

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, 2013 to December 31, 2016



FILED
12/28/2017

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SCHEDULE OF OFFICIALS

<u>Office</u>	<u>Official</u>	<u>Term</u>
Clerk-Treasurer	Michael Griffin	01-01-12 to 12-31-19
President of the Town Council	Brian Novak	01-01-13 to 11-01-13
	Bernard Zemen	11-02-13 to 12-31-13
	Daniel Vassar	01-01-14 to 12-31-14
	Mark Herak	01-01-15 to 12-31-15
	Bernard Zemen	01-01-16 to 12-31-16
	Daniel Vassar	01-01-17 to 12-31-17
Public Works Director	John Bach	01-01-13 to 12-31-17



STATE OF INDIANA
AN EQUAL OPPORTUNITY EMPLOYER

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

This report is supplemental to our examination report of the Town of Highland (Town), for the period from January 1, 2013 to December 31, 2016. It has been provided as a separate report so that the reader may easily identify any Examination Results and Comments that pertain to the Town. It should be read in conjunction with our Financial Statements Examination Report of the Town, which provides our opinion on the Town's financial statements. 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 Examination Result and Comment contained herein describes the identified reportable instance 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 Examination Result and Comment, incorporated within this report, was not verified for accuracy.

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

December 14, 2017

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CLERK-TREASURER
TOWN OF HIGHLAND

CLERK-TREASURER
TOWN OF HIGHLAND
EXAMINATION RESULT AND COMMENT

INTERNAL CONTROLS AND ERROR CORRECTION

The Town established an internal control system related to financial transactions and reporting; however, the controls were not adequately documented and not always effective. The internal control system provided for a review of the financial information submitted in the Indiana Gateway for governmental units financial reporting system (Gateway), which is the source of the financial statement. The review process, although not adequately documented, did detect errors; however, those errors were not corrected in a timely manner.

The Town maintained computerized ledgers on a modified accrual basis, but prepared the financial statements on the regulatory basis of accounting. The financial statements were prepared using a revenue and expenditure report from the computerized accounting software. Those reports included bank to bank transfers during 2013 through 2016, which were included as both a revenue and an expenditure within a given fund.

During 2015, the Town recorded various transactions that occurred during 2014 in the financial software. Those transactions were categorized as both prior period adjustments and journal entries. Although they were recorded in 2015, they were dated December 31, 2014. The Town also adjusted the amounts that were reported in Gateway without any documentation for the adjustments being made. As a result, the 2014 and 2015 financial statements were not reflective of the activity of the Town. These various adjustments resulted in the financial statement receipts and disbursements being understated by material amounts in 2014 and overstated by material amounts in 2015.

Adjustments were proposed, approved by Town management, and made to the financial statements.

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:

CLERK-TREASURER
TOWN OF HIGHLAND
EXAMINATION RESULT AND COMMENT
(Continued)

"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. . . .

The Green Book identifies a list of control activity categories that are meant only to illustrate the range and variety of control activities; the list is by no means all inclusive, but is reproduced here for reference purposes: . . .

- Accurate and timely recording of transactions. . . ."

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)

Town of Highland

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Thursday, December 21, 2017

Paul Joyce, State Examiner
State Board of Accounts
State of Indiana
302 W. Washington Street
Indianapolis, Indiana 46204

**Re: Town of Highland Responses to audit result and comment
Accompanying the filing of the FY 2013, 2014, 2015 & 2016 Revised.
Filed pursuant to IC 5-11-5-1(b)**

Overview and Operating Ethos.

This officer and the Town of Highland highly affirm the role of the Indiana State Board of Accounts as the entity tasked with performing the periodic external audits for the municipality, pursuant to IC 5-11 et seq. It is our belief that the State Board of Accounts, a public entity, provides the best, cost-effective performance of this essential duty in a professional and *disinterested* but not *uninterested* manner, promoting good stewardship, public accounting and the essential interests of the public we are both oath-bound to serve. Please, nothing in this response to the audit results and comments should be seen as departing from this ambient context, and deeply held opinion of this agency.

