B47392

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

SUPPLEMENTAL COMPLIANCE REPORT

OF

CITY OF ELKHART

ELKHART COUNTY, INDIANA

January 1, 2015 to December 31, 2015

FILED
12/29/2016

TABLE OF CONTENTS

Description	Page
Schedule of Officials	2
Transmittal Letter	3
Controller:	
Federal Findings:	
2015-001 - Internal Controls over Financial Transactions and Reporting	6-7
2015-002 - Preparation of the Schedule of Expenditures of Federal Awards	7-9
Corrective Action Plan	10-12
Audit Result and Comment:	
Overdrawn Cash Balances	13
Exit Conference	14
Community and Redevelopment:	
Federal Findings:	
2015-003 - Internal Controls over Community Development Block Grant/Entitlement Grants	16-17
2015-004 - Special Tests and Provisions - Wage Rate Determination	17-19
Corrective Action Plan	20-21
Exit Conference	22

SCHEDULE OF OFFICIALS

Office	Official	Term
Controller	Stephen J. Malone	01-01-15 to 12-31-15
	Jeffrey L. Spalding	01-01-16 to 12-31-16
Mayor	Dick Moore	01-01-12 to 12-31-15
	Timothy Neese	01-01-16 to 12-31-19
President of the Board of Public Works	Michael C. Machlan	01-01-15 to 12-31-15
	Carol McDowell	01-01-16 to 12-31-16
President of the Common Council	Brian A. Thomas	01-01-15 to 12-31-16

STATE OF INDIANA
AN EQUAL OPPORTUNITY EMPLOYER

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TO: THE OFFICIALS OF THE CITY OF ELKHART, ELKHART COUNTY, INDIANA

This report is supplemental to our audit report of the City of Elkhart (City), for the period from January 1, 2015 to December 31, 2015. It has been provided as a separate report so that the reader may easily identify any Federal Findings that pertain to the City. It should be read in conjunction with our Financial Statement and Federal Single Audit Report of the City, which provides our opinions on the City'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 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 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

December 1, 2016

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CONTROLLER
CITY OF ELKHART

FINDING 2015-001 - INTERNAL CONTROLS OVER FINANCIAL TRANSACTIONS AND REPORTING

Condition

There were multiple deficiencies in the internal control system of the City related to financial transactions and reporting.

1. *Lack of Segregation of Duties*: The City had not separated incompatible activities related to cash reconcilements.

   a. Cash reconcilements were prepared by employees in the Controller and Clerk's offices. There was no evidence that the completed reconcilements were reviewed by a second employee of those offices.

   b. Disbursements made from City funds by electronic funds transfer (EFT), journal entry, or other means, were created and recorded in the ledger by the Controller's office personnel. Claims were not prepared for these disbursements nor were they included within a schedule or docket presented to the Board of Public Works for their approval.

   c. The City established a bank account for the Lerner Theatre. Transactions within this bank account were not being recorded on the City Funds Ledger or any Ledger, a reconcilement was not being prepared for this bank account during the year, and complete financial transactions were not being properly reported on the Annual Financial Report (AFR). There was no review by management of the activity in this account.

2. *Monitoring of Controls*: The City had not developed a process to identify or communicate corrective actions to improve controls. Effective internal controls over financial reporting required the City to monitor and assess the quality of the system of internal control.

   a. The AFR was not reviewed; therefore, the omission of $2,624,409 in Bank of New York transactions in the Sewer Replacement and WWTP Revenue Fund #4 funds occurred. This resulted in the understatement of receipts and disbursements.

   b. The Controller's office did not complete a reconcilement of all funds of the City to all bank accounts and investments of the City. The bank reconcilement that was completed included numerous adjusting entries dating back to May 2014 that remain uncorrected as of August 2016. The December 31, 2015, reconcilement included unidentified differences that leave the bank $149,018 greater than the funds ledger cash and investment balance.

Criteria

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 Cities and Towns, Chapter 7)

Cause

Management of the City had not established a proper system of internal control that would have ensured proper reporting on the AFR. An evaluation of the City's system of internal control had not been conducted and management had not conducted a risk assessment related to the City's financial reporting and transactions.

