

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

SUPPLEMENTAL COMPLIANCE REPORT
OF
KOONTZ LAKE REGIONAL SEWER DISTRICT
STARKE COUNTY, INDIANA
January 1, 2011 to December 31, 2012



FILED
01/15/2016

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SCHEDULE OF OFFICIALS

| <u>Office</u> | <u>Official</u> | <u>Term</u> |
|------------------------|--|--|
| Treasurer | Michael B. McKenna | 01-01-11 to 12-31-15 |
| President of the Board | Paul M. Warnke (Vacant) Gerald Weber | 01-01-11 to 07-10-14 07-11-14 to 08-17-14 08-18-14 to 12-31-15 |



STATE OF INDIANA
AN EQUAL OPPORTUNITY EMPLOYER

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TO: THE OFFICIALS OF THE KOONTZ LAKE REGIONAL
SEWER DISTRICT, STARKE COUNTY, INDIANA

This report is supplemental to our audit report of the Koontz Lake Regional Sewer District (District), for the period from January 1, 2011 to December 31, 2012. It has been provided as a separate report so that the reader may easily identify any Federal Findings that pertain to the District. It should be read in conjunction with our Financial Statement and Federal Single Audit Report of the District, which provides our opinions on the District's financial statement and federal program compliance. This report may be found at www.in.gov/sboa.

The Federal Findings, identified in the above referenced audit report, are included in this report and should be viewed in conjunction with the Audit Result and Comment as described below.

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 Result and Comment contained herein describes 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 Corrective Action Plan for the Federal Findings and Official Response to the Audit Result and Comment, incorporated within this report, were not verified for accuracy.

Paul D. Joyce
Paul D. Joyce, CPA
State Examiner

October 19, 2015

KOONTZ LAKE REGIONAL SEWER DISTRICT
FEDERAL FINDINGS

FINDING 2012-001 - FINANCIAL TRANSACTIONS AND REPORTING

We noted deficiencies in the internal control system of the District related to financial transactions and reporting.

1. **Lack of Segregation of Duties:** The District has not separated incompatible activities related to financial close and reporting. The Treasurer prepares and submits the Gateway Annual Financial Report which is used to generate the financial statement without oversight, review, or approval. The failure to establish these controls enabled material misstatements or irregularities to remain undetected. Control activities should be in place to reduce the risks of errors in financial reporting.
2. **Monitoring of Controls:** An evaluation of the District's system of internal control has not been conducted. The failure to monitor the internal control system places the District at risk that controls may not be either designed properly or operating effectively to provide reasonable assurance that controls will prevent, or detect and correct, material misstatements in a timely manner. Additionally, the District has no process to identify or communicate corrective actions to improve controls. Effective internal controls over financial reporting require the District to monitor and assess the quality of the system of internal control.

Due to the lack of adequate controls, the financial statement presented for audit contained material errors. The January 1, 2011 Cash and Investment balance was overstated by \$22,605, the December 31, 2011 Cash and Investment balance was overstated by \$355,100, and the December 31, 2012 Cash and Investment balance was overstated by \$6,376. In addition, the Disbursements reported for 2011 and 2012 were understated by \$332,495 and overstated by \$348,724, respectively. These errors were the result of not recognizing disbursements for financial reporting until the disbursements cleared the bank.

Audit adjustments were proposed, accepted by the District, and made to the financial statement presented in this report.

Governmental units should have internal controls in effect which provide reasonable assurance regarding the reliability of financial information and records, effectiveness and efficiency of operations, proper execution of management's objectives, and compliance with laws and regulations. Among other things, segregation of duties, safeguarding controls over cash and all other assets, and all forms of information processing are necessary for proper internal control.

Controls over the receipting, disbursing, recording, and accounting for the financial activities are necessary to avoid substantial risk of invalid transactions, inaccurate records and financial statements and incorrect decision making. (Accounting and Uniform Compliance Guidelines Manual for Special Districts, Chapter 10)

All documents and entries to records should be done in a timely manner to ensure that accurate financial information is available to allow the governmental unit to make informed management decisions and to help ensure compliance with IC 5-15-1-1 et seq., commonly referred to as the Public Records Law. (Accounting and Uniform Compliance Guidelines Manual for Special Districts State of Indiana, Chapter 10)

KOONTZ LAKE REGIONAL SEWER DISTRICT
FEDERAL FINDINGS
(Continued)

FINDING 2012-002 - THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

The District did not have a proper system of internal control in place to prevent, or detect and correct, errors on the Schedule of Expenditures of Federal Awards (SEFA). The Treasurer prepared the District's grant schedule on the Gateway reporting website, which is used to prepare the SEFA. The information was prepared and submitted without oversight, review, or approval.

