

October 22, 2018

To the Mayor and City Council  
City of Davison, Michigan

We have audited the financial statements of City of Davison, Michigan (the "City") as of and for the year ended June 30, 2018 and have issued our report thereon dated October 22, 2018. Professional standards require that we provide you with the following information related to our audit, which is divided into the following sections:

Section I - Required Communications with Those Charged with Governance

Section II - Other Recommendations, Legislative, and Informational Items

Section I includes information that current auditing standards require independent auditors to communicate to those individuals charged with governance. We will report this information annually to the mayor and City Council of the City of Davison, Michigan.

Section II presents recommendations related to internal control, procedures, and other matters noted during our current year audit. These comments are offered in the interest of helping the City in its efforts toward continuous improvement, not just in the areas of internal control and accounting procedures, but also in operational or administrative efficiency and effectiveness. This section also contains updated legislative and informational items that we believe will be of interest to you.

We would like to take this opportunity to thank the City's staff, especially Andrea and Julie, for the cooperation and courtesy extended to us during our audit. Their assistance and professionalism are invaluable.

This report is intended solely for the use of the mayor, the City Council, and others within the City and is not intended to be and should not be used by anyone other than these specified parties.


We welcome any questions you may have regarding the following communications, and we would be willing to discuss any of these or other questions that you might have at your convenience.

Very truly yours,

**Plante & Moran, PLLC**



Pamela Hill, CPA  
Partner



Amanda Cronk, CPA  
Manager

## **Section I - Required Communications with Those Charged with Governance**

### **Our Responsibility Under U.S. Generally Accepted Auditing Standards**

As stated in our engagement letter dated April 25, 2018, our responsibility, as described by professional standards, is to 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 to obtain reasonable, but not absolute, assurance that the financial statements are free of material misstatement.

As part of our audit, we considered the internal control of the City of Davison, Michigan. Such considerations were solely for the purpose of determining our audit procedures and not to provide any assurance concerning such internal control.

We are responsible for communicating significant matters related to the audit that are, in our professional judgment, relevant to your responsibilities in overseeing the financial reporting process. However, we are not required to design procedures specifically to identify such matters.

### **Planned Scope and Timing of the Audit**

We performed the audit according to the planned scope and timing previously communicated to you in our meeting about planning matters on August 27, 2018.

### **Significant Audit Findings**

#### ***Qualitative Aspects of Accounting Practices***

Management is responsible for the selection and use of appropriate accounting policies. In accordance with the terms of our engagement letter, we will advise management about the appropriateness of accounting policies and their application. The significant accounting policies used by the City are described in Note 1 to the financial statements.

No new accounting policies were adopted and the application of existing policies was not changed during the year, with the exception of the adoption of GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other than Pensions*. Accordingly, the accounting change has been retrospectively applied to prior periods, as indicated in Note 16.

We noted no transactions entered into by the City 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 are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected.

The most sensitive estimates affecting the financial statements were the estimated liability related to the net pension liability and net other postemployment benefit liability. Management's estimates of the net pension liability and net other postemployment benefit liability is based on the pension actuarial valuations and the other postemployment benefit valuation, respectively. We evaluated the key factors and assumptions used to develop the estimates in determining that they are reasonable in relation to the financial statements taken as a whole.

## **Section I - Required Communications with Those Charged with Governance (Continued)**

The disclosures in the financial statements are neutral, consistent, and clear.

### ***Difficulties Encountered in Performing the Audit***

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

### ***Disagreements with Management***

For the purpose 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, 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.

### ***Corrected and Uncorrected Misstatements***

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management.

We did not detect any misstatements as a result of audit procedures.

### ***Significant Findings or Issues***

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, business conditions affecting the City, and business plans and strategies that may affect the risks of material misstatement, with management each year prior to our retention as the City's auditors. However, these discussions occurred in the normal course of our professional relationship, and our responses were not a condition of our retention.

### ***Management Representations***

We have requested certain representations from management that are included in the management representation letter dated October 22, 2018.

### ***Management Consultations with Other Independent Accountants***

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the City'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.

## **Section II - Other Recommendations, Legislative, and Informational Items**

### **Other Recommendations**

During our audit, we noted areas where we believe there are opportunities for the City to further strengthen internal control or to increase operating efficiencies. Our observations on those areas are presented below for your consideration:

**Accounting Structure** - The City's current fund structure for the payroll, fringe, and revolving funds is more complex than a typical governmental entity. To simplify the fund structure, the City could combine the above-named funds into the General Fund, using a separate department to account for the activity. We feel this would allow the City to more efficiently account for various activities in the general ledger. We would be happy to discuss this process further with the City if this is something it is interested in implementing.

