

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

SUPPLEMENTAL COMPLIANCE REPORT

OF

CITY OF HAMMOND

LAKE COUNTY, INDIANA

January 1, 2017 to December 31, 2017



**FILED**  
11/21/2018



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SCHEDULE OF OFFICIALS

<u>Office</u>	<u>Official</u>	<u>Term</u>
City Controller	Heather Garay	01-01-17 to 12-31-18
Mayor	Thomas M. McDermott, Jr.	01-01-16 to 12-31-19
City Clerk	Robert J. Golec	01-01-16 to 12-31-19
City Judge	Amy Jorgensen	11-21-16 to 12-31-19
President of the Board of Public Works and Safety	Stanley J. Dostani Heather Garay	01-01-17 to 02-07-18 02-08-18 to 12-31-18
President of the Common Council	Janet Venecz	01-01-17 to 12-31-18
Sanitary District Manager	Marty J. Wielgos	01-01-17 to 12-31-18
Sanitary District Business Manager	Rachel Montes	01-01-17 to 12-31-18
President of the Sanitary District Board of Commissioners	Dean Button Sam Dimopoulos	01-01-17 to 12-31-17 01-01-18 to 12-31-18
Chief Executive Operator of the Water Utility	Edward Krusa	01-01-17 to 12-31-18
Water Utility Office Manager	Deborah L. Van Meter	01-01-17 to 12-31-18
President of the Water Works Board of Directors	Sharon M. Daniels	01-01-17 to 12-31-18
Director of the Port Authority	Milan A. Kruszynski	01-01-17 to 12-31-18
Chairman of the Port Authority Board of Directors	Thomas E. Kuhn Jeffery Smith	01-01-17 to 12-31-17 01-01-18 to 12-31-18
Port Authority Financial Director	Richard A. Szany	01-01-17 to 12-31-18



**STATE OF INDIANA**  
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TO: THE OFFICIALS OF THE CITY OF HAMMOND, LAKE COUNTY, INDIANA

This report is supplemental to our audit report of the City of Hammond (City), for the period from January 1, 2017 to December 31, 2017. It has been provided as a separate report so that the reader may easily identify any Federal Findings and Audit Results and Comments 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/](http://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 Results and Comments 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 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 Corrective Action Plan for the Federal Findings and Official Response to the Audit Results and Comments, incorporated within this report, were not verified for accuracy.

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

October 9, 2018

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CITY CONTROLLER  
CITY OF HAMMOND

CITY CONTROLLER  
CITY OF HAMMOND  
FEDERAL FINDINGS

***FINDING 2017-001***

Subject: Financial Transactions and Reporting  
Audit Findings: Material Weakness, Noncompliance

*Repeat Finding*

This is a repeat finding from the immediately prior audit. The prior audit finding numbers were 2016-001 and 2016-002.

*Condition*

There were several deficiencies in the internal control system of the City related to financial transactions and reporting. The internal controls implemented by the City related to cash and investments, receipts, disbursements, and financial reporting, including the financial statement and the Schedule of Expenditures of Federal Awards (SEFA), were not effective. Furthermore, the internal controls were not monitored and evaluated for effectiveness.

*Cash and Investments (Bank Reconciliations) - City*

The control over cash and investments and trust bank reconciliations was not effective and did not ensure that bank reconciliations were prepared and reviewed in a timely manner, or that reconciling items were corrected in a timely manner.

Reconciliations of the record balances to the depository balances were not prepared and reviewed in a timely manner. Trust account reconciliations were also not completed in a timely manner. January through October trust account reconciliations were not completed until November of 2017.

As of December 31, 2017, the City had accumulated reconciling adjustments to the payroll account, which had not been corrected. A \$16,065,281 transfer due from the payroll bank account to the general bank account had been carried since December 31, 2014. Additional reconciling items in the payroll account included accumulated balances, receipts, and disbursements of payroll and payroll withholding amounts totaling \$19,695,009. The net effect of these reconciling items was a decrease in the balance of the payroll bank account of \$3,629,728. The City refunded the 2012 Potash Bond in 2017. A fund was not created for the new 2017 Potash Refunding Bond in the financials. The trust account for the bond had an ending cash and investment balance of \$7,107,175, as of December 31, 2017.