Further, this officer has relied and continues to rely enthusiastically upon the State Board of Accounts to review the compliance and financial reporting of the Town generally and the office of the Clerk-Treasurer in particular, welcoming its comments as instructive and helpful, consistent with the general objective of this officer to pursue excellence in the performance of the duties of office. This has been true for the whole of this officer's career as a public finance professional, now completing 26 years as the Town's elected fiscal officer. It is acknowledged that the governing body (management), is ultimately responsible for the policies of internal control, and this officer as fiscal officer is primarily responsible for the implementation of the controls affecting the control environment, providing reasonable – *not absolute assurance* -- reducing error or misstatement.

Appreciation. Highland further acknowledges and is very grateful to the State Board of Accounts for conducting and completing this examination, covering the period January 1, 2013 through December 31, 2016, to meet an undue deadline imposed by Standard and Poor's. It is noted that this examination was planned, organized and performed under a sudden and unexpected requirement by the rating agency. While an external audit

Town Council

Bernie Zeman
Ward One

Mark A. Herak
Ward Two

Dan Vassar
Ward Three

Steven Wagner
Ward Four

Konnie Kuiper
Ward Five

John Bach
Public Works Director

Rhett Tauber
Attorney

Clerk-Treasurer
Michael Griffin

frequency of not less than four years is lawful under the new risk based criteria of IC 5-11-1-25(b), Standard and Poor's suddenly and without reasonable notice, insisted that for its Indiana entities that had rated debt, the frequency of external audits must be 3 years or less. Further, it threatened to downgrade existing rated debt, if audits were not conducted before year-end. Highland and this officer recognize with deep appreciation the marshaling of the external audit resources by the State Board of Accounts to protect Highland's rated debt from any downgrading. Thank you very much.

Response to audit results and comments.

The *Response to audit results and comments* section should be read in the context of *Significant aspects of the entity or its environment including complex or unusual activities* section, which immediately follows, as it is of essence to this response.

Noting the foregoing, this audited entity remains perplexed and vexed by the comments regarding adequacy of documentation and the reporting issues. The controls in place operated such that the disparities noted in the audit report *were discovered* within a reasonable time by Highland following the first AFRs reporting and prior to audit. At the outset of the audit, the proper officer explained that the posted AFRs on the gateway needed to have correcting or adjusting entries. Further, this officer and the deputy indicated that Highland wished to enter the known changes to correct the incorrect balances in AFRs as posted. *(The next section explains that there was an ongoing software conversion, which in part explained the corrections.)* The Town was able to provide -- whether produced by employed staff or provided by the engaged accounting firm -- supporting documentation identifying the balances that required changes and the adjustments, in some cases after some added industry, tied to the adjustments the audited entity had identified.

There was also added documentation in work papers supporting reconciliations associated with a daily cash clearing account, that were available and supported adjustments made to the working financial records of the Town.

Highland fully concurs that at all times the manual or computerized records, subsidiary ledgers, control ledger and reconciled bank balance must agree. This guidance is what informed Highland's desire to address the variances by rendering the adjustments.

So, Highland takes exception from the audit reports statements regarding documentation and **in particular with the statement in the third paragraph of the report. That statement nearly traduces the audit entity, which is a profound departure from the usual professional and customary practices that Highland has experienced with the State Board of Accounts.**

Further, this officer and Highland are further dispirited that the audit report dilates upon variances in financial reporting, which were identified by it and for which it wished to correct or adjust at the outset of the audit. However, in the course of the audit, the lead examiner instructed the Town to let the reports remain as posted on AFR portal of Gateway. He then instructed Highland could later change them with adjustments that the auditors would later provide.

In fact, this officer had delayed completing the Form 13 -- in which the proper officer confirms among other things, that the financial documents are ready for audit -- knowing that the reports required adjustments, most of which were identified in work papers, reports and associated documents generated prior to the examination.

Highland notes the following provisions of law:

The state examiner shall appoint assistants not exceeding the number required to administer this article. The assistants are to be known as "field examiners" and are at all times subject to the order and direction of the state examiner. Field examiners shall inspect and examine accounts of all state agencies, municipalities, and other governmental units, entities, or instrumentalities. (IC 5-11-1-7(a))

The state examiner, personally or through the deputy examiners, field examiners, or private examiners, shall examine all accounts and all financial affairs of every public office and officer, state office, state institution, and entity. (IC 5-11-1-9(a))

A public officer who ... fails to follow the directions of the state examiner in keeping the accounts of the officer's office; ... or interferes with an examiner in the discharge of the examiner's official duties; commits a Class B infraction and forfeits office. (IC 5-11-1-10(2) & (4))

Highland regards the field examiners as officials through which the state examiner conducts the audit. So, a field examiner's instruction is respected -- greeted with the same dignity as an instruction of the state examiner. This officer honored the examiner's instruction regarding the adjustments. Further, this officer did include a special note or disclaimer on the Form 13 when finally filed during the field work.