The District should have proper controls in place over the preparation of the SEFA to ensure accurate reporting of federal awards. Without a proper system of internal control in place that operates effectively, material misstatements of the SEFA remained undetected.

During the audit of the SEFA, we noted that \$4,192,460 and \$330,033 in federal expenditures were omitted for the years ended December 31, 2011 and 2012, respectively. Audit adjustments were proposed, accepted by the District, and made to the SEFA presented in this report.

Governmental units should have internal controls in effect which provide reasonable assurance regarding the reliability of financial information and records, effectiveness and efficiency of operations, proper execution of management's objectives, and compliance with laws and regulations. Among other things, segregation of duties, safeguarding controls over cash and all other assets, and all forms of information processing are necessary for proper internal control.

Controls over the receipting, disbursing, recording, and accounting for the financial activities are necessary to avoid substantial risk of invalid transactions, inaccurate records and financial statements and incorrect decision making. (Accounting and Uniform Compliance Guidelines Manual for Special Districts, Chapter 10)

OMB Circular A-133, Subpart C, section .300 states in part: "The auditee shall: . . . (d) Prepare appropriate financial statements, including the schedule of expenditures of Federal Awards in accordance with section .310."

OMB Circular A-133, Subpart C, section .310(b) states in part:

"Schedule of expenditures of Federal awards. The auditee shall also prepare a schedule of expenditures of Federal awards for the period covered by the auditee's financial statements. While not required, the auditee may choose to provide information requested by Federal awarding agencies and pass-through entities to make the schedule easier to use. For example, when a Federal program has multiple award years, the auditee may list the amount of Federal awards expended for each award year separately. At a minimum, the schedule shall:

- (1) List individual Federal programs by Federal agency. For Federal programs included in a cluster of programs, list individual Federal programs within a cluster of programs. For R&D, total Federal awards expended shall be shown either by individual award or by Federal agency and major subdivision within the Federal agency. For example, the National Institutes of Health is a major subdivision in the Department of Health and Human Services.
- (2) For Federal awards received as a subrecipient, the name of the pass-through entity and identifying number assigned by the pass-through entity shall be included.
- (3) Provide total Federal awards expended for each individual Federal program and the CFDA number or other identifying number when the CFDA information is not available."

KOONTZ LAKE REGIONAL SEWER DISTRICT
FEDERAL FINDINGS
(Continued)

FINDING 2012-003 - CASH MANAGEMENT AND REPORTING

Federal Agency: Department of Agriculture
Federal Program: ARRA-Water and Waste Disposal Systems for Rural Communities - ARRA
CFDA Number: 10.781
Federal Award Number: IN-701-00-02

Management of the District has not established an effective internal control system, which would include segregation of duties, related to the grant agreement and the Cash Management and Reporting compliance requirements. The failure to establish an effective internal control system places the District at risk of noncompliance with the grant agreement and the compliance requirements. A lack of segregation of duties within an internal control system could also allow noncompliance with compliance requirements and allow the misuse and mismanagement of federal funds and assets by not having proper oversight, reviews, and approvals over the activities of the program.

The District has not designed or implemented adequate procedures to ensure that requests for grant funds and other reports are prepared accurately and submitted as required. The Treasurer prepared the grant draw requests, Estimate of Funds Needed, Form 440, Project Expenditure Reports, annual Balance Sheets, the Statement of Budget, Income and Equity, and the Section 312 ARRA reports without oversight, review, or approval.

An internal control system, including segregation of duties, should be designed and operate effectively to provide reasonable assurance that material noncompliance with the grant agreement or a compliance requirement of a federal program will be prevented, or detected and corrected, on a timely basis. In order to have an effective internal control system, it is important to have proper segregation of duties. This is accomplished by making sure proper oversight, reviews, and approvals take place and to have a separation of functions over certain activities related to the program. The fundamental premise of segregation of duties is that an individual or small group of individuals should not be in a position to initiate, approve, undertake, and review the same activity.