Effect

The failure to establish controls could have enabled material misstatements or irregularities to remain undetected. The failure to monitor the internal control system placed the City at risk that controls may not be either designed properly or operating effectively to provide reasonable assurance that controls would have prevented, or detected and corrected, material misstatements in a timely manner.

Views of Responsible Officials

For the views of responsible officials, refer to the Corrective Action Plan that is part of this report.

FINDING 2015-002 - PREPARATION OF THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

Condition

The City 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 City should have proper controls in place over the preparation of the SEFA to ensure accurate reporting of federal awards. We noted the following errors:

1. Expenditures reported for Community Development Block Grants/Entitlement Grants were overstated by $45,362.

2. Vendor transactions were erroneously included in the SEFA.

3. Equitable Sharing Program was omitted from the SEFA.

4. Four grants listed either an incorrect pass-through agency or were listed as direct grants from the federal government when they actually were received from a pass-through.

5. Two grants listed an incorrect CFDA number.

6. Subrecipient awards were overstated for the Community Development Block Grants/ Entitlement Grants by $14,992.

Audit adjustments were proposed, accepted by the City, and made to the SEFA.

Criteria

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 Cities and Towns, Chapter 7)

2 CFR 200.508 states in part: "The auditee must: . . . (b) Prepare appropriate financial statements, including the schedule of expenditures of Federal awards in accordance with § 200.510 financial statements. . . ."

2 CFR 200.510(b) states:

"*Schedule of expenditures of Federal awards*. The auditee must also prepare a schedule of expenditures of Federal awards for the period covered by the auditee's financial statements which must include the total Federal awards expended as determined in accordance with § 200.502 Basis for determining Federal awards expended. 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 Federal award years, the auditee may list the amount of Federal awards expended for each Federal award year separately. At a minimum, the schedule must:

(1) List individual Federal programs by Federal agency. For a cluster of programs, provide the cluster name, list individual Federal programs within the cluster of programs, and provide the applicable Federal agency name. For R&D, total Federal awards expended must be shown either by individual Federal 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 must 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. For a cluster of programs also provide the total for the cluster.

(4) Include the total amount provided to subrecipients from each Federal program.

(5) For loan or loan guarantee programs described in § 200.502 Basis for determining Federal awards expended, paragraph (b), identify in the notes to the schedule the balances outstanding at the end of the audit period. This is in addition to including the total Federal awards expended for loan or loan guarantee programs in the schedule.

(6) Include notes that describe the significant accounting policies used in preparing the schedule, and note whether or not the auditee elected to use the 10% de minimis cost rate as covered in § 200.414 Indirect (F&A) costs."

Cause

Management had not established a system of internal control that would have ensured proper reporting of the SEFA.

Effect

Without a proper system of internal control in place that operated effectively, material misstatements of the SEFA remained undetected. The SEFA contained the errors identified in the *Condition*.

Views of Responsible Officials

For the views of responsible officials, refer to the Corrective Action Plan that is part of this report.

The Honorable
Timothy Neese
Mayor

Jeffrey L. Spalding
City Controller

City of Elkhart
city with a heart

City Controller's Office
229 S. Second St.
Elkhart, IN 46516

574.294.5471
Fax: 574.294.8491

CORRECTIVE ACTION PLAN

FINDING 2015-001

Contact Person Responsible for Corrective Action: Jeff Spalding, Controller or Jamie Arce, Deputy Controller
Contact Phone Number: 574-294-5471 x2014 or (574) 294-5471 x202

Views of Responsible Official: The City concurs with the finding.

Description of Corrective Action Plan:

1a.) The City will create a bank reconciliation summary report, to be prepared and signed by the Deputy Controller. That summary report, along with detailed support documents, will then be presented to the Controller for review and approval. Once approved, the Controller will sign and date the report.

1b.) The City will end the practice of posting electronic funds transfer (EFT) payments as journal entries. Instead, all EFT payments will be posted through the City's accounts payable system. By doing so, all EFT payments will be included on the accounts payable summary reviewed and approved by the Board of Public Works.

1c.) Initially the City will create a sub-fund (within the Lerner Theatre Fund) to account for the transactions of the Lerner Theatre Show Clearing bank account. The City will also begin exploring the legal requirements associated with the handling of those monies to determine whether or not a separate agency fund must be established for this purpose or alternatively, if the City may legally disavow any obligation to accounting for these transactions.

