SIKICH

CITY OF BRAIDWOOD, ILLINOIS

MANAGEMENT LETTER

April 30, 2018

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The Honorable Mayor
Members of the City Council
City of Braidwood, Illinois

Ladies and Gentlemen:

In planning and performing our audit of the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Braidwood, Illinois (the City) as of and for the year ended April 30, 2018, in accordance with auditing standards generally accepted in the United States of America, we considered the City'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 City's internal control. Accordingly, we do not express an opinion on the effectiveness of the City's internal control.

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

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 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. 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 City's financial statements will not be prevented, or detected and corrected, on a timely basis.

The City's written responses to these matters identified in our audit has not been subjected to the audit procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

This communication is intended solely for the information and use of the Mayor, City Council and management and is not intended to be and should not be used by anyone other than these specified parties.

Sikich LLP

Naperville, Illinois
December 21, 2018

MATERIAL WEAKNESSES

1. Segregation of Duties

A system of internal control provides for a proper segregation of the accounting functions. This system would segregate recording of transactions, custody of assets, and authorization of transactions. Proper segregation is not always possible in Finance departments, but limited segregation to the extent possible can and should be implemented to reduce the risk of errors or fraud. We recommend that the City Council and management continuously review the current assignments of accounting functions and accounting software user restrictions. This also includes functions such as cash disbursements, cash receipts, payroll, general journal entries, reporting and others. Where possible, duties should be segregated and/or additional compensating controls should be implemented to reduce the risk of errors or fraud.

During our audit we identified the following areas that lacked proper segregation of duties or proper compensating controls:

- The payroll processing function had been performed by one individual in the Finance department. There is no formal policy in place regarding the review of the final payroll and, additionally, no payroll change form is printed and reviewed with payroll before finalizing. We also noted that the Finance employee was able to create new employees without review or approval by an appropriate employee or member of management We recommend that the payroll internal control process be formalized, which would include proper review of the payroll processing by an appropriate employee or member of management, and that the City prints a change log with each payroll that is reviewed to ensure that changes made in each payroll period are properly reviewed and approved.

- Bank reconciliations had been prepared by one individual in the Finance department, and there was no formal review and approval of the completed reconciliation. We recommend that the reconciliations are reviewed and approved by an appropriate employee or member of management.

- During our review of the accounts payable and cash disbursement cycle, we noted that the employees responsible for those functions have the ability to add vendors into the system, and there is no review of a master vendor list. We recommend that a review of the vendor listing is performed in a periodic basis. Additionally, we noted that the employees responsible for performing the accounts payable function have access to most steps in the process, including coding invoices, posting to the general ledger, and printing checks. Where possible, we recommend that these duties are segregated.

Management Response

The City is considering both a payroll reporting and payroll processing policy to address the segregation of duties issues raised.

Regarding bank reconciliations, as of May 1, 2018, the City now has all bank reconciliations signed and dated by the person preparing the reconciliations. The Commissioner of Finance also signs and dates the reconciliation to show the reconciliations have been reviewed and approved.

MATERIAL WEAKNESSES (Continued)

2. Cash Reconciliations

During our testing of cash at the City, we noted that cash had not been fully reconciled for the entire fiscal year and the full reconciliation was not completed for several months after year end. It was also noted that there were differences between the bank reconciliation and the general ledger balance that carried forward each month. We proposed an adjusting journal entry to the general ledger to eliminate this difference which was reviewed and approved by management. Not reconciling the accounts on a monthly basis means that errors or other problems might not be recognized and resolved on a timely basis. Also, it is generally easier and less time-consuming to reconcile accounts while transactions are fresh in mind. This is deemed to be a material weakness in internal control as the cash reconciliation process is an integral component of sound financial practices. We recommend the City institute a formal bank reconciliation process, including setting parameters for the timing of when the reconciliation will be performed and reviewed.

At present, finance personnel perform bank reconciliations. We recommend that management open the bank statements and review them for any unusual checks or other transactions before forwarding them to accounting to perform the reconciliation. Management's review of the bank statement will ensure that unusual items are investigated on a timely basis.

Additionally, during our review of the bank reconciliations we noted that there were a significant number of outstanding checks greater than six months old. We recommend that the City follows up on checks older than six months, reclassify them into an unclaimed property account, and determine if they need to be turned over the State of Illinois.

Management Response

The City has begun reconciling all cash accounts on a monthly basis. Due to the bank accounts not being fully reconciled in the previous year, the City could not complete the Fiscal Year 2019 reconciliations until the audit was completed and all adjustments to cash had been identified.

