

Schulze, Oswald, Miller & Edwards PC

To: Montmorency County Board of Commissioners, and Management

From: Kristy Schulze, of Schulze Oswald, Miller & Edwards PC

On behalf of our firm, I would like to thank Aprille, Cheri, their respective offices, and the Commissioners for your continued trust in our firm to not only perform the audit but also to try to provide value adding services along the way. We enjoy working in our home county.

Now let's jump right to the heavy stuff.... Page 1, the **Audit Report** itself. As expected, the letter, paraphrased, reads: "In our opinion, based on our audit and the reports of other auditors, the financial statements present fairly, in all material respects, the financial position of Montmorency County as of December 31, 2022...."

This is what the goal is, a clean (unqualified) audit opinion. Note, we do not audit the component units of the county, which are the road commission, the council on aging and the library. We rely on the reports of their auditors for disclosure in the county's full financials.

You'll also notice that the letter is longer than it used to be. The standard audit report letter is now required to list several items that we do as part of our audit procedures. These are the bullet points on page 2.

- ✓ We did propose journal entries to the county's books, as a result of our audit.
The adjustments were routine in nature, and all of them were reviewed and agreed upon with the controller and treasurer. They are already posted to the County's general ledger.
- ✓ The next section of the report is called "**Management's Discussion and Analysis.**" This goes from pg 4-11. This is a narrative of the activity of the County for the fiscal year. While your financial statements in the main section of the report do not present comparatives with the prior year, you can find summarized comparative numbers here in the management's discussion and analysis.
 - These summarized numbers are often much easier to digest than multi-page spreadsheets are, so hopefully you may find these pages useful. There are also several narratives that describe the flow of

information between the two types of financial statements presented within this report, and the differences between them, which we will discuss shortly as well.

- Also, readers will find some financial highlights from the year, some financial analysis information, budgetary references, capital asset information compared to the prior year, and contact information.
- ✓ Next, on page 9 you'll find the **Statement of Net Position**. This is similar to a business's balance sheet, including all "assets, liabilities, and equity." This statement is the *economic resources measurement focus* and includes capital assets and long-term debt but also includes more complicated items such as those relating to net pension liabilities (of which, more detail can be found in note #9-11 which we will talk about in a little bit). A few things I noticed when comparing this to 2021 are:
 - Cash is lower by about \$357K. However, 2021 had the ARPA funds sitting in cash.
 - Most other accounts have a reasonable balance as compared to the prior year.
- ✓ Page 10 is the **Statement of Activities**, which shows the change in Net Position. The goal is to show what programs of the government pay for themselves, and which are subsidized by the general revenues. Of course, this type of statement is much more useful in a large government whose multiple branches of government can pay for themselves. It is not practical for smaller, more rural local governments, but we are held to the same reporting standards as them, so please don't misunderstand all of the bracketed numbers on this page. They are not bad things, but rather just the way the statement is designed. The expenses within this statement include depreciation expense of the county's capital assets, which totaled \$184,642.

The net increase for the overall government was \$329,338 under this method of accounting. This is likely a foreign way for you as a board to look at the county's financials, since it's not the way you budget. It's more of a long-term focus. So, let's move on to the next set of financials.
- ✓ Page 11 is the **Balance Sheet**, shown under the *current financial resources measurement focus*. It shows no capital assets and no long-term debt. The point of this statement is to focus on what is available for use in the next 12 months only. There are two different types of reports to help users understand governmental performance, and you will see the reconciliation of

both on pages 15 and 17. This page may help the reader identify the differences between the two types of reports.

- A notable difference in this year's balance sheet is the ARPA fund. The remainder of the grant was received and all but \$591K was spent as of 12/31/2022.