2a.) For 2014, gaps in accounting processes resulted in a failure to post all State Revolving Fund (SRF) transactions in the City's accounting system. To avoid this problem in the future, the City's Utility Finance Manager will be required to submit transactions for all revenues and disbursements of SRF monies throughout the year. If that is done properly then no discrepancies with the SRF bank accounts will exist at the time of entry data for the City's Annual Financial Report (AFR). Since the Utility Finance Manager must have accurate data to manage the City's SRF funds, that position is highly motivated to account for these transactions accurately.

2b.) The City will begin to include the following monies in the bank reconciliation process: a) Lerner Theater Show Clearing Account; b) Clerk's Court Fees Account; c) Clerk's Bail Bond Account; and d) Clerk's Trust Account. For the Lerner Show Clearing Account, the Controller's Office will include if in its regular bank reconciliation process. For the three (3) Clerk's bank accounts, the Deputy Controller will verify that those bank reconciliations have been completed and report the status on the bank reconciliation summary report submitted to the Controller.

For the numerous unrectified adjusting entries which have been carried as reconciling items, the City will identify the accuracy of as many as possible. For those that are determined to be inaccurate, they will be reversed in a single or a few reconciling journal entries.

The Honorable
Timothy Neese
Mayor

Jeffrey L. Spalding
City Controller

City of Elkhart
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City Controller's Office
229 S. Second St.
Elkhart, IN 46516

574.294.5471
Fax: 574.294.8491

Anticipated Completion Date: December 2016 and January 2017.

(Signature)

Controller
(Title)

November 28, 2016
(Date)

The Honorable
Timothy Neese
Mayor

Jeffrey L. Spalding
City Controller

City of Elkhart
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City Controller's Office
229 S. Second St.
Elkhart, IN 46516

574.294.5471
Fax: 574.294.8491

CORRECTIVE ACTION PLAN

FINDING 2015-002

Contact Person Responsible for Corrective Action: Jeff Spalding, Controller or Jamie Arce, Deputy Controller
Contact Phone Number: 574-294-5471 x2014 or (574) 294-5471 x202

Views of Responsible Official: The City concurs with the finding.

Description of Corrective Action Plan:

The City has had a Grant Writer position for a number of years. We will begin leveraging that position to also collect and organize all data associated with grants received by the City that must be reported on the Schedule of Expenditures of Federal Awards (SEFA). That individual is quite familiar with grant accounting and reporting requirements established by Federal agencies. He will use that knowledge to ensure that the SEFA is prepared accurately going forward.

Anticipated Completion Date: December 2016 and January 2017.

(Signature)

Controller
(Title)

November 28, 2016
(Date)

CONTROLLER
CITY OF ELKHART
AUDIT RESULT AND COMMENT

OVERDRAWN CASH BALANCES

The financial statements presented for audit included a Sales Tax fund with overdrawn cash balances at December 31, 2015, of $4,362.

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 governmental unit. (Accounting and Uniform Compliance Guidelines Manual for Cities and Towns, Chapter 7)

CONTROLLER
CITY OF ELKHART
EXIT CONFERENCE

The contents of this report were discussed on December 1, 2016, with Jeffrey L. Spalding, Controller; Jamie Arce, Deputy Controller; Richard Shively, Council member; Pam Kurpgeweit, Council member; and Mary Olson, Council member.

COMMUNITY AND REDEVELOPMENT
CITY OF ELKHART

FINDING 2015-003 - INTERNAL CONTROL OVER COMMUNITY DEVELOPMENT BLOCK GRANTS/ENTITLEMENT GRANTS

Federal Agency: Department of Housing and Urban Development
Federal Program: CDBG - Entitlement Grants
CFDA Number: 14.218
Federal Award Numbers and Years (or Other Identifying Numbers): B-08-MN-18-0002, B-11-MN-18-0002, B-13-MC-18-0015, B-14-MC-18-0015, B-15-MC-18-0015
Pass-Through Entity: Direct Grant

This is a repeat finding from the immediate prior year. The prior year finding number was 2014-003.