**Cash Accounts** - The City currently has a significant number of bank accounts, often multiple bank accounts within a fund. While this is an acceptable practice, pooling some of these cash accounts may lead to efficiencies for the City, particularly when performing monthly bank reconciliations, and could help to reduce the number of interbank transfers needed throughout the year. We would be happy to assist the City in reviewing the various bank accounts to identify accounts that could be pooled for efficiency purposes.

**Building Permit Rates** - In recent years, the City's expenditures incurred related to building construction costs have exceeded the building permit fees charged. We would encourage the City to review the building permit rate structure to ensure rates are appropriately capturing the costs incurred by the City.

### **Legislative and Informational Items**

#### **Updated Uniform Chart of Accounts**

In April 2017, the State released an updated Uniform Chart of Accounts. Originally, local units of government were expected to comply with the changes beginning with June 30, 2018 year ends. However, on June 4, 2018, the State extended the deadline for compliance to "sometime in 2019." This extension allows officials more time to convert to new accounts. In the meantime, the Treasury is working on developing training and additional information to assist in the transition.

Local units should begin evaluating this new chart of accounts to determine what changes will be necessary, including any budgetary changes, and set up a plan to achieve compliance. Some accounting software vendors have already been working with some local units on an automated remapping solution. The changes in the chart of accounts are not voluminous, but will require some review. The new chart of accounts can be found at the following link:

[http://www.michigan.gov/documents/uniformchart\\_24524\\_7.pdf](http://www.michigan.gov/documents/uniformchart_24524_7.pdf)

#### **Launch of Michigan Community Financial Dashboard**

The Michigan Department of Treasury launched the Michigan Community Financial Dashboard. This dashboard will provide you and your community members with easy-to-use visual data regarding your municipality. The data presented on the dashboard is pulled from the Annual Local Fiscal Report (F65) submitted by your local unit. The dashboard will present data from fiscal years 2010 through 2017. You can sign in and review the dashboard here:

<http://micommunityfinancials.michigan.gov#!/dashboard/COUNTY/?lat=44.731431779455505&lng=-83.018211069625&zoom=5>

## **Section II - Other Recommendations, Legislative, and Informational Items (Continued)**

### **Legacy Costs**

Legacy costs and the challenge of funding them continues to be a topic of discussion. GASB pronouncements of late have placed even more focus on the net long-term liability arising from these benefit promises by requiring governmental financial statements to now reflect the net pension/OPEB liability. For many governments, these net liabilities are significant. In addition, PA202 of 2017 has brought further focus on the funding level of these plans.

The following are the funding levels per the funding valuations for the last three years for both pension and OPEB:

	Pension - Union (Valuation Year)	Pension - Nonunion (Valuation Year)	OPEB (Fiscal Year)
2017	50.0%	83.0%	8.2%
2016	52.0%	85.8%	2.2%
2015	52.0%	82.3%	2.2%

Maintaining or even improving the funded status of the plans is dependent upon a number of factors, including the City's contribution policies, its amortization policy for funding the unfunded actuarial accrued liability, its benefit levels, and the ability to make future changes to the plan.

That said, the challenge here is significant. We are happy to assist you in thinking through alternative ways to manage this liability.

### **Legacy Cost Reporting**

#### **Public Act 530 of 2016**

On December 31, 2016, the governor signed Public Act 530 of 2016, which amends Public Act 314 of 1965, also known as Public Employee Retirement System Investment Act (PERSIA). This act was effective March 29, 2017.

Under the prior act, communities were required to publish a summary annual report setting forth key information related to pension and retiree healthcare plans. The amendment requires that this summary annual report also be submitted to the Michigan Department of Treasury within 30 days of publication.

In addition, for any system (either pension or retiree healthcare) that is not funded at a level of at least 60 percent, the community must now post a report to its website indicating steps that are being undertaken to address the liability. In addition, this report must be submitted to the Department of Treasury within a reasonable time frame.

The legislation calls for the Department of Treasury to accumulate all of the reports and publish a summary of funding levels throughout the State.

#### **Public Act 202 of 2017**

On January 5, 2018, the Michigan Department of Treasury released initial reporting requirements under Public Act 202 of 2017 (the "Act"), which was a primary component of the Act. These reporting requirements apply to all local units of government that offer or provide defined benefit pension and/or defined benefit OPEB retirement benefits.

## **Section II - Other Recommendations, Legislative, and Informational Items (Continued)**

The releases by the Department of Treasury included Numbered Letter 2018-1, Form 5572, detailed instructions for completion of Form 5572 and a listing of frequently asked questions. All documents can be located at:

[http://www.michigan.gov/treasury/0,4679,7-121-1751\\_51556\\_84499---,00.html](http://www.michigan.gov/treasury/0,4679,7-121-1751_51556_84499---,00.html)

Form 5572 is due annually for both pension and OPEB plans provided by an employer no later than the six months after the end of your fiscal year.