*Receipts, Disbursements, and Financial Reporting - City and Port Authority*

The City and Port Authority implemented internal controls over receipts, disbursements, and financial reporting; however, the controls were not effective and did not ensure that transactions were properly recorded in the ledgers and reported in the financial statement.

The City and Port Authority opened new bank accounts during 2017 and recorded bank-to-bank transfers of \$35,335,252 and \$18,600,000 as receipts and disbursements, respectively. The receipts and disbursements reported in the financial statement were overstated by the amount of the bank-to-bank transfers.

CITY CONTROLLER  
CITY OF HAMMOND  
FEDERAL FINDINGS  
(Continued)

The City advance refunded the 2012 Potash Bond in 2017. The bond proceeds were placed in trust to retire the 2012 bonds as they become due. A fund was not created for the 2017 Potash Refunding Bond Trust in either the ledger or the financial statement. The cash and investment balance and receipts were understated in the financial statement by \$7,107,175.

*Disbursements - Sanitary District*

The Accounts Payable Clerk prepared the checks and recorded the invoices to the accounting system without oversight or review.

The Payroll Manager was responsible for the entire payroll process and was able to make payroll rate changes in the computer system. The Sanitary District Manager implemented a procedure to select up to 15 employees each pay period whose payroll records were audited by an accountant. That audit did not include a verification of the pay distribution to the proper funds and accounts.

*Financial Reporting - Water Utility*

The Office Manager prepared and reported the cash and investment balances, receipts, and disbursements in the Indiana Gateway for Government Units financial reporting system, which was the source for the City's financial statement, without any prior review or oversight. The reports were submitted to the Water Board for review; however, the Water Board approved the reports after the information had been submitted.

*Schedule of Expenditures of Federal Awards (SEFA)*

The City did not have a proper system of internal controls in place to prevent, or detect and correct, errors on the SEFA. Due to the lack of controls, the SEFA presented for audit included the following errors:

1. Insurance in effect during the year of \$2,000,000 was reported for the Beach Monitoring and Notification Program Implementation Grants. No supporting documentation for the entry was provided.
2. The state Maternal and Child Health Services Block Grant to the States expenditures of \$1,605 were reported in error.
3. The Urban and Community Forestry Program expenditures of \$30,000 were omitted.
4. The Crime Victim Compensation Grant expenditures of \$1,271 were omitted.
5. The State Clean Diesel Grant Program expenditures of \$55,000 were omitted.

Audit adjustments were proposed, accepted by the City, and made to the SEFA presented in this report.

*Context*

The lack of controls and the noncompliance were systemic issues throughout the audit period.

CITY CONTROLLER  
CITY OF HAMMOND  
FEDERAL FINDINGS  
(Continued)

*Criteria*

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. . . ."

"Evaluations are used to determine whether each of the five components of internal control is present and functioning. These evaluations may be conducted on an ongoing or periodic basis. The criteria used are developed by the oversight body, elected officials, management, governing boards, or recognized standard-setting bodies or regulators. . . .

A baseline of the current state of the internal control system is compared against the original design of the internal control system. The baseline consists of issues and deficiencies identified in the internal control system. The results of the monitoring process are evaluated and documented. . . .

Management remediates identified issues. . . ."

Indiana Code 5-13-6-1(e) states: "All local investment officers shall reconcile at least monthly the balance of public funds, as disclosed by the records of the local officers, with the balance statements provided by the respective depositories."

