Treasurer's ability to perform one of the above functions and improve controls for cash.

East Bay Township internal response/change –

The Treasurer no longer completes the bank reconciliations. The Treasurer and the Deputy Treasurer no longer have the ability to make journal entries through the Cash Receipt software. The journal entries are now written up on a form with the appropriate backup attached and given to the Clerk's office for input into the general ledger. All journal entries are reviewed by the Clerk, Treasurer and Supervisor.

3) Fund Classification of Bonds

Auditor Issue: Incorrect recording of bonds

Auditor Recommendation: None

East Bay Township internal response/change –

Treasurer will review the detailed spreadsheet quarterly to ensure detail ties to the trial balance.

**East Bay Township Internal changes/progress in response to the auditor's report
on internal control issues for audit year ended 2007:**

4) Wire Transfer Access:

Auditor Issue: The Treasurer has the ability to initiate a wire transfer and add a new transferee. This access allows for potential misappropriation of Township funds.

Auditor Recommendation: Limit wire transfers to pre-approved vendors. Changes/additions should be approved by a second account signer or by the Township board.

East Bay Township internal response/change –

A change has been put in place with the bank to have dual control on all wire transfers. The Treasurer's office will initiate the transfer request and the clerk's office will perform a secondary approval.

5) Special Assessments:

Auditor Issue: Special Assessment general ledger did not reconcile to the detail listing.

Auditor Recommendation: Receivable balances be adjusted on a regular basis to reflect cash receipts as they are collected and balances compared to the property tax software (BS&A) on a regular basis.

East Bay Township internal response/change –

Further understanding occurred during the 2007 audit from the Treasurer as to the entries needed for special assessment. The Treasurer and the Accountant are in the process of setting up procedures to monitor these cash receipts and ensure the general ledger, the listing, the spreadsheets and the special assessment software all balance. These procedures will be performed quarterly and in a timely fashion after year end to ensure accuracy prior to the audit.

**East Bay Township Internal comments/progress in response to Audit
Adjustments for year ended 2007 (original report from Auditor's attached):**

Water and Sewer Revenue & Expenditures –

Adjustments were made internally for the first time prior to the auditors visit. Education has occurred during the 2007 audit to ensure understanding for accurate internal adjustments going forward. One of the reasons the dollar amount was larger was due to a glitch in the billing of the DPW Sewer and Water usage for Sept & Oct. of 2007.

Posting of 2006 Audit Adjustments –

Year end financial statements post audit and audit adjustments will be checked to ensure that all adjustments provided by the auditors have been posted to the East Bay Township accounting system and posted correctly.

Depreciation –

The depreciation schedule has been updated for 2008 and checked for accuracy by our Accountant. Entries have been posted monthly into the accounting software for 2008 depreciation expense. Yearly additions of assets will be added accordingly and all entries posted and spreadsheets completed prior to future years audit fieldwork.

Septage Treatment Facility –

East Bay is now educated as to the Septage Treatment Facility and the impact this has on East Bay Township and it's financials and will make necessary entries as needed.

SUMMARY:

Out of the 19 audit adjustments, 11 of them had analysis completed internally but were not posted in a timely fashion. There has been good education and learning from the Clerk and the Treasurer during the 2007 audit and these internal adjustments will be completed prior to the audit going forward.

The Clerk, Supervisor, Treasurer and Accountant will meet quarterly and review in detail the trial balance and look at all financial accounts. They will also tie out the spreadsheets to the activity that occurred and ensure that items are corrected on a timely basis.

The Accountant was not able to help with items other than catching up bank reconciliations prior to the 2007 audit but going forward will work with the Clerk and the Treasurer to ensure that all end of the year entries are processed timely and accurately. It is the intention to be ready for the audit in late February or early March.

Please feel free to discuss any of the above issues with the Clerk or Treasurer. It is our intention and desire to continue to improve processes and efficiency at East Bay Charter Township

Glen Lile, Supervisor

Tracey Bartlett, Treasurer

Sue Courtade, Clerk

Kymerly Judge, CPA Accountant 

FROM AUDITOR'S REPORT

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control. We believe that the following deficiencies constitute material weaknesses.