Highland again gratefully acknowledges that this audit was being conducted by the State Board of Accounts owing to and under the added pressure of a fast approaching deadline unexpectedly imposed by Standard and Poor's for all of its Indiana entities for which it had rated debt. This officer believes that the desire and need to complete the process in an accelerated manner may have informed the examiner's instruction. Had the audit been conducted without the added deadline pressures, the entity may have been granted leave to enter its correcting adjustments.

Additionally, while there were many adjustments to make in the four-year audit period, this officer is further dispirited by a reference to "material amounts". In one case, there was an incorrect reported balance for a capital fund at the end of one fiscal year, which was corrected in the capital fund's starting balance in the immediately succeeding year. Again, Highland noted that it needed to correct the preceding year. Pursuant to the instruction of the examiner, even though we identified this and had the documentary support to make the needed adjustment, Highland yielded to the instruction of the examiner and did not render the correction. Ideally, external examinations should be corrective and heuristic. In yielding to the examiner's instruction, receiving a comment regarding reporting seemingly in consequence of honoring the instruction seems at least inequitable. The comment itself strongly and unreasonably implicates that there was no due diligence in place, which is not the case.

Controls were sufficient that the incorrect balances were discovered by Highland well before the examiners' arrived. Further, it is supposed that had it not been for the need to conduct the audit in the timetable made necessary by Standard and Poor's, the AFRs would have been corrected before any external audit. The cause of some of the reports requiring correction had to do with the ongoing protracted conversion and implementation of the new financial and accounting software. The system is dynamic and integrated as explained before. Some reporting was affected by the learning curve of staff. However, once discovered, additional training and consultation with the Software vendor was put in place.

Highland further notes that during the protracted conversion process for the new financial and accounting software, completing the bank reconciliations was challenged in part owing to the use of a clearing account for daily cash. The use of a cash clearing account, *considered a public finance best practice*, is used to support the daily deposit of receipts for governmental and enterprise charges. Unable to perform complete bank reconciliation in the system with this daily cash account, the clearing account was reconciled with an external report and spreadsheet. Over the period of the software conversion for both utility billing and governmental funds accounting, the

adjustments were considerable in the beginning but were much less as the system and staff were increasingly acclimated.

Corrective measures inferred from the audit report. Highland possesses written policies describing segregation of duties and identifying assignments for certain tasks consistent with this control concept. This officer states that Highland's data entry processes for the AFR on the Gateway portal, can be enhanced perhaps by including adding still another step of review before the submission of data to the Gateway. Final submission will remain solely under the purview of the office holder.

Further, Highland concurs with the audit report comment stating that the changes to the Annual Financial Reports should and could have been more timely. As stated, the delay was due in part to the ongoing software conversion process and the nettlesome issue with the reconciliation of the daily cash account with the system. Our first approach will be to enhance processes to support accurate data entry. However, should correction or adjustments become needed, *absent the confluence of experiences memorialized in the following section*, the adjustments will be posted timely.

During the course of the audit, the Gateway portal was closed to external users, for its annual processing maintenance and data roll over. However, once advised by the State Board of Accounts, the adjusting entries will be posted to the portal for the AFRs.

The audit results and comments references variances reported as *bank to bank transfers*, which is related to the manner in which the software processes payroll. While balancing, we concur that it unduly inflates financial activity. The software vendor has been contacted to take steps to address this.

We again note, internal controls are a combination of policies, people and procedures or practices that management relies upon to obtain reasonable assurance that the government is meeting its objectives in regard to effectiveness, efficiency, the safeguarding of compliance, and the reliability of reporting. The controls worked as Highland discovered in reasonable time where there were needs for correcting reported balances. *But for the instruction of the examiner* and perhaps even the added undue deadline imposed upon the audit by Standard and Poor's, Highland would have taken steps to correct the reports and apply the adjustments.

Significant Aspects of the Entity or its Environment including complex or unusual activities.