Condition

An effective internal control system was not in place at the City in order to ensure compliance with requirements related to the grant agreement and the following compliance requirements: Program Income and Reporting.

Program Income

The City had not designed or implemented internal control procedures to ensure compliance with the requirements for Program Income. The City did not have controls in place to ensure that program income was properly reported to the grantor agency or subsequently deducted from future reimbursement requests.

Reporting

The City had not designed or implemented internal control procedures to ensure compliance with the requirements for Reporting. There were no procedures in place to verify the information being submitted on required reports was complete and adequate. The City has indicated that a monthly reconcilement between the ledger and the Community Development department's grant records took place, however there was a lack of evidence that process has occurred.

Context

This applies to all the program income received by the City during 2015, and to each of the financial and performance reports required by the Department of Housing and Urban Development.

Criteria

2 CFR 200.303 states in part:

"The non-Federal entity must:

(a) Establish and maintain effective internal control over Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal awards in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in 'Standards for Internal Control in the Federal Government' issued by the Comptroller General of the United States or the 'Internal Control Integrated Framework', issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). . . ."

Cause

Management had not developed a system of internal controls that segregated key functions.

Effect

The failure to establish an effective internal control system placed the City at risk of noncompliance with the grant agreement and the compliance requirements. A lack of segregation of duties within an internal control system could have also allowed noncompliance with compliance requirements and allowed the misuse and mismanagement of federal funds and assets by not having proper oversight, reviews, and approvals over the activities of the program.

Questioned Costs

There were no questioned costs identified.

Recommendation

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

Views of Responsible Officials

For the views of responsible officials, refer to the Corrective Action Plan that is part of this report.

FINDING 2015-004 - SPECIAL TESTS AND PROVISIONS - WAGE RATE DETERMINATION

Federal Agency: Department of Housing and Urban Development
Federal Program: CDBG - Entitlement Grants
CFDA Number: 14.218
Federal Award Number and Year (or Other Identifying Number): B-08-MN-18-002,
B-11-MN-18-002,
B-13-MC-18-0015,
B-14-MC-18-0015,
B-15-MC-18-0015
Pass-Through Entity: Direct Grant

Condition

An effective internal control system was not in place at the City in order to ensure compliance with requirements related to the grant agreement and the following compliance requirement: Special Tests and Provisions - Wage Rate Requirements.

The City did not include language and documentation specific to Wage Rate Requirements in applicable contracts.

Context

This applied to six construction contracts in excess of $2,000. All six applicable contracts were tested; three of these contracts did not include a prevailing wage rate clause, thus those contracts were not in compliance with the wage rate requirements.

Criteria

2 CFR 200.303 states in part:

"The non-Federal entity must:

> (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in 'Standards for Internal Control in the Federal Government' issued by the Comptroller General of the United States or the 'Internal Control Integrated Framework', issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). . . ."

40 USC 3142(a) states:

"APPLICATION-The advertised specifications for every contract in excess of $2,000, to which the Federal Government or the District of Columbia is a party, for construction, alteration, or repair, including painting and decorating, of public buildings or public works of the Government or the District of Columbia that are located in a State or the District of Columbia and which requires or involves the employment of mechanics or laborers shall contain a provision stating the minimum wages to be paid various classes of laborers and mechanics."

Cause

Management had not developed a system of internal controls that segregated key functions. Management did not include the required clause within the applicable contracts.

Effect

The failure to establish internal controls enabled material noncompliance to go undetected which could have resulted in the loss of federal funds to the City.

Questioned Costs

There were no questioned costs identified.

Recommendation

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

Views of Responsible Officials

For the views of responsible officials, refer to the Corrective Action Plan that is part of this report.

City of Elkhart
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CORRECTIVE ACTION PLAN

FINDING 2015-003

Contact Person Responsible for Corrective Action: Crystal Welsh, Director of Development Services
Contact Phone Number: 574-294-5471 x 124

Views of Responsible Official: The City agrees with the finding related to internal controls over program income for programs and reporting under the US Department of Housing and Urban Development.

Description of Corrective Action Plan:
The Community, Economic and Redevelopment Department as of July 1, 2016 has instituted the following internal controls regarding to program income related to programs under the US Department of Housing and Urban Development.