All financial transactions pertaining to the unit must be recorded in the records of the unit at the time of the transaction. (Accounting and Uniform Compliance Guidelines Manual for Cities and Towns, Chapter 1)

All documents and entries to records must be made in a timely manner to ensure that accurate financial information is available to allow the unit to make informed management decisions and to help ensure compliance with IC 5-15-1-1. (Accounting and Uniform Compliance Guidelines Manual for Cities and Towns, Chapter 1)

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. . . ."

CITY CONTROLLER  
CITY OF HAMMOND  
FEDERAL FINDINGS  
(Continued)

2 CFR 200.510(a) states:

*"Financial statements.* The auditee must prepare financial statements that reflect its financial position, results of operations or changes in net assets, and, where appropriate, cash flows for the fiscal year audited. The financial statements must be for the same organizational unit and fiscal year that is chosen to meet the requirements of this part. However, non-Federal entity-wide financial statements may also include departments, agencies, and other organizational units that have separate audits in accordance with § 200.514 Scope of audit, paragraph (a) and prepare separate 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 that 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."

CITY CONTROLLER  
CITY OF HAMMOND  
FEDERAL FINDINGS  
(Continued)

*Cause*

Management of the City had not established a proper and effective system of internal control. Management had not conducted a risk assessment related to the City's financial reporting and transactions.

*Effect*

The failure to establish controls enabled misstatements and irregularities to occur on the financial statement and the SEFA. The failure to monitor the internal control system placed the City at risk that controls were either not designed properly or not operating effectively to provide reasonable assurance that controls would have prevented, or detected and corrected, material misstatements in a timely manner.

*Recommendation*

We recommended that the City's management design and implement a proper system of internal controls, which would segregate key functions and also perform periodic monitoring of its system of internal controls. We also recommended that the City reconcile bank accounts in accordance with state statute, monitor the recording of receipts and disbursements, and ensure the accuracy of the SEFA.

*Views of Responsible Officials*

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

**FINDING 2017-002**

Subject: Highway Planning and Construction Cluster - Period of Performance

Federal Agency: Department of Transportation

Federal Program: Highway Planning and Construction

CFDA Number: 20.205

Federal Award Numbers and Years (or Other Identifying Numbers): DES#1297017, DES#1382659,  
DES#1500221, DES#1500724,  
DES#1601163, DES#1601164

Pass-Through Entity: Indiana Department of Transportation

Compliance Requirement: Period of Performance

Audit Finding: Material Weakness

*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 Period of Performance compliance requirement.

The grant expenditures were not reviewed to ensure that federal funds were not expended outside of the period of performance.

*Context*

The lack of controls was a systemic issue throughout the audit period.

CITY CONTROLLER  
CITY OF HAMMOND  
FEDERAL FINDINGS  
(Continued)

*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). . . ."

*Cause*

Management had not developed or implemented a system of internal controls to ensure compliance with the grant agreement and the period of performance requirements.

*Effect*

The failure to establish an effective internal control system placed the City at risk of noncompliance with the grant agreement and the period of performance requirements. A lack of segregation of duties within an internal control system could have also allowed noncompliance with the compliance requirement 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 related to the grant agreement and the Period of Performance compliance requirement.

*Views of Responsible Officials*

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



Heather Garay, J.D.  
Controller

October 9, 2018

## CORRECTIVE ACTION PLAN

### **Section II – Financial Statement Findings**

#### Finding 2017-001 – **FINANCIAL TRANSACTIONS AND REPORTING**

Contact Person Responsible for Corrective Action: Heather Garay, City Controller

Contact Phone Number: 219-853-6324

#### Corrective Action Plan:

##### Cash and Investments (Bank Reconciliations) – City

- a. We partially concur with the finding.

The City reconciles all bank accounts on a monthly basis. The bank reconciliations are then reviewed by the City Controller. The outstanding amount in the payroll account has carried from 2014 and is related to a bank to bank transfer for the payroll sweeping account. The City will work with a consultant and the financial software provider to attempt to resolve the outstanding payroll transfers from 2014. All other bank accounts are balanced monthly. The City began preparing bank reconciliations for all trust accounts in 2017. The trust activity was reconciled for the entire year for 2017 and are now reconciled and reviewed monthly.

