

STATE BOARD OF ACCOUNTS
302 West Washington Street
Room E418
INDIANAPOLIS, INDIANA 46204-2769

SUPPLEMENTAL COMPLIANCE REPORT

OF

TOWN OF HIGHLAND

LAKE COUNTY, INDIANA

January 1, 2021 to December 31, 2022



FILED

11/06/2023

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SCHEDULE OF OFFICIALS

<u>Office</u>	<u>Official</u>	<u>Term</u>
Clerk-Treasurer	Michael W. Griffin	01-01-21 to 02-05-22
	Dawn Kovacich	02-06-22 to 03-02-22
	Mark Herak	03-03-22 to 12-31-23
President of the Town Council	Roger Sheerman	01-01-21 to 12-31-21
	Bernie Zemen	01-01-22 to 12-31-22
	Tom Black	01-01-23 to 12-31-23



STATE OF INDIANA
AN EQUAL OPPORTUNITY EMPLOYER

STATE BOARD OF ACCOUNTS
302 WEST WASHINGTON STREET
ROOM E418
INDIANAPOLIS, INDIANA 46204-2769

Telephone: (317) 232-2513
Fax: (317) 232-4711
Web Site: www.in.gov/sboa

TO: THE OFFICIALS OF THE TOWN OF HIGHLAND, LAKE COUNTY, INDIANA

This report is supplemental to the audit report of the Town of Highland (Town), for the period from January 1, 2021 to December 31, 2022. It has been provided as a separate report so that the reader may easily identify any Audit Results and Comments that pertain to the Town. It should be read in conjunction with the Financial Statement Audit Report of the Town, which provides our opinions on the Town's financial statement. This report may be found at www.in.gov/sboa/.

As authorized under Indiana Code 5-11-1, we performed procedures to determine compliance with applicable Indiana laws and uniform compliance guidelines established by the Indiana State Board of Accounts. The Audit Results and Comments contained herein describe the identified reportable instances of noncompliance found as a result of these procedures. Our tests were not designed to identify all instances of noncompliance; therefore, noncompliance may exist that is unidentified.

Any Official Response to the Audit Results and Comments, incorporated within this report, was not verified for accuracy.

A handwritten signature in blue ink that reads "Beth Kelley".

Beth Kelley, CPA, CFE
Deputy State Examiner

October 23, 2023

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CLERK-TREASURER
TOWN OF HIGHLAND

CLERK-TREASURER
TOWN OF HIGHLAND
AUDIT RESULTS AND COMMENTS

CONDITION OF RECORDS

Similar comments appeared in prior Report B58194, entitled *CONDITION OF RECORDS* and *INTERNAL CONTROLS*.

Condition and Context

There were deficiencies in the internal control system of the Town related to cash and investments, journal entries, receipts, and financial close and reporting. The Town had not established internal controls, which would include appropriate segregation of duties over cash and investments, journal entries, receipts, and financial close and reporting.

Cash and Investments

Internal controls had not been designed or implemented to ensure that bank reconciliations were completed monthly as required by state statute. Furthermore, a process was not in place that ensured a combined monthly bank reconciliation was prepared which agreed to the records and to the financial statement.

The Town had not performed its own reconciliations of its bank accounts since 2019; however, the Town engaged a consultant to perform the reconciliations. The consultant prepared reconciliations during the audit period. From December 2021 through December 2022, there was no documentation that a review or approval process occurred for the bank reconciliations after they were received from the consultant.

The Town has numerous bank accounts and had not included the investment amounts in its reconciliations. As of December 31, the Town provided a list of 337 reconciling items in 2021 and 637 items in 2022. Some of these items dated back to 2019. Reconciling items listed included bank accounts that owed amounts to other bank accounts, returned checks from customers that did not clear through the bank due to non-sufficient funds, and other unidentified differences. The total amount of the reconciling items for each year were as follows:

	2021		2022
Receipts	\$ 5,479,509		\$ 11,595,613
Disbursements	5,390,206		11,299,753
Cash Difference	\$ 89,303		\$ 295,860

The Town had not performed any research or recorded any correcting adjustments needed for the reconciling items identified.

There were various items noted in the reconciliations that could not be identified, explained, or supported. Additional audit procedures were performed, and as of December 31, 2021 and 2022, the adjusted bank balance was determined to be less than the ledger balance by \$327,707 and \$298,764, respectively. The financial statement was not adjusted for these variances.