The person performing the reconciliation process does not open the bank statement. It is opened by other personnel to ensure cash receipts have been properly recorded. Going forward a member of management will open the bank statements and review for any unusual items.

Old outstanding checks were reviewed during the May 2018 reconciliation process. It was noted that checks had cleared in previous years but were not marked as cleared within the accounting software. These checks have been cleared out of the software as of May 2018. Other checks should have been voided as a replacement check had been issued. These checks were voided within the system as of May 2018.

The City is considering an accounts receivable policy to address these issues as well.

MATERIAL WEAKNESSES (Continued)

3. Utility Billing

During our audit of the utility billing cycle, we identified the following items to be addressed:

In the previous fiscal year, the City approved amending the utilities ordinance to change utility billing from monthly to bi-monthly. While the change was implemented, the water bills only generated the bill amount based on one month of usage. As a result, citizens were significantly underbilled. The issue was rectified during July 2017; however, bills were not retroactively corrected. We recommend that the City implements review procedures to correct utility billings and ensure any future errors are detected and corrected in a timely manner.

While testing the enterprise revenues at the City, we noted that ordinances and the Municipal Code that contained the authorized rates to be charged were out of date and not clearly defined as to what the current rate should be. We recommend that the City reviews the rates being charged and ensure that they have appropriate authorization to charge those rates through an ordinance that specifically states the rates to be charged.

During our testing of the enterprise revenues, we identified a significant amount of balances outstanding greater than 120 days as of April 30, 2018. While this amount came down slightly during the following fiscal year, we still proposed an entry to record an allowance for doubtful accounts. We recommend that the City continues to review the old outstanding accounts receivable balances, follow up on these accounts, and consider implementing a formal policy on how to address balances that are not paid.

Additionally, we noted during our review of the utility billing control cycle that rates and meter readings can be modified within the City's software, and bills can go out, without proper review and approval. We recommend that a level of review is built into the utility billing process.

Management Response

The City is considering an accounts receivable policy for invoices over 120 days old to ensure that those invoices due the City are collected in a timely fashion.

4. Prior Period Adjustments

During our audit of the City, we noted certain balances that were misstated as of April 30, 2017, as described in Note #10 in the City's Annual Financial Report as of April 30, 2018. We proposed journal entries, which were reviewed, approved, and recorded by the City to correct these misstatements. We recommend that the City closely monitor its general ledger accounts and perform regular reconciliations to ensure that transactions are being recorded in the proper period. Additionally, we recommend the City reviews its controls over long-term debt and its revenue recognition policies to ensure amounts are recorded in the proper period.

MATERIAL WEAKNESSES (Continued)

4. Prior Period Adjustments (Continued)

Management Response

Going forward, the City will now provide a reconciliation workpaper as of year-end to properly account for the various revenue streams and to properly account for receivables, deferred revenue and unbilled revenue as of year-end.

SIGNIFICANT DEFICIENCY

1. Capital Asset Reporting

Our testing of the City's capital asset workpapers identified several journal entries that were required to correctly state the City's governmental and business-type capital assets at year-end. Detailed capital asset records are an important management tool in maintaining control over capital assets. The detailed records should be updated periodically throughout the fiscal year in order to appropriately track capital asset purchases, sales, and disposals. We recommend that the City review its year-end close procedures to ensure that the capital asset balances recorded on the general ledger are accurately stated and reflect the appropriate level of detail and to update capital asset records on a periodic basis throughout the fiscal year to ensure that assets are being maintained appropriately.

Management Response

The City will be performing a capital asset reconciliation before the current fiscal year ends to ensure the capital asset listing is complete and accurate.

OTHER INFORMATION

1. Future Accounting Pronouncements

The Governmental Accounting Standards Board (GASB) has issued a number of pronouncements that may impact the City in the future.

GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, addresses reporting by governments that provide OPEB to their employees and for governments that finance OPEB for employees of other governments and replaces the requirements of GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions,* as they relate to governments that provide benefits through OPEB plans administered as trusts or similar arrangements that meet certain criteria. Statement No. 75 requires governments providing defined benefit OPEB to recognize their long-term obligation for OPEB as a liability for the first time, and to more comprehensively and comparably measure the annual costs of OPEB benefits. The Statement also enhances accountability and transparency through revised and new note disclosures and required supplementary information (RSI). The provisions in Statement No. 75 are effective for fiscal year beginning ending April 30, 2019.