Anticipated Completion Date: December 2018

##### Receipts, Disbursements, and Financial Reporting - City and Port Authority

- b. We concur with the finding.

The City and Port Authority operate on the same financial software. The reports generated by the financial software are unable to distinguish between expenditure and non-expenditure transactions related to bank to bank transfers. 2017 had a significant number of these transactions related to transferring funds to new bank accounts to earn better interest rates and as required by bond agreements. The City and Port Authority will work with their software provider to exclude non-expenditure transfers from reports used for the preparation of the annual financial report.

The City has implemented new controls for the administration of trust accounts which include instructions to set-up the funds and accounts timely, the reconciliation of trust accounts and reporting of activity.

Anticipated Completion Date: March 2019

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**Heather Garay, J.D.**  
Controller

Disbursements - Sanitary District  
c. We concur with the finding.

Due to the timing of the 2016 audit, this finding was not resolved in 2017 but has been resolved in 2018.

Completion Date: 2018

Financial Reporting – Water Utility  
d. We partially concur with the finding.

The Water Utility established a corrective action plan in February 2018 to address the 2016 audit finding. It stated that financials would be reviewed and approved by the Water Utility COO and Board of Directors prior to submitting them to the controller for inclusion in the annual financial report. The anticipated completion date was December 2018. The Water Utility began sending these reports to the board and COO for approval in February 2018. The financials were submitted to the Controller prior to the next board meeting and were then approved by the board a few days later. No adjustments were required following the boards review and the financial report was submitted with the original entries. Going forward, the board will review and approve the financials prior to submission the Controller.

Anticipated Completion Date: March 2019

Schedule of Expenditures of Federal Awards (SEFA)  
e. We concur with the finding.

The Controller will work with other departments to develop a procedure for the proper reporting and verification of federal awards. All entries will be reviewed by an additional individual prior to the submission of the SEFA.

Anticipated Completion Date: March 2018

\_\_\_\_\_  
(Signature)

\_\_\_\_\_  
Controller  
(Title)

10/9/2018

\_\_\_\_\_  
(Date)

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Heather Garay, J.D.  
Controller

October 9, 2018

CORRECTIVE ACTION PLAN

**Section III – Federal Award Findings and Questioned Costs**

Finding 2017-002 – Highway Planning and Construction Cluster - Period of Performance  
Contact Person Responsible for Corrective Action: Heather Garay, City Controller  
Contact Phone Number: 219-853-6324

Corrective Action Plan:

- a. We concur with the finding.

Although all federal grants tested met the compliance requirements of the Period of Performance, there was no documentation to verify the compliance requirements were reviewed for accuracy. The City will put in place controls to document compliance reviews for all federal grants.

Anticipated Completion Date: March 2019

\_\_\_\_\_  
(Signature)

\_\_\_\_\_  
Controller  
(Title)

10/9/2018

\_\_\_\_\_  
(Date)

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CITY CONTROLLER  
CITY OF HAMMOND  
AUDIT RESULTS AND COMMENTS

**ADVANCE PAYMENTS**

A similar comment also appeared in 12 prior reports, including the 4 most recent Reports B45294, B47291, B47309, and B49726, entitled *PAYROLL DEFICIENCIES*.

Employee compensation, hours, and leave time were reported by the departmental payroll clerks to the City Controller's office on a biweekly "Payroll Earnings Forecast" (forecast). The forecasts were submitted for payroll processing by the Monday or Tuesday prior to the pay date, which was on the following Friday. Salaried employees were paid for the prior and current week and were, therefore, paid in advance of performing the service. This pay also did not reflect leave time used for the period covered.

Indiana Code 5-7-3-1 states in part: "Public officers may not draw or receive their salaries in advance. . . ."

**PAYROLL DEFICIENCY - LEAVE POLICIES**

A similar comment also appeared in 12 prior reports, including the 4 most recent Reports B45294, B47291, B47309, and B49726, entitled *PAYROLL DEFICIENCIES*.