CLERK-TREASURER
TOWN OF HIGHLAND
AUDIT RESULTS AND COMMENTS
(Continued)

Journal Entries

The Town had not designed or implemented a system of internal controls that ensured journal entries were recorded accurately. One employee recorded the journal entries without a review or approval process. The following errors were noted related to incorrect journal entries:

1. Temporary loans for 2021 and 2022 were recorded by a journal entry. The Town recorded various temporary loans totaling \$974,784 for 2021 and \$2,128,472 in 2022, but when the temporary loans were repaid, the Town reversed the journal entry eliminating the transaction from the record.
2. Most transfers were done by journal entry. Monthly transfers from the Sewage Operating fund to the Sewage Improvement and Sewage Cash Reserve funds were performed by decreasing the revenue in the Sewage Operating fund causing an understatement of revenue collected from sewage fees by \$3,059,957 in 2021 and \$2,368,399 in 2022. The same process was used for the Water Operating fund transfers causing an understatement of revenue collected for water fees by \$828,911 in 2021 and \$897,745 in 2022.
3. The Special Community Crossing Grant Fund received \$1,511,693 in 2022 that was not reported in the financial statement. Upon further investigation, it was determined that the Town had recorded a journal entry to transfer funds to other funds. Instead of recording an expenditure out of the Special Community Crossing Grant Fund, the Town recorded a journal entry out of the revenue account which caused the revenue to be eliminated from the fund.

Adjustments were proposed, accepted by the Town, and made to the financial statement.

Receipts

The Town had not designed or implemented a system of internal controls that ensured receipts were recorded timely and to the proper fund. The Town received money through the Automated Clearing House (ACH) that is automatically deposited into the Town's bank accounts. One employee recorded the ACH into the financial software system without a review or approval process.

Financial Close and Reporting

The Town had not designed or implemented a system of internal controls that ensured amounts reported on the financial statement were accurate. One employee entered and submitted the Annual Financial Report (AFR) into the Indiana Gateway for Government Units (Gateway) financial reporting system without a review or approval process. The following errors were noted related to financial close and reporting:

1. The Town maintains the records through an accrual software program. As a result, adjustments were performed to convert the accrual amounts to cash amounts to report on the regulatory basis in Gateway. In 2021, the Town reduced accounts receivable by increasing the expenditures for various funds instead of decreasing revenues by \$719,536.
2. The Payroll fund receipts and disbursements were each understated by \$3,590,551 for 2021. For 2022, the receipts and disbursements were understated by \$3,557,304 and \$3,557,397, respectively, and the ending cash and investments balance was overstated by \$93.

CLERK-TREASURER
TOWN OF HIGHLAND
AUDIT RESULTS AND COMMENTS
(Continued)

3. The Water Utility - Customer Deposit fund receipts and disbursements were each understated by \$39,848 for 2021, and by \$41,840 for 2022.

Adjustments were proposed, accepted by the Town, and made to the financial statement.

Criteria

Indiana Code 5-11-1-4(a) states:

"The state examiner shall require from every audited entity financial reports covering the full period of each fiscal year. These reports shall be prepared, verified, and filed with the state examiner not later than sixty (60) days after the close of each fiscal year. The reports must be in the form and content prescribed by the state examiner and filed electronically in the manner prescribed under [IC-5-14-3.8-7](#)."

The Indiana State Board of Accounts (SBOA) is required under Indiana Code 5-11-1-27(e) to define the acceptable minimum level of internal control standards. To provide clarifying guidance, the State Examiner compiled the standards contained in the manual, *Uniform Internal Control Standards for Indiana Political Subdivisions*. All political subdivisions subject to audit by SBOA are expected to adhere to these standards. The standards include adequate control activities. According to this manual:

"Control activities are the actions and tools established through policies and procedures that help to detect, prevent, or reduce the identified risks that interfere with the achievement of objectives. Detection activities are designed to identify unfavorable events in a timely manner whereas prevention activities are designed to deter the occurrence of an unfavorable event. Examples of these activities include reconciliations, authorizations, approval processes, performance reviews, and verification processes.

An integral part of the control activity component is segregation of duties. . . .

There is an expectation of segregation of duties. If compensating controls are necessary, documentation should exist to identify both the areas where segregation of duties are not feasible or practical and the compensating controls implemented to mitigate the risk. . . ."