OMB Circular A-133, Subpart C, section .300 states in part:

"The auditee shall: . . . (b) Maintain internal control over Federal programs that provides reasonable assurance that the auditee is managing Federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements that could have a material effect on each of its Federal programs."

The failure to establish internal controls could enable material noncompliance to go undetected. Noncompliance with the grant agreement or the compliance requirements could result in the loss of federal funds to the District.

We recommended that the District's management establish controls, including segregation of duties, related to the grant agreement and compliance requirements listed above.

KOONTZ LAKE REGIONAL SEWER DISTRICT

P.O. Box 204
Walkerton, IN 46574

RE: 2012 SBOA AUDIT CORRECTIVE ACTION PLAN

Contact Person Responsible for Corrective Action: Michael McKenna
Contact Phone Number: 574 910-0033

Finding 2012-001 - Financial Transactions and Reporting

Although it has been believed by the Trustees that the KLRSD has had sufficient internal controls by segregating duties between a bookkeeper to record transactions, the Board to review claims and approve disbursements, the Treasurer to write checks and the President to countersign checks, it is recognized that the Treasurer is currently allowed to prepare and submit financial reports without separate review and approval.

The errors reported in this Finding were due to the Treasurers misunderstanding of the proper accounting definition of 'a disbursement'. The Treasurer operated under the belief that a disbursement did not occur until a check written was cleared by the bank and the account was charged. However, the Treasurer now understands that proper accounting practice dictates that a disbursement occurs when the check is written. This difference of understanding leads to incorrect year-end reporting of balances when checks are written in one calendar year and not cleared until the next calendar year.

The KLRSD will develop a written policy and procedure that assures all future financial reporting complies with proper accounting practice and will be reviewed by another Board member, a committee of Board members appointed by the Board President or by an independent accountant or accounting firm. Such policy and procedure will also include some mechanism to periodically monitor and evaluate the adequacy of internal controls by a committee of Board members appointed by the Board President or an independent consultant.

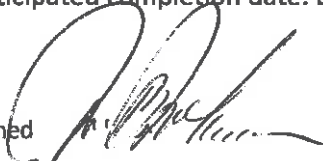
Finding 2012-002 – The Schedule of Expenditures of Federal Awards

The KLRSD will develop a written policy and procedure that assures all future federal award expenditures are reported on the SEFA and reviewed by another Board member, a committee of Board members appointed by the Board President or by an independent accountant or accounting firm.

Finding 2012-003 – Cash Management and Reporting

The KLRSD will develop a written policy and procedure that assures internal control, including segregation of duties such that the same individual will not be in the position to initiate, approve, undertake and review the same activity.

Anticipated completion date: December 31, 2015

Signed 

Title *TREASURER*

Date *10/19/15*

KOONTZ LAKE REGIONAL SEWER DISTRICT
AUDIT RESULT AND COMMENT

ORDINANCES AND RESOLUTIONS

The District has not created an operation and maintenance fund or sinking fund or separate construction account as required by bond ordinance 2009-01. The District's financial statement reports all financial transactions in a General fund.

Each governmental unit is responsible for complying with the ordinances, resolutions, and policies it adopts. (Accounting and Uniform Compliance Guidelines Manual for Special Districts, Chapter 10)

KOONTZ LAKE REGIONAL SEWER DISTRICT

P.O. Box 204
Walkerton, IN 46574

KOONTZ LAKE REGIONAL SEWER DISTRICT AUDIT RESULTS AND COMMENTS 2011 -2012

ORDINANCES AND RESOLUTIONS


The Regional Sewer District has not created an operation and maintenance fund or sinking fund or separate construction account as required by bond ordinance 2009-01. The District's financial statements show all financial transactions accounted for in a general fund.

KOONTZ LAKE REGIONAL SEWER DISTRICT RESPONSE:

The KLRSD has defined the following funds in 2015 for reporting purposes:

Operating
Principle and Interest (Sinking Fund)
Debt Service
Capital Improvement

There are no current construction plans nor funds available for construction and therefore no separate construction account has been defined.


TREASURER, KLRSD
10/19/15

KOONTZ LAKE REGIONAL SEWER DISTRICT
EXIT CONFERENCE

The contents of this report were discussed on October 19, 2015, with Michael B. McKenna, Treasurer, and with Gerald Weber, President of the Board.