Audit Adjustments

During the course of the audit, Plante & Moran suggested audit adjustments in the following areas:

- *Water and Sewer Revenue and Expenditures* - The Township made correcting adjustments in May 2008 for business activities relating to special assessments and water and sewer revenues and expenditures for the year ended December 31, 2007. The total adjustment resulted in gross adjustments of \$209,570 to revenue and expenditures. Accounts receivable for business-type activities were increased by \$101,369.
- *Posting of 2006 Audit Adjustments* - The Township did not record two prior year audit adjustments for business-type activities. This produced an adjustment to increase the fund balance in the current year by \$371,012.
- *Depreciation* - In 2007, depreciation had not been recorded in a timely manner for business-type activities. The adjustment for depreciation at year end created an additional expense and accumulated depreciation of \$361,617. Depreciation should be recorded on a monthly basis. In addition, a prior period adjustment was recorded for \$90,099 to correct depreciation expense on the governmental capital assets for an error in the calculation in prior years.
- *Septage Treatment Facility* - In 2003, the Township entered into a contract with Grand Traverse County and four other townships to construct a septage treatment facility. The Township's participation rate was set at 30.75 percent. At the same time, the County issued debt of \$6.5 million, of which the Township guaranteed \$1,998,750. In 2004, the County issued additional debt of \$1.3 million, of which the Township guaranteed \$399,750. The first principal payment on these bonds was paid in November 2005 with unspent bond proceeds and revenues from operations held at the County. The Township was not required to make a direct payment at that time. However, in 2006 and 2007, all five townships jointly borrowed \$438,044 (\$134,699 for East Bay Township) from Grand Traverse County to pay the second and third debt service payments. The Township did not record this activity on its general ledger or in the financial statements because there had not been any cash outlay directly from the Township. This resulted in a significant audit adjustment at year end to the Water and Sewer Fund classified as a prior period adjustment.
- Overall, the audit resulted in 19 journal entries to adjust Township balances as of December 31, 2007. A majority of the journal entries were accrual/balance sheet type entries that may not be submitted to the board for review during the course of the year.

East Bay Township Internal changes/progress in response to the auditor's report on significant deficiencies and control deficiencies for audit year ended 2006:

The letter from the Auditor's dated April 17, 2007 is attached for reference.

Auditor's Notes:

Significant Deficiencies

1) Bank Reconciliations:

Auditor Issue: Bank reconciliation's are not prepared on a timely basis.

Auditor Recommendation: Prepare bank reconciliation on a timely basis, signed by responsible parties and copies given to the board. Adjustments to be made dated to the appropriate month and done on a timely basis.

East Bay Township internal response/change – An Accountant was hired in February, 2008 who is proficient at completing bank reconciliations. Bank reconciliations are now being completed by the end of the month for the month prior. The reconciliations are also being signed by both Clerk and Treasurer and given to the board monthly. Adjustments are prepared with appropriate support and given to the Clerk for input on a timely basis and verified via the bank reconciliations.

2) Property Tax Activity:

Auditor Issue: Fund Balance was not being used for the Property Tax collection.

Auditor Recommendation: The treasurer enters all property tax information into the Fund Balance software and performs the monthly bank reconciliation on a timely basis.

East Bay Township internal response/change - The treasurer started utilizing the Fund Balance software in June of 2006 and has the monthly bank reconciliations are being done by the accountant on a timely basis.

3) Special Assessments :

Auditor Issue: Unable to form an opinion of the Special Assessments due to the balances not being correct for a number of years.

Auditor Recommendation: The receivable balances be adjusted on a regular basis to reflect cash receipts as they are collected and balances be compared to the property tax software (BS&A) on a regular basis monthly or at least quarterly.

East Bay Township internal response/change - The treasurer has continued to learn the Special Assessment/Fund Balance process and make the appropriate corrections. During the 2007 Audit fieldwork we became aware of another feature of the Special Assessments and how we were tracking

them for the yearend adjustment and made the appropriate adjustments. The treasurer and the accountant are working on putting in place procedures to tie the Special Assessment software to the Fund Balance on a quarterly basis.