All program income received for CDBG, NSP-1 and NSP-3 is forwarded to Laura Miller, CD Specialist for Housing to be receipted into the City's INCODE.

Laura Miller provides Joe Halter, CD Specialist for Compliance, with the receipt that is produced from INCODE so that he can report that Program Income into either IDIS for CDBG or DRGR for NSP-1 or NSP-3.

Joe Halter is responsible for all draws of funds for the CDBG, NSP-1 and NSP-3 programs.

When he is creating a draw request in the IDIS system – it identifies if Program Income is available for use at that time. If there is Program Income available Joe Halter uses those funds first and then funds the remaining request from the oldest Grant funds first. The draw request is approved by either Laura Miller or Crystal Welsh. When staff is completing the Consolidate Annual Performance and Evaluation Report (CAPER) a Program Income report from INCODE and IDIS are created and compared for consistency.

When he is creating a draw request in DRGR – the system required the use of any Program Income prior to requesting Grant funds. The draw request is approved by either Laura Miller or Crystal Welsh. When staff is completed the Quarterly Program Reports (QPR) in DRGR) a Program Income report from INCODE and DRGR are created and compared for consistency.

The CDBG program submits a FS425 quarterly cash report to HUD. This report is prepared by Joe Halter, approved and signed by Crystal Welsh and then submitted by Joe Halter to US HUD.

The NSP program submits Quarterly Progress Reports through the DRGR system. These reports are prepared by Joe Halter and reviewed by Crystal Welsh before submittal.

Anticipated Completion Date: July 1, 2016

(Signature)

Director of the Office of Development Services
(Title)

November 23, 2016
(Date)

City of Elkhart
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CORRECTIVE ACTION PLAN

FINDING 2015-004

Contact Person Responsible for Corrective Action: Crystal Welsh, Director of Development Services
Contact Phone Number: 574-294-5471 x 124

Views of Responsible Official: The City agrees with the finding related to internal controls over Special Tests and Provisions: Wage Rate Determination

Description of Corrective Action Plan:
The Community, Economic and Redevelopment Department as of July 1, 2016 has instituted the following internal controls regarding to Wage Rate Requirements programs under the US Department of Housing and Urban Development.

The City of Elkhart provides CDBG funds to local not-for-profit organizations known as Subrecipients to carry-out CDBG eligible activities. The Subrecipients are selected via an application process each calendar year. Subrecipient applications are reviewed and scored given an grant review sheet by Jenny Recinos. She and the Director meet to review the application score sheets and provide recommendations to the Redevelopment Commission for award of the funds. In the process of preparing a contract Jenny Recinos will work with the Director to identify any regulatory requirements triggered by the project. Starting in June 2017 when new agreements are signed, the agreement will also include a coversheet which indicates what regulatory requirements are triggered by the grant agreement. This will notify staff that additional review is required. When a construction project is part of a Subrecipient Agreement, Laura Miller, CD Specialist for Housing will be included in the review of the grant application and determining of appropriate regulatory requirements, specifically Wage Determination.

For any construction contract, once the Subrecipient Agreement is in place, Laura Miller will hold a meeting with the Subrecipient to ensure they understand the Wage Determination rules and responsibilities. She will work with the Subrecipient during the biding process to ensure compliance with wage determination rules at that phase of the project. Once a contractor is selected by the Subrecipient a pre-contract meeting will be held to ensure contract compliance and discuss construction requirements under the Davis-Bacon and Related Acts program including payroll and interview. Any claim for CDBG funds related to a construction project will be reviewed for compliance by Laura Miller and approved by Crystal Welsh. A copy of the Subrecipient contract with the construction contractors will be required prior to payment for the project to ensure compliance with the Wage Determination language in that contract.

Anticipated Completion Date: July 1, 2017

(Signature)

Director of the Office of Development Services
(Title)

November 23, 2016
(Date)

COMMUNITY AND REDEVELOPMENT
CITY OF ELKHART
EXIT CONFERENCE

The contents of this report were discussed on December 1, 2016, with Jeffrey L. Spalding, Controller; Jamie Arce, Deputy Controller; Richard Shively, Council member; Pam Kurpgeweit, Council member; and Mary Olson, Council member.