- ✓ Page 16 is likely the most useful to you, the board. This is the **Statement of Revenues, Expenditures and Changes in Fund Balance**, and It shows a summary of the revenues and expenditures of the governmental funds, coming down to a net increase of \$23,806 across all funds, leaving a positive fund balance of \$3,535,555 across all governmental funds. The general fund itself had a positive change in fund balance of \$318,532 and an ending fund balance of \$2,053,224. When considered fund balance as a percent, the County ended the fiscal year with a 42% fund balance in the general fund. This means fund balance was 42% of the year's expenditures. Another way to look at it is that the County's general fund has just over 5 months of reserve, should all incoming funds stop. For comparison's sake, here are some other local counties' general fund balance percents:
 - Alpena 46%
 - Presque Isle 20%
 - Cheboygan 77%
 - Oscoda 61%
 - Alcona 9%
 - Crawford 19%
 - Roscommon 17%

So that's the good fund balance conversation. The bad part is that the Sheriff's fund ended the year with a negative fund balance of \$42,080. We will talk more about that when we get to the letters at the back.

Pages 18-21 present the budget vs actual of the major governmental funds. The general fund and ARPA fund were within budgetary limits. However the Sheriff's fund spent in excess of budgeted amounts. Again, we will discuss this again when we get to the letters at the back.

- ✓ Pages 22-24 reports on the financial activities of the county's **proprietary funds**. Page 22 reports the balance sheet activity, Page 23 reports the revenues, expenses and changes in net position, and page 24 reports the state of cash flow activity. There was a net increase of \$1,354 across all enterprise funds.

- ✓ Pages 25 and 26: These are the county's fiduciary accounts. This means the county is the trustee for funds held for others. Examples of things running through these accounts are payroll liabilities, benefit deductions and property tax collections for other entities.
- ✓ Pages 27 and 28 report on the County's **component unit's** activity, that of the Road Commission, the Council on Aging and the Library.
- ✓ Pages 29-54 are the **notes to the financial statements**. These notes are required disclosures. They do provide a lot of drilled down detail though. Although we will not go into these in detail, I will draw your attention to a few pages.
 - Please look at page 39. This is nothing new, but in light of recent bank failures, I will draw your attention to the fact that the County has \$2.9M of uninsured bank deposits.
 - If you take a look at page 47, I'll mention a few things that our pension plan auditor noted for me.
 - The MERS Plan had \$977,998 of investment losses this year due to the stock market. Last year, we discussed the gains and mentioned that we would be seeing the opposite effect now. Other factors include service costs, interest expense on the overall liability which was \$1,023,052, change in actuarial assumptions, payments to retirees, and current year contributions. There was an overall increase to the liability of \$1,147,577.
- ✓ The last thing I'd like to point out to you in the notes can be found on page 53. Regarding the information provided on the Landfill, the needed information is never available until the last minute. We will update this page before submitting this to the state.
- ✓ The rest of the bound report is the **combining statements** of the nonmajor funds, of which the detail is summarized in total columns in the statements we've already examined. When you've had an opportunity to look at them in more detail, do let me know if you have any questions.
 - One observation we have is that we urge the County to minimize the number of funds that you have to the legally required minimum number of funds. The State continues to push for this.
 - For example, millages require a separate fund. You really only legally need a general fund and a fund for each millage source

within your governmental funds. Every other governmental fund could be folded into the general fund and the amount transferred over could be assigned or committed so that it doesn't just disappear.

- We feel this would not only streamline your reporting process, but also make your reports more digestible.
- ✓ Now the letters: Take a look to the letters at the back of your reports. There should be two. The first one is titled: “**Communication with those charged with governance at the conclusion of the audit.**” There’s nothing to note here, which is awesome. If we had problems, here is where we would tell you all about it!
- ✓ Next, please find the report on the additional procedures we performed this year as a result of the ARPA spending. Because more than \$750,000 of federal funds were spent in 2022, we needed to do additional procedures on how the ARPA money was spent, the controls surrounding it, and the reporting process. There were no problems noted. Had your federal funds exceeded \$750,000 for reasons other than just ARPA, a full single audit would have been necessary, but thankfully, no single audit requirements were needed and this step-down engagement covers all of your federal expenditures.
- ✓ Lastly, the **report on internal controls**: First, you’ll find the standard comments which are the same ones we always mention, the comment regarding us preparing your report on your behalf and the segregation of duties. Again, it does not make financial sense to the county to hire a CPA on staff to compensate for this so the letter reflects the commissioner’s response. The state is well aware of this and thinks nothing of it.
- ✓ Next, I’d like to mention a few things we noted that do not rise to the level of a formal write up, but noteworthy enough that we thought a quick discussion was warranted.
 - Credit card usage. As a firm, we have a tightened stance on the use of credit cards within a government. We were recently involved in a fraud case that in part, was committed with credit cards. While we noted so such problems were noticed here, it doesn’t hurt to have increased scrutiny. We noticed a few instances of minor purchases

being made with the county's credit card that did not seem to have prior approval. There was an email thread that mentioned a small purchase shouldn't have been approved but since it was already bought, it could slide. Again, this amount was not a big deal. But, the bigger deal is that the purchasing control function was overtaken by use of the credit card.