4) Journal Entries:

Auditor Issue: Supervisory review of journal entry was not being preformed and the supporting documentation was inadequate.

Auditor Recommendation: That a master journal entry form be used and include support for journal entries in addition to documenting a preparer and a reviewer with periodic review by the supervisor.

East Bay Township internal response/change - Starting in July 2007 the Clerk, Treasurer and Supervisor review and initialed all journal entries.

5) Accounts Payable:

Auditor Issue: Checks issued in 2007 for the 2006 year end were not adjusted correctly.

Auditor Recommendation: Maintain the listing of expenses that come in after year end but relate to the prior year (with expenditure accounts), to produce a manual accounts payable journal entry to record at December 31. This entry would then be immediately reversed as of January 1.

East Bay Township internal response/change: Clerk worked with Fund balance software representative to address this issue for year end. All expenses that are presented for end of year after December 31 are entered as December 31 issued. All Purchase Order/invoices are marked with the actual year of service. Such as 2007 expense on an item invoiced January 2008. The clerk maintains a file of these invoices and keeps a spreadsheet of all activity.

Control Deficiencies

Debit Activity:

Yearend tie out and adjustments for 2007 were completed during the fieldwork for the audit. This was the first full year that the township was able to do this. During the process we gained a deeper understanding of how the Special Assessment software works and how that related to the Fund Balance software and were able to make appropriate adjustments. The treasurer and accountant are working on a procedure to best handle the collection and payment of the special assessments and bonds.

Bank Reconciliation Differences:

The adjustments are being done on a timely basis during the bank reconciliation process.

Capital Asset Schedule:

Auditor issue: The Township relies on the Auditors to update the capital asset schedules and calculate depreciation expense.

Auditor Recommendations: The Township should consider having the Clerk attend training in order to take over these responsibilities.

East Bay Township internal response/change: The Clerk and the Accountant prepared these documents for the 2007 year end before the field audit began. As of 2008 the Clerk is recording depreciation monthly. Capital Assets will be recorded as new assets are acquired.

Other Items

Budgets:

There were journal entries done to correct the 2006 bond payments. The 2007 budget only reflected the interest payment.

Bank Accounts for Cash:

In December of 2006 we separated the T & A Escrow and the Roads and Lites into a one checking account.

Board Communications:

The board started receiving the Balance Sheet and Income Statement in July 2007 this was in addition to the Revenue and Expense Report.

Board Minutes:

The recording secretary is documenting the actions of the board meetings along with the motions. The review of the minutes is done by the Clerk and then presented to the board for review. If there are any discrepancies, they can be addressed before the meeting and recommended for amending.

IPS Submission of Payroll Information:

The Clerk and Treasurer's office implemented a sign off review of payroll records with the Clerk's office inputting the information off of time sheets and the Treasurer's office reviewing these reports before faxing the reports to IPS. As of 2008, the Township has begun the online input entry of Payroll. The Clerk's office inputs the information and releases it to the Treasurer's office for review and submission to IPS.

April 17, 2007

To the Township Board
Charter Township of East Bay

In planning and performing our audit of the financial statements of Charter Township of East Bay as of and for the year ended December 31, 2006, in accordance with auditing standards generally accepted in the United States of America, we considered the Township'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 Township's internal control. Accordingly, we do not express an opinion on the effectiveness of the Township's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control that we consider to be significant deficiencies and other deficiencies that we consider to be material weaknesses.

A control deficiency 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 misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control. We believe that the following deficiency constitutes a material weakness:

Audit Adjustments - The audit resulted in 25 journal entries posted to adjust the Township's balances as of December 31, 2006. A majority of the journal entries were accrual/balance sheet type entries that may not be submitted to the board for review during the course of the year. Most significantly changed were the Water and Sewer Funds from an unadjusted net income of \$1,443,379 to net income of \$1,825,235. We recommend the Township consider allowing the clerk and the treasurer (those with general ledger responsibilities) to obtain additional training in order to understand the accounting required to fulfill the duties of the elected position.