The City abided by negotiated union agreements for sick and injured leaves and benefits for firefighters and police officers. The union agreement was effective for the period of January 1, 2017 through December 31, 2020. The agreement did not contain the details of the leave and benefits policies. The City amended the Fire Department Rules and Regulations Section 3, item C (Calling off sick policy), which stated the regular biweekly salary and all insurance benefits would be paid while on sick leave. However, it did not address the number of days or hours of sick leave the police officers were entitled to. The City also amended the Police Department General Order #02-01 and approved General Order #18-02, which stated the regular biweekly salary and all insurance benefits would be paid while on sick leave. However, it did not address the number of days or hours of sick leave the police officers were entitled to. We could not determine what the policies entailed; therefore, we could not determine if the City complied with the approved policies.

Each unit must adopt a written policy regarding the accrual and use of leave time and compensatory time and the payment of overtime. Negotiated labor contracts approved by the governing body would be considered as written policy. The policy must conform to the requirements of all state and federal regulatory agencies. (Accounting and Uniform Compliance Guidelines Manual for Cities and Towns, Chapter 1)



**Heather Garay, J.D.**  
Controller

**CITY OF HAMMOND**

October 23, 2018

State Board of Accounts  
302 West Washington Street, Room E418  
Indianapolis, IN 46204-2765

Re: State Board of Accounts Examination and Audit Results and Comments  
(Exam Period: January 1, 2017 – December 31, 2017)

### **Advanced Payments**

#### Response

The City of Hammond's 2017 Salary Ordinance states, "For 2017 the payday shall be every other Friday commencing on January 13<sup>th</sup>, 2017, for a total of 26 pays." This allows for paydays to remain on an every other week schedule. This schedule has been maintained for at least 40 years. Salaried employees' annual salary is divided by the number of pay dates in the calendar year and that amount reflect the employees' bi-weekly pay. The City's Employee Handbook and department policies require advanced notification of scheduled vacations and planned personal time. The City utilizes payroll earnings forecasts to project time off. Unplanned and emergency leaves are not reflected until the following pay. The City retains the ability to pull-back payroll funds paid to employees that separate from the City with unearned compensation. In the event that timing prevents the City from pulling back funds, the former employee is required to repay the unearned funds. Overtime pay is paid after it is earned. The City will continue to research ways in which to change the pay schedule so that time is earned before it is paid without imposing an undue burden on employees by forcing them to have extended periods without pay.

### **Payroll Deficiency – Leave Policies (City of Hammond)**

#### Response

The negotiated union contracts for Police and Fire for the period of January 1, 2017 through December 31, 2020 do not include a set number of days allotted for sick leave. The Rules and Regulations for each department outline the required procedures to request sick leave and the salary and benefits paid during that time if the leave is approved. The Chiefs retain the discretion to approve or deny sick leave according to the outlined procedures. The City will work with the Administration, Chiefs and Police and Fire Department to develop language that more clearly defines the sick leave policy in the Rules and Regulations so that proper testing of the policy will be possible during future audits.

### **Delinquent Wastewater Accounts**

#### Response

1. The Hammond Sanitary District staff, Hammond City Controller and the Hammond Water Department CEO met to discuss the process for delinquent wastewater fees and penalties after the conclusion of the audit. The following will be the new procedure effective November 2018:
  - a. The Hammond Sanitary District will receive monthly reports from the Hammond Water Department for delinquent accounts.

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-16-

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**Heather Garay, J.D.**  
Controller

**CITY OF HAMMOND**

- b. An Accounts Receivable Clerk will verify owner name and address and create a spreadsheet with all necessary information to certify and record the wastewater fees and penalties with the County Auditor and County Recorder.
- c. The Accounts Receivable Clerk will then send the prepared sewer lien report to the Hammond Sanitary District attorney. The attorney will follow the Indiana Code for the process of certifying and recording the lien with the appropriate County offices.