At all times, the manual and/or computerized records, subsidiary ledgers, control ledger, and reconciled bank balance must agree. If the reconciled bank balance is less than the subsidiary or control ledgers, the amount needed to balance may be the personal obligation of the responsible official or employee. (Accounting and Uniform Compliance Guidelines Manual for Cities and Towns, Chapter 1)

When it is determined that an error has been posted in the financial records, the error must be corrected in a timely manner. The correction of the error should be dated as of the date that the correction occurred and should not be back dated to the date the error occurred. The adjustment should be labeled as a correcting entry. All documentation of the error and the adjustments must be maintained to support the correction. (Accounting and Uniform Compliance Guidelines Manual for Cities and Towns, Chapter 1)

CLERK-TREASURER
TOWN OF HIGHLAND
AUDIT RESULTS AND COMMENTS
(Continued)

ANNUAL FINANCIAL REPORT

Condition and Context

Required supplementary information, supplementary information, and other information was required to be entered annually into the Annual Financial Report (AFR) via the Indiana Gateway for Government Units (Gateway) financial reporting system. There was no documentation that anyone had reviewed the financial information after it was entered into Gateway this allowed errors to go undetected. The lack of effective internal controls over the AFR information entered into Gateway, resulted in the following errors:

Required Supplementary Information

Due to the lack of internal controls, the required supplementary information presented for audit included the errors as described above in the *Condition of Records* comment.

Adjustments were proposed, accepted by the Town, and made to the Combining Schedules of Receipts, Disbursements, and Cash and Investment Balances - Regulatory Basis presented in the Financial Statement Audit Report as Required Supplementary Information.

Leases and Debt

Debt information entered into Gateway contained the following errors:

1. The ending principal balance for the Economic Development Revenue Bonds Series 2018 was overstated at December 31, 2021 and 2022, by \$131,288 and \$440,000, respectively.
2. The Park Bonds Series 2021A principal due in one year was overstated by \$20,000 at December 31, 2022.
3. The Park Bonds Series 2021B ending principal balance and principal due within one year were understated at December 31, 2022, by \$29,000 and \$3,000, respectively.
4. The ending principal balance for the Economic Development Revenue Bonds Series 2022 was understated by \$10,602,250 at December 31, 2022.

Adjustments were proposed, accepted by the Town, and made to the Schedule of Leases and Debt presented in the Financial Statement Audit Report as Other Information.

Schedule of Expenditures of Federal Awards (SEFA)

In 2022, the Town reported \$705,950 as a federal grant on the SEFA when the amount was related to a state grant. The SEFA is used to determine if the entity will be a federal audit during the audit cycle.

CLERK-TREASURER
TOWN OF HIGHLAND
AUDIT RESULTS AND COMMENTS
(Continued)

Criteria

Indiana Code 5-11-1-4(a) states:

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An integral part of the control activity component is segregation of duties. . . .

There is an expectation of segregation of duties. If compensating controls are necessary, documentation should exist to identify both the areas where segregation of duties are not feasible or practical and the compensating controls implemented to mitigate the risk. . . ."

MOTOR VEHICLE HIGHWAY (MVH) - RESTRICTED FUND

A similar comment appeared in prior Report B58194, entitled *MOTOR VEHICLE HIGHWAY (MVH) RESTRICTED FUND*.

Condition and Context

The Town did not maintain a separate Motor Vehicle Highway Restricted fund as required. The Town receipted the distributions from the State Motor Vehicle Highway Account into a single Motor Vehicle Highway fund identifying 50 percent as Motor Vehicle Highway Restricted using a specified activity number.

In 2021, the Town's Highway Department recorded disbursements from the Motor Vehicle Highway and Motor Vehicle Highway Restricted funds based on account activity. Motor Vehicle Highway Restricted funds identified were used for non-restricted purposes, such as road repair supplies, road salt, gasoline, shop supplies, and snow shovels.

In 2022, it was unclear what disbursement accounts within the Motor Vehicle Highway fund were considered restricted. The Highway Department prepares an annual report that is submitted to the State, and the department maintains the disbursements by administrative and operations classifications, instead of by Motor Vehicle Highway and Motor Vehicle Highway Restricted funds. As a result, we were unable to test transactions to determine whether Motor Vehicle Highway restricted funds were used for non-restricted purposes.