We consider the following deficiencies to be significant deficiencies in internal control:

Bank Reconciliations - Bank reconciliations after June 2006 were not prepared on a timely basis due to the complexity of the cash accounts (in relation to the number of general ledger accounts included in each cash bank account and having most disbursements run through the General Fund with a duplicate reversing entry to move amounts to the appropriate fund). Bank reconciliations are required to be completed on a timely basis to provide accurate cash information for management to use in making decisions. The board is receiving a copy of the bank reconciliation and the bank statements when completed.

We recommend that a timely bank reconciliation is prepared. The treasurer should post adjustments from the bank statement (interest income and credit card deposits) back to the period it relates to - along with all other adjustments as of the end of the month being reconciled. To document timely preparation, we recommend the Township utilize the sign-off/date procedure for both the preparer and reviewer of the bank reconciliations

Property Tax Activity - During cash receipt testing, we noted that property taxes collected in the property tax receiving cash account were not recorded completely in the general ledger. In prior years, these transactions were not entered in the Fund Balance software; however, efforts have been made to enter this activity in 2006. As a result, the current treasurer was not able to reconcile this cash account to the general ledger. The property tax software (BS&A) does track cash received for property taxes and produces the amounts due to taxing authorities. We noted that all taxing authorities were paid accordingly regardless of the information being excluded from the Fund Balance software. We recommend the treasurer continue to enter all property tax information into the Fund Balance software and perform the monthly bank reconciliation timely.

Special Assessments - In 2006, a detailed listing of special assessment balances by parcel number was provided to us. However, the special assessment receivable general ledger balances did not reconcile to the detailed listing until an adjustment was made during audit fieldwork. This produced an adjustment of \$13,685 in additional revenue for the Water and Sewer Funds, due to the receivable balances not being correct for a number of years, which resulted in prior period scope limitations on the audit. As a result of the review performed by the new treasurer, these balances were identified as correct and we were able to test accordingly. In order to maintain accurate records, we recommend these receivable balances be adjusted on a regular basis to reflect cash receipts as they are collected and balances be compared to the property tax software (BS&A) on a regular basis, monthly, or at least quarterly.

Journal Entries - We noted that a supervisory review of journal entry support for reasonableness was not being performed during 2006. While the Township is now keeping some documentation for recorded journal entries, the available documentation is not adequate. For instance, there was a reclassification from the General Fund to the Agency Fund with the only documentation being a copy of the entry itself. We also noted that manual journal entries can select any type of source journal from a drop-down box when inputting into Fund Balance software and that the treasurer can post cash-related journal entries into the Fund Balance software.

Monthly revenue and expense reports are given to the board, who can identify significant changes and question them. However, a review of journal entries with adequate support is essential for strong internal controls. We recommend that the master journal entry form include support for journal entries in addition to documenting a preparer and a reviewer. As an additional control, we recommend a periodic review by the supervisor of all journal entries posted, looking at the reasonableness of the entry and who posted it.

Accounts Payable - The accounts payable general ledger balance was not accurate as of December 31, 2006 at the beginning of fieldwork. This was due primarily to checks issued during 2007 that related to 2006 expenses that were backdated in the system to reflect the expenditure in the proper period. As a result, cash and accounts payable were improperly reduced as of December 31, 2006 for the backdated checks. We obtained a listing of the backdated checks and adjusted both cash and AP to reflect the actual balances as of year end. For future year ends, we recommend the clerk maintain the listing of expenses that come in after year end but relate to the prior year (with expenditure accounts), to produce a manual accounts payable journal entry to record at December 31. This same entry can then be immediately reversed as of January 1. This will produce the correct cash and accounts payable balance effectively as of December 31.