**Payroll Deficiency – Leave Policies (Fire Department)**

Response

The negotiated union contracts for the Fire department for the period of January 1, 2017 through December 31, 2020 do not include a set number of days allotted for sick leave. The Rules and Regulations for the department outline the required procedures to request sick leave and the salary and benefits paid during that time if the leave is approved. The Chief retains the discretion to approve or deny sick leave according to the outlined procedures. The City will work with the Administration, Fire Chief and Fire Department to develop language that more clearly defines the sick leave policy in the Rules and Regulations so that proper testing of the policy will be possible during future audits.

**Payroll Deficiency – Leave Policies (Police Department)**

Response

The negotiated union contracts for the Police department for the period of January 1, 2017 through December 31, 2020 do not include a set number of days allotted for sick leave. The Rules and Regulations for the department outline the required procedures to request sick leave and the salary and benefits paid during that time if the leave is approved. The Chief retains the discretion to approve or deny sick leave according to the outlined procedures. The City will work with the Administration, Police Chief and Police Department to develop language that more clearly defines the sick leave policy in the Rules and Regulations so that proper testing of the policy will be possible during future audits.



(Signature)

Heather Garay, City Controller  
(Title)

October 23, 2018  
(Date)



CITY CONTROLLER  
CITY OF HAMMOND  
EXIT CONFERENCE

The contents of this report were discussed on October 9, 2018, with Thomas M. McDermott, Jr., Mayor; Heather Garay, City Controller; Robert Markovich, Common Council member; Pete Torres, Common Council member; Anthony Higgs, Common Council member; Scott Rakos, Common Council member; and Phil Taillon, Chief of Staff.

SANITARY DEPARTMENT  
CITY OF HAMMOND

SANITARY DEPARTMENT  
CITY OF HAMMOND  
FEDERAL FINDING

***FINDING 2017-001***

Subject: Financial Transactions and Reporting  
Audit Findings: Material Weakness, Noncompliance

*Repeat Finding*

This is a repeat finding from the immediately prior audit. The prior audit finding numbers were 2016-001 and 2016-002.

*Condition*

There were several deficiencies in the internal control system of the City related to financial transactions and reporting. The internal controls implemented by the City related to cash and investments, receipts, disbursements, and financial reporting, including the financial statement and the Schedule of Expenditures of Federal Awards (SEFA), were not effective. Furthermore, the internal controls were not monitored and evaluated for effectiveness.

*Cash and Investments (Bank Reconciliations) - City*

The control over cash and investments and trust bank reconciliations was not effective and did not ensure that bank reconciliations were prepared and reviewed in a timely manner, or that reconciling items were corrected in a timely manner.

Reconciliations of the record balances to the depository balances were not prepared and reviewed in a timely manner. Trust account reconciliations were also not completed in a timely manner. January through October trust account reconciliations were not completed until November of 2017.

As of December 31, 2017, the City had accumulated reconciling adjustments to the payroll account, which had not been corrected. A \$16,065,281 transfer due from the payroll bank account to the general bank account had been carried since December 31, 2014. Additional reconciling items in the payroll account included accumulated balances, receipts, and disbursements of payroll and payroll withholding amounts totaling \$19,695,009. The net effect of these reconciling items was a decrease in the balance of the payroll bank account of \$3,629,728. The City refunded the 2012 Potash Bond in 2017. A fund was not created for the new 2017 Potash Refunding Bond in the financials. The trust account for the bond had an ending cash and investment balance of \$7,107,175, as of December 31, 2017.

*Receipts, Disbursements, and Financial Reporting - City and Port Authority*

The City and Port Authority implemented internal controls over receipts, disbursements, and financial reporting; however, the controls were not effective and did not ensure that transactions were properly recorded in the ledgers and reported in the financial statement.