CLERK-TREASURER
TOWN OF HIGHLAND
AUDIT RESULTS AND COMMENTS
(Continued)

Based on the Highway Department's annual report submitted to the State, the Motor Vehicle Highway and Motor Vehicle Highway Restricted funds financial activity was as follows:

	Cash and Investments 01-01-21			Cash and Investments 12-31-21			Cash and Investments 12-31-22		
	Receipts	Disbursements	Receipts	Disbursements	Receipts	Disbursements	Receipts	Disbursements	
Motor Vehicle Highway	\$ 1,017,029	\$ 522,879	\$ 153,952	\$ 1,385,956	\$ 508,701	\$ 609,252	\$ 1,285,405		
Motor Vehicle Highway Restricted	(307,174)	497,704	783,082	(592,552)	505,189	280,727	(368,090)		
Motor Vehicle Highway	<u>\$ 709,855</u>	<u>\$ 1,020,583</u>	<u>\$ 937,034</u>	<u>\$ 793,404</u>	<u>\$ 1,013,890</u>	<u>\$ 889,979</u>	<u>\$ 917,315</u>		

Adjustments were proposed, accepted by the Town, and made to the financial statement.

Criteria

Indiana Code 8-14-1-5(c) states: "For funds distributed to a city or town from the motor vehicle highway account, the city or town shall use at least fifty percent (50%) of the money for the construction, reconstruction, and preservation of the city's or town's highways."

The purpose of this Directive is to authorize and require . . . towns that receive distributions from the State Motor Vehicle Highway Account to **create a new sub-fund within the MVH Fund** to properly manage and account for the usage restrictions that were included in House Enrolled Act 1002-2017 and House Enrolled Act 1290-2018. . . .

On the chart of accounts, the MVH Fund and MVH Restricted sub-fund shall be shown as follows:

. . .

Cities and Towns

Fund 201	MVH
Fund 203	MVH Restricted

Together, MVH and MVH Restricted shall constitute the total MVH Fund. . . .

(State Examiner Directive 2018-2)

Units are required to comply with all grant agreements, rules, regulations, bulletins, directives, letters, letter rulings, court decisions and filing requirements concerning reports and other procedural matters of federal and state agencies. Units must file accurate reports required by federal and state agencies. Noncompliance may require corrective action. (Accounting and Uniform Compliance Guidelines Manual for Cities and Towns, Chapter 1)

CLERK-TREASURER
TOWN OF HIGHLAND
AUDIT RESULTS AND COMMENTS
(Continued)

OVERDRAWN CASH BALANCES

The same comment appeared in prior Report B58194.

Condition and Context

The financial statement presented for audit included the following overdrawn funds during the audit period:

Fund	Amount Overdrawn	Year
Motor Vehicle Highway Restricted	\$ 592,552	2021
Insurance - Other	128,351	2021
Motor Vehicle Highway Restricted	368,090	2022

Criteria

The cash balance of any fund may not be reduced below zero. Routinely overdrawn funds could be an indicator of serious financial problems which should be investigated by the unit. (Accounting and Uniform Compliance Guidelines Manual for Cities and Towns, Chapter 1)



TOWN OF HIGHLAND

Highland Municipal Building • 3333 Ridge Road

Highland, Indiana 46322

219-838-1080 • Fax 219-972-5097



Population 23,696

Incorporated in 1910

November 2, 2023

Paul Joyce, State Examiner
Indiana State Board of Accounts
302 West Washington Street, Room E418
Indianapolis, IN 46204

Re: Town of Highland's Official Response to the Financial Statement Audit Report for the period January 1, 2021 through December 31, 2022

Dear Mr. Joyce:

Please allow this letter to serve as the Town of Highland's Official Response to the audit of the books and records of our accounts for the period January 1, 2021, through and including December 31, 2022.

I was caucused into the Clerk-Treasurer's position and took office on March 3, 2022, after the unanticipated resignation of our long serving Clerk-Treasurer upon his selection to serve in higher public office. I provide this to give background as I address the issues noted by your audit team.

We acknowledge that while our audit once again resulted in the receipt of an *unqualified or unmodified regulatory opinion*, we recognize that we have room for improvement concerning the recording and reporting of certain segments of our operations. As a result of this process, we believe we are on track to address and correct the items that were brought to our attention. Specifically, we would like to address the following items noted in the Audit Results and Comments section of your report:

Condition of Records:

We concur with the majority of the findings concerning the Conditions of Records as it pertains to the systems of internal controls over Journal Entries, Receipts and Financial Close/Reporting. Many of these issues were noted in the comments contained in the prior audit report.

With the rapid change in officials and the continued high rate of staff turnover during the transition, there was a great loss of institutional knowledge, including unaddressed and/or unresolved prior audit

November 2, 2023

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comments. All of which resulted in the continuation of these conditions which led to the repeated comments. In all of these instances, the records were corrected, with the assistance of the audit team.