In addition to submitting this new form to the Department of Treasury, local units must also post this information on its website or in a public place, if the local unit does not have a website. The governing body of a local unit will also need to receive a copy of this form, in accordance with the Act, but the Act does not require approval by the governing body before submission to the Treasury.

Public Act 202 defines that a local unit of government is in “underfunded status” if any of the following apply:

1. OPEB - Total plan assets are less than 40 percent of total plan liabilities, according to the most recent annual report, and, for primary units of government<sup>1</sup>, the annual required contribution for all of the retirement health systems of the local unit is greater than 12 percent of the local unit of government’s governmental funds operations revenue.
2. Retirement pension plans - Total plan assets are less than 60 percent of plan total liabilities according to the most recent annual report, and, for primary units of government, the annual required contribution for all of the retirement health systems of the local unit is greater than 10 percent of the local unit of government’s governmental funds operations revenue.

If, after submission of Form 5572, the Treasury determines your community to have underfunded status, you will have the opportunity to file a “waiver” under Section 6 of the Act. The waiver needs to provide a plan for how the underfunding is being addressed. This waiver will then be submitted to the Treasury.

In the event that a local unit has underfunded plans and does not submit a waiver or the waiver is not approved, the Treasury will perform an internal review. The local unit will also need to submit a corrective action plan to the newly created Municipal Stability Board (under Section 7 of the Act). The local unit will be responsible for creating the corrective action plan.

For governments with OPEB plans, Section 4(l)(a)(i)(ii) of Public Act 202 of 2017 requires the local unit to pay retiree insurance premiums for the year, as well as the normal costs for the new employees hired after June 30, 2018. The actuary will likely need to calculate this number in order for governments to comply. In addition, if your community must essentially prefund this additional cost, those communities without a qualifying OPEB trust will need to consider where this contribution will go.

Questions should be directed via email to the treasury offices at:

[LocalRetirementReporting@michigan.gov](mailto:LocalRetirementReporting@michigan.gov) or by visiting their website at:

[www.Michigan.gov/LocalRetirementReporting](http://www.Michigan.gov/LocalRetirementReporting)

---

<sup>1</sup> Primary units of government are cities, villages, townships and counties.

## Section II - Other Recommendations, Legislative, and Informational Items (Continued)

### Other New Legislation

#### **LCSA Act Amendments**

Public Acts 247 and 248 of 2018 were signed into law on June 27, 2018 by Governor Snyder. These acts significantly impact the Local Community Stabilization Authority (LCSA) Act, including how personal property tax reimbursements are calculated.

The State Department of Treasury issued a summary of the amendments in July 2018, which can be found at the following link:

[https://www.michigan.gov/documents/treasury/Overview\\_of\\_2018\\_LCSA\\_Act\\_Amendments\\_627459\\_7.pdf](https://www.michigan.gov/documents/treasury/Overview_of_2018_LCSA_Act_Amendments_627459_7.pdf)

This summary document lists the following changes that resulted from these acts:

1. Accelerate some reporting deadlines and added two new reporting requirements
2. Change the calculation of the millage rate to be used in the calculation of the PPT reimbursements
3. Change the calculation of the personal property exemption loss and eliminate the requirements to recalculate prior year taxable values
4. Change the millage rate to be used in the calculation of a Tax Increment Finance Authority's (TIFA) PPT reimbursement
5. Make the Local Community Stabilization Authority responsible for distributing the fire protection services payments
6. Create a process for correcting PPT reimbursements
7. Allow for a one-time PPT advance for prior year underpayments of \$500,000 or more
8. Change the payment dates of the PPT reimbursements to allow for corrections to current year reimbursements, and delay the payment of qualified loss in excess of 100 percent until May 20
9. Change how municipalities are required to record and allocate the revenue

While we strongly recommend reviewing the link provided above for an in-depth look at the changes, highlighted below are the more significant changes.

- PPT reimbursement calculations are changing, as follows:
  - The requirements for recalculation of prior year taxable value have changed. Going forward, prior year property tax values for commercial and industrial personal property will only be modified for municipality boundary changes, as well as to exclude any that were classified in the municipality where it is currently located as utility personal property or real property after 2012.
  - The calculation of PPT reimbursements that are based on the acquisition cost of eligible personal property for two years has been delayed until 2021.
  - Reimbursement for 100 percent of the calculated qualified loss going forward will be received in either October or February.