- Secondly, as a result of doing the audit of the ARPA funds, we chose to look at all grants the county received in 2022. While we noted no particular problem with any grants, we do suggest that the board designate someone to manage all grants applied for on behalf of the County. There seemed to be numerous departments applying for grants with no centralized approval.
 - Problems that could result from this include:
 - Grant applications should include approved financial statement numbers. If a particular department head is preparing a grant application, he/she may not have the most up to date numbers.
 - Budgets need to be adjusted as grants get approved.
 - The Board should be aware of incoming grant money before it arrives so that if it doesn't, someone knows to investigate it.
 - If the County's grant applications are denied, the Board should know why.
- I asked for all grants received during 2022. I did receive the requested information, but it did seem as though one department did not want to supply the information. I'm not sure if I was supposed to read down through the email that was forwarded to me, but it said something to the effect of "I'm supplying this as a courtesy, but I do not have to." I found that concerning from an employee of a county to feel so secretive about an approved grant.
- ✓ Next, please find on page 4 of that letter the comment that does matter. As previously mentioned, the Sheriff's Fund ended the year with a negative fund balance. In addition, the same fund spent in excess of budgeted amounts. The amounts and the relating state statutes are mentioned in the finding #2022-003. This was not a situation where the audit adjustments caused these issues. There were only minor adjustments to this fund which involved adjusting for the 12-1-2022 millage, which is done every year, and a reclassification of an expense, neither of which increased expenses. The

County will receive a request to submit deficit elimination plan and a request for a corrective action plan from the State soon after this report is uploaded. As a board, you will want to ensure that a qualified individual takes responsibility for not only completing the requests of the State but also helping to ensure that 2023 doesn't present further issues within this fund.

In closing, it has been our honor to work for Montmorency County. Despite the control comments I just mentioned, the audit went exceptionally well this year. Please, do not hesitate to reach out if any of us can assist you in any way during the year.

Respectfully,

Kristy Schulze

Julia Oswald

Claudia Miller

Sandra Edwards



**INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING
AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS
PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS***

May 16, 2023

Board of Commissioners
Montmorency County
Atlanta, Michigan

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of Montmorency County, Michigan (also referred to as "the County"), as of and for the year ended December 31, 2022, and the related notes to the financial statements, which collectively comprise Montmorency County, Michigan's basic financial statements, and have issued our report thereon dated May 16, 2023. Our report includes a reference to other auditors who audited the financial statements of the Montmorency County Public Library and Montmorency County Commission on Aging, as described in our report on the County's financial statements. The financial statements of the component units were not audited in accordance with *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the County's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the County's internal control. Accordingly, we do not express an opinion on the effectiveness of the County's internal Control.

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. 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 of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, weaknesses or significant deficiencies may exist that have not been identified.

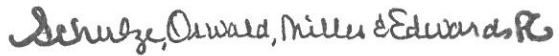
Report on Compliance and Other Matters

As part of obtaining reasonable assurance about whether the County's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the financial statement. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Very truly yours,

A handwritten signature in cursive script that reads "Schulze, Oswald, Miller & Edwards PC".