I want to restate the significant circumstances that took place during the four-year period being examined, January 1, 2013 through December 31, 2017. *(These were reported on the FORM 9, used by the State Board of Accounts as part of the entrance process to provide information about the entity being examined).* It was hoped that it would inform the audit judgments regarding the examination.

Please do not read what follows too incredulously. Further, these are only reported to offer context, and more fully inform the examiners as well as others regarding the variables affecting the environment. Beginning January 1, 2013 extending for a protracted period of 48 months the responsible officer *experienced an undue confluence of life challenging and unlikely incidents. It is understood that any single one of these could well be experienced by anyone. However, it is the confluence that is unusual. These in part explain the cessation of the voluntary, heightened financial reporting employing the format of the CAFR. Instead, Highland simply complied with the legal requirements of IC 5-11-1-4.*

A series of parental and personal life challenges. The office holder's mother was hospitalized on January 1, 2013 with a seizure caused by a brain cancer mass. She died in April 2013, following a brief period of hospice care in which the office holder assisted his father in her end of life care. The office holder's father then suffered congestive heart failure three days after her burial. His condition involved many hospitalizations in advance of a remediating procedure and several following as the repaired valve was acclimated. During the progression of the disease, the office holder's father was frequently hospitalized and required increased care, including engaging home care personnel and supervising his temporal affairs until he passed in February 2016. In August 2015, the office holder lost his father in law. Two other close relatives died, offering an undue and highly unusual confluence of external events affecting the office holder, one passing in May ending with the death of a close cousin in December 2016.

In addition, during this same period, the office holder was diagnosed and treated for prostate cancer in May 2013. This required surgery and a six-week period of convalescence. With a concern about the possible recurrence of the cancer, the office holder underwent radiation therapy daily for a period running from November 19, 2015 through January 14, 2016. (The prognosis is positive.)

Frequent and sometimes protracted absences from the office and its work became necessary in consequence of these life challenging matters.

Implementation, conversion to new financial accounting and billing software. In October 2013, the then serving deputy clerk-treasurer was recruited to take a new position offering a substantial increase in pay and responsibility. Her successor, the current deputy clerk-treasurer, began her duties on October 14, 2013. Her predecessor's last day, was October 6, 2017, although she did come in for one week to train. Given this limited transition time, the deputy was nascent to our workplace, further complicating the workplace's demands.

Moreover, all this came with the implementation, data conversion and transition to a new accounting software package that is now operating as hoped. Its implementation has been something of an ordeal and the decision to introduce it came before the staff member's departure was known. *It would not have been undertaken if the departure was known ahead of time by the office-holder.*

Unusual staff turnover. This process of implementation was still further complicated by additional, unusual turnover in several staff positions including the encumbering officer (accounts payable), two utility clerks, and a chancery bursar clerk. This represented a 65% turnover. As of this writing, there is a vacancy in the position of encumbering officer and one of the chancery/bursar clerk's positions. *Half of the remaining staff have tenure of 3 or less years.* Still further complicating is the nature of the new software, which is dynamic, and integrated, causing incorrect balances when a later adjustment or correction was instituted or when a process in the utility billing was instituted, having an impact on the general ledger, which was discovered in the course of the on-going practices.

In short, this 48-month period has been a profoundly daunting and challenging period. This is offered as context. While confounded by all this, this office has moved forward with software implementation. Compensating for the nascent staffing or absence of organization capacity, we engaged external accounting capacity to assist with the on-going software conversion, particularly regarding the bank reconciliations and to enhance our understanding of the new software.

Final Comments

The audit entity believes that the examiners were professional in their execution of the recent four-year examination. Perhaps the imperative of completing the examination in the short amount of time insisted upon by *Standard and Poor's* affected some of the comments in the audit report. The audit report should be informed by assaying the office and the office holder. In addition to a review of the control environment, risk assessment, control

activities, information and communication employed and monitoring, there should be some explication of the practitioners and the regular practices of the unit examined, as well as any relevant circumstances -- both exogenous as well as endogenous. (*Software conversions are rarely seamless or without complications, for example.*) It is hoped that the examiners consider the temperament of management and the working ethos of the unit. This officer affirms Highland's long public record of continuing improvement and endeavoring to conform to the highest standards of financial stewardship. Internal controls are always a work in progress. The decision to produce an audit result and comment rather than a management letter, this officer believes can unduly misrepresent and mischaracterize the comportment and ethos of the responsible public officer(s) of the Town in a fashion that however unintended, still traduces in some cases.