The City and Port Authority opened new bank accounts during 2017 and recorded bank-to-bank transfers of \$35,335,252 and \$18,600,000 as receipts and disbursements, respectively. The receipts and disbursements reported in the financial statement were overstated by the amount of the bank-to-bank transfers.

SANITARY DEPARTMENT  
CITY OF HAMMOND  
FEDERAL FINDING  
(Continued)

The City advance refunded the 2012 Potash Bond in 2017. The bond proceeds were placed in trust to retire the 2012 bonds as they become due. A fund was not created for the 2017 Potash Refunding Bond Trust in either the ledger or the financial statement. The cash and investment balance and receipts were understated in the financial statement by \$7,107,175.

*Disbursements - Sanitary District*

The Accounts Payable Clerk prepared the checks and recorded the invoices to the accounting system without oversight or review.

The Payroll Manager was responsible for the entire payroll process and was able to make payroll rate changes in the computer system. The Sanitary District Manager implemented a procedure to select up to 15 employees each pay period whose payroll records were audited by an accountant. That audit did not include a verification of the pay distribution to the proper funds and accounts.

*Financial Reporting - Water Utility*

The Office Manager prepared and reported the cash and investment balances, receipts, and disbursements in the Indiana Gateway for Government Units financial reporting system, which was the source for the City's financial statement, without any prior review or oversight. The reports were submitted to the Water Board for review; however, the Water Board approved the reports after the information had been submitted.

*Schedule of Expenditures of Federal Awards (SEFA)*

The City did not have a proper system of internal controls in place to prevent, or detect and correct, errors on the SEFA. Due to the lack of controls, the SEFA presented for audit included the following errors:

1. Insurance in effect during the year of \$2,000,000 was reported for the Beach Monitoring and Notification Program Implementation Grants. No supporting documentation for the entry was provided.
2. The state Maternal and Child Health Services Block Grant to the States expenditures of \$1,605 were reported in error.
3. The Urban and Community Forestry Program expenditures of \$30,000 were omitted.
4. The Crime Victim Compensation Grant expenditures of \$1,271 were omitted.
5. The State Clean Diesel Grant Program expenditures of \$55,000 were omitted.

Audit adjustments were proposed, accepted by the City, and made to the SEFA presented in this report.

*Context*

The lack of controls and the noncompliance were systemic issues throughout the audit period.

SANITARY DEPARTMENT  
CITY OF HAMMOND  
FEDERAL FINDING  
(Continued)

*Criteria*

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. . . ."

"Evaluations are used to determine whether each of the five components of internal control is present and functioning. These evaluations may be conducted on an ongoing or periodic basis. The criteria used are developed by the oversight body, elected officials, management, governing boards, or recognized standard-setting bodies or regulators. . . .

A baseline of the current state of the internal control system is compared against the original design of the internal control system. The baseline consists of issues and deficiencies identified in the internal control system. The results of the monitoring process are evaluated and documented. . . .

Management remediates identified issues. . . ."

Indiana Code 5-13-6-1(e) states: "All local investment officers shall reconcile at least monthly the balance of public funds, as disclosed by the records of the local officers, with the balance statements provided by the respective depositories."

All financial transactions pertaining to the unit must be recorded in the records of the unit at the time of the transaction. (Accounting and Uniform Compliance Guidelines Manual for Cities and Towns, Chapter 1)

All documents and entries to records must be made in a timely manner to ensure that accurate financial information is available to allow the unit to make informed management decisions and to help ensure compliance with IC 5-15-1-1. (Accounting and Uniform Compliance Guidelines Manual for Cities and Towns, Chapter 1)

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. . . ."

SANITARY DEPARTMENT  
CITY OF HAMMOND  
FEDERAL FINDING  
(Continued)

2 CFR 200.510(a) states:

*"Financial statements.* The auditee must prepare financial statements that reflect its financial position, results of operations or changes in net assets, and, where appropriate, cash flows for the fiscal year audited. The financial statements must be for the same organizational unit and fiscal year that is chosen to meet the requirements of this part. However, non-Federal entity-wide financial statements may also include departments, agencies, and other organizational units that have separate audits in accordance with § 200.514 Scope of audit, paragraph (a) and prepare separate 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 that 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."