Schulze, Oswald, Miller & Edwards PC
Alpena, Michigan

SCHEDULE OF FINDINGS AND RESPONSES

INTERNAL CONTROL OVER FINANCIAL REPORTING

Preparation of the Financial Statements in Accordance With Generally Accepted Accounting Principles (Material Weakness)

Finding 2022-001

- Criteria:** The County is required to prepare financial statements in accordance with generally accepted accounting principles (GAAP). The preparation of financial statements requires having in place internal controls over recording, processing, reconciling and preparing financial statements.
- Condition:** The County relied on its independent external auditors to assist in reconciling accounts, preparing the financial statements and related footnotes. Accordingly, the County has placed reliance on its external auditors who cannot be considered a part of the County's internal controls.
- Cause:** It continues to be the decision of the County to have the independent auditor's assist in the preparation of the County's audited financial statements and related footnotes as it is more cost effective than incurring the time and expense to obtain the necessary training and expertise required for the County to perform this task internally.
- Effect:** As a result of this condition, the County lacks internal control over the financial statement preparation process and instead relied, in part, on its external auditors for assistance with this task.
- View of Responsible Officials:** Like many other governmental organizations, the County has made an ongoing evaluation of the respective costs and benefits of obtaining internal knowledge versus utilizing external resources for the preparation of the financial statements. As with many organizations, the County has determined that the additional benefits derived from implementing such an internal system would not outweigh the costs of utilizing external resources. The County will continue to review the draft financial statements and notes prior to approving them and accepting responsibility for their content and presentation.

This comment is a repeat from the prior audits.

Segregation of Duties (Material Weakness)

Finding 2022-002

- Criteria:** All governments are required to establish an internal control structure with segregation of responsibilities sufficient to provide reasonable assurance that errors (whether caused by error or fraud) will be prevented or detected and corrected by management on a timely basis. This is a responsibility of the County. Adequate segregation of duties as it related to the cash cycle of a municipality requires separation of the management function, the custody of assets function, and the accounting function.
- Condition:** Certain members of the accounting department are responsible for the custody of assets as well as for the accounting for those assets in the area of cash receipts and cash disbursements. Further, certain employees holding management positions also collect or disburse cash and account for the transactions of the County.
- Cause:** As is the case with many organizations of similar size, the County lacks a sufficient number of accounting personnel involved in the financial reporting process in order to ensure a complete segregation of duties within the accounting function.
- Effect:** As a result of this condition, the County's current system of internal control has limited safeguards in place to ensure that fraud or abuse is being prevented, specifically in the transactions of the cash cycle.
- View of Responsible Officials:** To the extent possible, duties are allocated between accounting personnel to mitigate risk of material misappropriation of assets. In addition, the County Board of Commissioners assumes a higher level of oversight responsibilities to mitigate risks related to this lack of segregation of duties.

This comment is a repeat from prior audits.

Negative Fund Balance and budget overage (Material Weakness)

Finding 2022-003

Criteria: All governments are required to maintain a positive fund balance in all funds. A positive fund balance helps ensure that there will be adequate liquid resources to serve as a financial cushion. In addition, all governments are required to not spend in excess of budgeted amounts.

Condition: As of December 31, 2022, the Sheriff's Fund had incurred accumulated expenses in excess of revenue, creating a fund deficit in the amount of \$42,080. In addition, the Sheriff's fund had expenditures in excess of budgeted amounts in the amount of \$17,556.

Cause: Spending in excess of budgeted amounts partially created the fund deficit. The beginning fund balance as of January 1, 2022 was \$18,887. Given the known revenue amounts, the Sheriff's fund should not have had expenditures of more than \$585,000 in order to avoid a fund deficit. This amount of expenditures still exceeds the revenue of the fund by \$18,137. In addition, due to the excess spending, spent in excess of budgeted amounts. Public safety budgeted expenditures were \$527,733 but expenditures for public safety totalled \$545,289.

Effect: As a result of this condition, the County is in violation of Michigan Compiled Laws, Municipal Financing Statement 141.1545. and the Uniform Budgeting and Accounting Act, PA 2 of 1968, as amended (MCL 141.421 et seq). The State of Michigan requires that a reasonable plan to eliminate a deficit condition is vital to the fiscal well-being of the County, as is early implementation of that plan. A plan and certified resolution is required to be filed as soon as possible following the submission of the County's audit report to the State of Michigan. In addition, the County will be required to submit a corrective action plan regarding budgetary compliance.

View of Responsible Officials:

The County Officials will create a one year deficit elimination plan to ensure the Sheriff's Fund no longer has a negative fund balance as of December 31, 2023.