This response is prepared to offer additional insight and an expository reply to the audit comments and results report.

The TOWN of HIGHLAND

A handwritten signature in blue ink, appearing to read "Michael W. Griffin", with a long horizontal line extending to the right.

Michael W. Griffin, M.P.A., IAMC/MMC/CPFA/CPFIM/CMO
Clerk-Treasurer

TOWN OF HIGHLAND
Management Oversight of Nonaudit Services
January 1, 2013 to December 31, 2016

Name of Individual Designated by Management to oversee nonaudit services:

Michael W. Griffin

Title of Individual:

Town Clerk-Treasurer

Review of nonaudit services performed:

(Management's designee should check each item as it is reviewed.)

Statement of Receipts, Disbursements, and Cash and Investment Balances:

- Beginning cash and investments agree with prior year ending balances for each fund and for the total of all funds.
- Ending balances are reported correctly for each fund and the total of all funds.
(See designee's note at end)
- Titles of funds are reported correctly for each fund. **(Yes. Limited by Gateway. I have provided a separate list and fund number to give full names of funds. See note below.)**

Notes to the Financial Statement:

- Notes to the financial statement as compiled accurately reflect the governmental unit.
(We have made some recommended minor changes to the texts and they are attached)

Combining Schedule of Receipts, Disbursements, and Cash and Investment Balances:

- Beginning cash and investments agree with prior year ending balances for each fund.
- Ending balances are reported correctly for each fund.
(See designee's note at end)
- Titles of funds are reported correctly for each fund.
The fund titles are sometimes modified from the enacted full titles, owing to limitations in the Gateway and a historic shorthand. However, the fund numbers in the AFR correspondent to the fund numbers and funds in our records. I am providing with this form a list of the fund number, the depicted name and the full name for your further use.

Other Supplementary Schedules (Schedule of Payable and Receivables, Schedule of Leases and Debt, Schedule of Capital Assets)

- All information is correct and presented as management intended.

Schedule of Expenditures of Federal Awards:

- All federal grants disbursed are included in the schedule of expenditures.
- Amounts reported for each program is correct.
- Amounts provided to subrecipients are correct.

TOWN OF HIGHLAND
Management Oversight of Nonaudit Services
January 1, 2013 to December 31, 2016

Total federal awards expended per the schedule are correct.


All Statements, Schedules, and Notes:

Fund names are correct. (Fund names will appear as shown in the report.)
The fund titles are sometimes modified from the enacted full titles, owing to limitations in the Gateway and a historic shorthand. However, the fund numbers in the AFR correspondent to the fund numbers and funds in our records. I am providing with this form a list of the fund number, the depicted name and the full name for your further use.

Unit name is correct throughout report.

As the management designee, I have reviewed the financial statement, notes to the financial statement, and schedule of expenditures of federal awards for each of the aforementioned items. These items were prepared by use of our books and records. Our books and records adequately support the financial statement, notes to the financial statement, and schedule of expenditures of federal awards prepared, and accordingly, I approve these items as compiled by the State Board of Accounts, except where indicated. I understand that slight modifications such as spelling, grammatical and formatting errors may be corrected during the processing of our report by the State Board of Accounts. I acknowledge that the financial statement, including the notes to the financial statement, and the schedule of expenditures of federal awards are our responsibility. I have determined that the regulatory basis of accounting, as established by the Indiana State Board of Accounts, is an acceptable basis of presentation.

Management designee's note: The cash balances agree with the filed and posted AFRs for the Town of Highland for the period under audit. It is noted that the town of Highland noted and reported to the examiners that owing to our review, three of the four reports would require correcting adjustments to the cash balances owing to discovery of adjustments made necessary owing to the nascent training on the new financial accounting and reporting software, first implemented in October 2013. The Town of Highland expressed willingness to provide corrected AFRs, but were advised to allow the examiners to prepare adjustments to the Town.


Michael W. Griffin
Title: Clerk-Treasurer
Date: 12/01/2017

CLERK-TREASURER
TOWN OF HIGHLAND
EXIT CONFERENCE

The contents of this report were discussed on December 14, 2017, with Michael Griffin, Clerk-Treasurer; Katie Minchuk, Deputy Clerk-Treasurer; and Mark Herak, Town Council member.