**Section II - Other Recommendations, Legislative, and Informational Items  
(Continued)**

- Each year, any remaining balance of the local community stabilization share fund revenue for the calendar year will be distributed to counties, cities, townships, villages, and community colleges. The allocation will be based on each municipality’s share of the total reimbursement based on the acquisition cost of all eligible personal property and qualified loss. These reimbursement payments will be a separate payment which will be reimbursed in May. This allows time for any errors in that year’s PPT reimbursement calculation to be identified and corrected.
- There are also changes to the tax increment finance authority (TIFA) PPT reimbursement calculation; please refer to the link above for more details.
- Fire protection service payments will begin being distributed by LCSA to municipalities in 2018. The payment distributions will occur by November 30 each year. Each municipality is to continue to complete and submit the required questionnaire to LARA in order to qualify.
- Timing of PPT reimbursements: Beginning in 2018, PPT reimbursement payment dates are different than prior years.
  - a. Tax Increment Finance Authorities (TIFAs) - For a TIFA that previously received payments in November, reimbursements will be issued October 20 of each year. Corrections for the underpayment of a 2017 PPT reimbursement or a current year reimbursement will be issued May 20 of each year.
  - b. Municipalities, excluding school districts, ISDs, and TIFAs - For a municipality that previously received payments in November, reimbursements for essential services, small taxpayer exemption loss, and qualified loss up to 100 percent will be issued October 20 of each year. For municipalities that previously received payments in February, reimbursements for essential services, small taxpayer exemption loss, and qualified loss up to 100 percent will continue to be issued February 20 of each year. Corrections for the underpayment of a 2017 PPT reimbursement or a current year reimbursement will be issued May 20 of each year, as will the portion of qualified loss exceeding 100 percent reimbursement.

The table below provides a schedule of payment dates for all municipalities.

<b>Description of PPT Reimbursement</b>	<b>Date of Reimbursement</b>
Advance for 2017 underpayment of \$500,000 or more	October 20, 2018
Payment of calculated current year PPT reimbursements up to 100 percent of the calculated losses for county allocated millage to municipalities that do not levy millage 100 percent in December and TIFAs	October 20 (each year)
Payment of calculated current year PPT reimbursements up to 100 percent of the calculated losses for townships, county extra-voted millage, and to municipalities that levy millage 100 percent in December	February 20 (each following year)
Payment of 2017 underpayment that was not advanced, current year underpayment, and prorated qualified loss in excess of 100 percent	May 20 (each following year)



## **Section II - Other Recommendations, Legislative, and Informational Items (Continued)**

- Changes to the requirement to restrict revenue - To date, the previous LCSA act had only required a municipality to use the reimbursement amount received for debt millage to pay for debt and to use the essential service reimbursement to pay for the cost of essential services. The newly signed amendment now also requires that each municipality allocate and record the payments received in the same manner as the millage levied, up to 100 percent reimbursement. In addition, for county road millages levied under Section 20b of 1909 PA 283, MCL 224.20b, a formula to allocate a portion of the PPT reimbursement to each city and village must be decided on by March 31 by the cities, villages, and road commission. If this does not occur, a formula for allocating payments will be determined by the Department of Treasury.

As a reminder, the LCSA reimbursements should not be reported on the financial statements with property taxes; instead, they should be included with other intergovernmental revenue from the State (state-shared revenue, grants, and other). The State has created a new account number for the revenue, 573, and titled it "Local Community Stabilization Share Appropriation." As always, communities should follow the State's guidance related to the Uniform Chart of Accounts.

### **Upcoming Accounting Standards Requiring Preparation**

#### **GASB Statement No. 84, Fiduciary Activities**

GASB Statement No. 84 provides criteria for state and local governments to use to identify whether an activity is fiduciary and should be reported as a fiduciary fund type in its financial statements. In addition, once identified as a fiduciary activity, Statement No. 84 also provides specific reporting requirements.

This statement has the potential to significantly impact what governments report currently as a fiduciary activity. Upon adoption, we anticipate that some government's fiduciary activities will need to move to governmental funds while other activities that never before were considered fiduciary will now be reported as such. It is also possible that certain pension and OPEB fiduciary funds will no longer be reported in a local unit's financial statements.

Although this standard will not be effective for another year, given its potential to have a major impact on many governments, not only to its external financial statements, but also to its accounting system requirements and budget document, we encourage you to start analyzing the impact of this standard now. The first step to implementation is identifying the type of activities that should be analyzed and then running those activities through the lens of this standard.

#### **GASB Statement No. 87, Leases**

This new accounting pronouncement related to leases will be effective beginning with the City's fiscal year 2021. This statement requires recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and recognized as inflows of resources or outflows of resources based on the payment provisions of the contract. It establishes a single model for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset. Under this statement, a lessee is required to recognize a lease liability and an intangible right-to-use lease asset, and a lessor is required to recognize a lease receivable and a deferred inflow of resources.

We recommend the City begin accumulating information related to all significant lease agreements now in order to more efficiently implement this new standard once it becomes effective.

**Section II - Other Recommendations, Legislative, and Informational Items  
(Continued)**

Plante & Moran, PLLC will be providing trainings and other resources to our clients over the coming months in order to help prepare for the implementation of all these new standards. In the interim, please reach out to your engagement team for assistance in getting started.