1. Future Accounting Pronouncements (Continued)

GASB Statement No. 83, *Certain Asset Retirement Obligations*, addresses accounting and financial reporting for certain asset retirement obligations (AROs). An ARO is a legally enforceable liability associated with the retirement of a tangible capital asset. A government that has legal obligations to perform future asset retirement activities related to its tangible capital assets should recognize a liability based on the guidance in this Statement. The requirements of this standard are effective for the fiscal year ending April 30, 2020.

GASB Statement No. 84, *Fiduciary Activities*, establishes criteria for identifying fiduciary activities. The focus of the criteria generally is on (1) whether a government is controlling the assets of the fiduciary activity and (2) the beneficiaries with whom a fiduciary relationship exists. Separate criteria are included to identify fiduciary component units and postemployment benefit arrangements that are fiduciary activities. The statement describes four fiduciary funds that should be reported, if applicable: (1) pension (and other employee benefit) trust funds, (2) investment trust funds, (3) private-purpose trust funds, and (4) custodial funds. Custodial funds generally should report fiduciary activities that are not held in a trust or equivalent arrangement that meets specific criteria. The requirements of this standard are effective for the fiscal year ending April 30, 2020.

GASB Statement No 85, *Omnibus 2017*, addresses a number of issues across a spectrum of topics including issues related to blending component units where the primary government is a business type activity that reports basic financial statements in a single column, accounting for goodwill, fair value measurement and application related to real estate held by insurance activities and measuring certain investments at cost or amortized cost, and various issues related to accounting and reporting for postemployment benefits (pensions and other postemployment benefits [OPEB]). Statement No. 85 is effective for the fiscal year ending April 30, 2019.

GASB Statement No. 86, *Certain Debt Extinguishment Issues*, is intended to improve accounting and financial reporting for in-substance defeasances of debt, prepaid insurance on debt that is extinguished and notes to financial statements for debt that is defeased in substance. The requirements of this statement are effective for the fiscal year ending April 30, 2019.

GASB Statement No. 87, *Leases*, establishes a single model for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset and aims to enhance comparability of financial statements among governments. This statement also requires additional notes to the financial statements related to the timing, significance, and purpose of a government's leasing arrangements. The requirements of this statement are effective for the fiscal year ending April 30, 2021.

1. Future Accounting Pronouncements (Continued)

GASB Statement No. 88, *Certain Disclosures Related to Debt*, including Direct Borrowings and Direct Placements, was issued in March 2018 and provides guidance on improving disclosures in the notes to the financial statements related to debt, including direct borrowings and direct placements of debt. This Statement defines debt for purposes of disclosure in notes to financial statements as a liability that arises from a contractual obligation to pay cash (or other assets that may be used in lieu of cash) in one or more payments to settle an amount that is fixed at the date the contractual obligation is established. This Statement requires that additional essential information related to debt be disclosed in notes to financial statements, including unused lines of credit; assets pledged as collateral for the debt; and terms specified in debt agreements related to significant events of default with finance-related consequences, significant termination events with finance-related consequences, and significant subjective acceleration clauses. This statement is effective for the fiscal year ending April 30, 2020.

GASB Statement No. 89, *Accounting for Interest Costs Incurred Before the End of a Construction Period*, was issued in June 2018 and provides guidance for interest cost incurred before the end of a construction period, including interest previously accounted for in accordance with the requirements of paragraphs 5-22 of Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 GASB and AICPA Pronouncements,* which are superseded by this statement. This statement requires that interest cost incurred before the end of a construction period be recognized as an expense in the period in which the cost is incurred for financial statements prepared using the economic resources measurement focus. As a result, interest incurred before the end of a construction period will not be included in the historical cost of a capital asset reported in a business-type activity or enterprise fund. This statement is effective for the fiscal year ending April 30, 2021.

GASB Statement No. 90, *Majority Equity Interests*, an amendment of GASB Statements No. 14 and No. 61, was issued in August 2018. The primary objectives of this Statement are to improve the consistency in the measurement and comparability of reporting a government’s majority equity interest in a legally separate organization and to improve the relevance of financial statement information for certain component units. This Statement establishes that ownership of a majority equity interest in a legal separate organization results in the government being financially accountable for the legally separate organization and, therefore, the government should report that organization as a component unit. This Statement also requires that a component unit in which a government has a 100 percent equity interest account for its assets, deferred outflows of resources, liabilities, and deferred inflows of resources at acquisition value at the date the government acquired a 100 percent equity interest in the component unit. This statement is effective for the fiscal year ending April 30, 2020.

We will advise the City of any progress made by GASB in developing this and other future pronouncements that may have an impact on the financial position and results of operation of the City.