We appreciate the assistance and patience demonstrated by the audit team as we worked through these matters and have begun and will continue to put controls and policies in place to avoid similar issues going forward. Those written controls and policies will be retained and presented at the time of the next audit.

However, we take issue with the comments concerning Cash and Investments. Many of the reconciliation items were held over from the prior administration. We continued our engagement of our consultant to perform the necessary reconciliations and assist with identifying the required adjusting entries. Over the course of 2023, with the assistance of the consultant, we have continued to identify and make the necessary reconciling adjustments. During the examination, monthly reconciliations were performed and provided to the audit team.

We dispute the amounts identified in the audit report as variances between the ledger and bank reconciliation independently by the audit team. No documentation to support the alleged variances was provided to us nor was there an opportunity to verify the identified variances reported.

Annual Financial Report:

We acknowledge that there were several adjustments required to be made to address oversights with the Annual Financial Reports for 2021 and 2022. We assumed that the documentation of the review and approval of the final form of the 2022 report submitted through the Gateway Portal was adequately documented by the use of my sign off (signature and PIN) in the submission/uploading process. However, after discussing this with the audit team, we will take the necessary steps to address this matter when completing and submitting the 2023 report. The procedures to be put into place will be documented and made available at the time of the next audit.

Debt Reporting Matters - General:

The overstatement and understatement of the various Park Bonds payable due within one year on December 31, 2022, was due to a misapplication of the scheduled payment date versus the actual date the payments were made. We will address this during the preparation and submission of the 2023 report.

Debt Reporting Matters - Economic Development Revenue Bonds:

We respectfully disagree with the reported overstatement of the principal balances of Economic Development Revenue Bonds of 2018 and 2021. These bonds were issued in connection with the Cardinal Campus Project (Phases I and II). The 2018 and 2021 bonds were both purchased by the

developer as part of an incentive supported by a pledge of TIF revenues generated from defined site developments. The developer/bondholder is only entitled to receive the generated increment. Additionally, the increment is only generated as the site is developed. The bonds do not constitute a general or moral obligation of the Redevelopment Commission or Town.

At the time of issuance of the bonds, the estimated amortization schedule is uploaded into the Gateway Debt Management Portal based upon the maximum bond principal amount which assumes that the project has been fully developed at the time of closing. From the practical standpoint, the Bond Trustee will reflect and record the outstanding principal balance, based upon the submission of construction costs associated with the projects (up to the maximum principal bond amount).

That assumption is carried forward to the Schedule of Long-Term Debt in the Annual Financial Report. This schedule is a supplementary schedule and has no impact on the regulatory financial statements presented. These noted overstatements will occur during the construction period associated with each bond series. We feel that it is more appropriate to report the total potential obligation under the terms of the financing and be overstated during the construction cycle rather than report an increasing obligation each year during the construction cycle giving the appearance that the Town assumed additional debt obligations without an intervening action by the Redevelopment Commission and Council.

Schedule of Expenditures of Federal Awards (SEFA):

We acknowledge that when reporting grants in the Annual Financial Report in 2022, we reported a grant associated with the Community Crossing Matching Grant Program (a grant from the State of Indiana for road construction). Future grant reporting will address only federal grants that are received by the Town.

Motor Vehicle Highway (MVH) Restricted Fund:

We acknowledge that the Town needs to report the activity associated with the restricted portion of the MVH distributions received from the State of Indiana in a separate fund. This will be addressed and included in the submission of the 2023 Annual Financial Report.

Overdrawn Cash Balances:

We acknowledge that there was an issue with overdrawn cash balances at the end of 2021 and 2022. The creation and maintenance of the MVH Restricted Fund will allow us to monitor the activity within the fund and avoid potential shortfalls in the future.

Summary:

November 2, 2023

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In closing, I would again wish to express my profound gratitude for the assistance and professionalism demonstrated by the members of the audit team. They provided a great deal of guidance and I believe that it will make this next audit year a much better one.

Sincerely,

A handwritten signature in black ink that reads "Mark Herak". The signature is written in a cursive style with a large, stylized initial "M".

Mark Herak

Clerk-Treasurer

CLERK-TREASURER
TOWN OF HIGHLAND
EXIT CONFERENCE

The contents of this report were discussed on October 23, 2023, with Mark Herak, Clerk-Treasurer; Tom Black, President of the Town Council; Michael W. Griffin, former Clerk-Treasurer; Chad Kinley, Deputy Clerk-Treasurer; and Jim Higgins, CPA/Consultant.