Control Deficiencies

Debt Activity - In 2006, the new treasurer spent time investigating the debt for proper classification between Water and Sewer Funds. As a result, debt was moved to the proper Water and Sewer Funds to reflect more accurate recording of the amounts owed by each fund. This adjustment is to further reflect more accurate information on a per-fund basis. During the year, some bond payments were recorded to offset the liability, but some still were posted to expense. As a result, during the year the balance sheet was misstated. The Township is still working through understanding the difference between an enterprise and a governmental fund. As a result, showing the debt payments as an expense gave the board information on debt payments, even though it was incorrect. The Township has also spent significant time analyzing future debt payments versus cash flows. Overall, this misstatement in the balance sheet has not materially affected the Township's ability to make financial decisions.

We recommend that the treasurer reduce the proper accounts when debt payments are made for the Water and Sewer Bonds and installment purchase agreements. Principal portions should reduce the balance sheet liability accounts and the interest/fees/capacity payments should be recorded as an expense. The board should be provided with a balance sheet as well as a revenue and expense report for proper analysis of the funds at board meetings.

Further, we noted that the special assessment funds are collecting cash to pay for debt. Cash will be recorded in those specific funds and then transferred to the proper Water or Sewer Fund to help pay debt. An alternative would be to close out the specific special assessment funds and record them as line item accounts receivable balances in the respective Water or Sewer Fund.

Bank Reconciliation Differences - There were reconciliation differences maintained month to month on several bank reconciliations. These adjustments reflect errors requiring journal entries to correct the general ledger to accurately reflect cash activity in the bank. We recommend these reconciling amounts be adjusted in a timely manner to prevent future bank reconciliation differences.

Capital Asset Schedule - The Township relies on the auditor to update the capital asset schedule and calculate depreciation expense. The Township provides the additions to the auditor each year. In addition, the Water and Sewer Funds show capital outlay expense for capitalizable projects during the year. Due to the nature of the Water and Sewer Funds being enterprise funds, capital project costs should be capitalized when paid versus expensed. We adjusted these costs out of expense and into capital asset balance sheet accounts as part of the audit. As a result, the statement of activities was misstated during the year, showing inappropriate expenses and omitting depreciation expense. To correct this deficiency, the Township should consider having the clerk attend accounting training in order to take over these types of responsibilities.

Other Items

Budgets - The budget is required to include a beginning fund balance for each fund with a calculated ending fund balance based on the budgeted revenues and expenditures. In addition, a budget cannot reflect a negative (deficit) fund balance.

We also noted that for special assessment funds, the Township budgets for special assessment collections of cash as revenue for Water and Sewer Special Assessment Funds when it should decrease to the special assessment receivable. Bond principal payments for Water and Sewer Funds were also budgeted for as an expenditure when those payments should be decreasing the liability account when paid. The Township should discontinue this practice in the Water and Sewer Funds and only budget for interest payments related to special assessments.

Bank Accounts for Cash - It was noted that there is still a commingling of cash from various funds in the same bank account. For example, the Traverse City State Bank general cash account includes the General Fund, the Township Improvement Fund, and Agency and Lite Fund special assessments (considered agency funds). We recommend the Township continue to assess the cash accounts and related general ledger accounts for appropriate groupings. This could alleviate time spent on reconciliations.

Board Communication - Currently the board is only receiving a revenue and expenditure report for all funds (with budget information included). We recommend the board, at least, be provided a cash summary sheet showing all cash balances by fund at the monthly board meeting. Ideally, a balance sheet would also make sense.

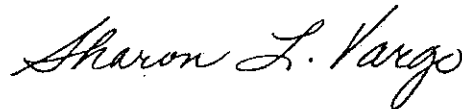
Board Minutes - We noted a large number of board minute edits (i.e., on March 12, 2007, noted edits to the January 8, 2007 minutes). Edits are documented and attached to the board minutes. We recommend the Township make efforts to provide accurate minutes and question why this is happening so frequently.

IPS Submission of Payroll Information - Currently the payroll spreadsheets are faxed to IPS. There may be a more effective and efficient means of communicating this information to IPS. The Township should look into the option of online access to directly input the payroll spreadsheet information. There may also be a feature that lets the clerk enter the information, but doesn't release the information until the treasurer reviews.

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

Very truly yours,

Plante & Moran, PLLC



Sharon Vargo, CPA
Partner