SANITARY DEPARTMENT  
CITY OF HAMMOND  
FEDERAL FINDING  
(Continued)

*Cause*

Management of the City had not established a proper and effective system of internal control. Management had not conducted a risk assessment related to the City's financial reporting and transactions.

*Effect*

The failure to establish controls enabled misstatements and irregularities to occur on the financial statement and the SEFA. The failure to monitor the internal control system placed the City at risk that controls were either not designed properly or not operating effectively to provide reasonable assurance that controls would have prevented, or detected and corrected, material misstatements in a timely manner.

*Recommendation*

We recommended that the City's management design and implement a proper system of internal controls, which would segregate key functions and also perform periodic monitoring of its system of internal controls. We also recommended that the City reconcile bank accounts in accordance with state statute, monitor the recording of receipts and disbursements, and ensure the accuracy of the SEFA.

*Views of Responsible Officials*

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



Heather Garay, J.D.  
Controller

October 9, 2018

## CORRECTIVE ACTION PLAN

### **Section II – Financial Statement Findings**

#### Finding 2017-001 – **FINANCIAL TRANSACTIONS AND REPORTING**

Contact Person Responsible for Corrective Action: Heather Garay, City Controller

Contact Phone Number: 219-853-6324

#### Corrective Action Plan:

##### Cash and Investments (Bank Reconciliations) – City

- a. We partially concur with the finding.

The City reconciles all bank accounts on a monthly basis. The bank reconciliations are then reviewed by the City Controller. The outstanding amount in the payroll account has carried from 2014 and is related to a bank to bank transfer for the payroll sweeping account. The City will work with a consultant and the financial software provider to attempt to resolve the outstanding payroll transfers from 2014. All other bank accounts are balanced monthly. The City began preparing bank reconciliations for all trust accounts in 2017. The trust activity was reconciled for the entire year for 2017 and are now reconciled and reviewed monthly.

Anticipated Completion Date: December 2018

##### Receipts, Disbursements, and Financial Reporting - City and Port Authority

- b. We concur with the finding.

The City and Port Authority operate on the same financial software. The reports generated by the financial software are unable to distinguish between expenditure and non-expenditure transactions related to bank to bank transfers. 2017 had a significant number of these transactions related to transferring funds to new bank accounts to earn better interest rates and as required by bond agreements. The City and Port Authority will work with their software provider to exclude non-expenditure transfers from reports used for the preparation of the annual financial report.

The City has implemented new controls for the administration of trust accounts which include instructions to set-up the funds and accounts timely, the reconciliation of trust accounts and reporting of activity.

Anticipated Completion Date: March 2019

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Controller's Office  
5925 Calumet Avenue  
Hammond, Indiana 46320

**219.853.6324**

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**Heather Garay, J.D.**  
Controller

Disbursements - Sanitary District  
c. We concur with the finding.

Due to the timing of the 2016 audit, this finding was not resolved in 2017 but has been resolved in 2018.

Completion Date: 2018

Financial Reporting – Water Utility  
d. We partially concur with the finding.

The Water Utility established a corrective action plan in February 2018 to address the 2016 audit finding. It stated that financials would be reviewed and approved by the Water Utility COO and Board of Directors prior to submitting them to the controller for inclusion in the annual financial report. The anticipated completion date was December 2018. The Water Utility began sending these reports to the board and COO for approval in February 2018. The financials were submitted to the Controller prior to the next board meeting and were then approved by the board a few days later. No adjustments were required following the boards review and the financial report was submitted with the original entries. Going forward, the board will review and approve the financials prior to submission the Controller.

Anticipated Completion Date: March 2019

Schedule of Expenditures of Federal Awards (SEFA)  
e. We concur with the finding.

The Controller will work with other departments to develop a procedure for the proper reporting and verification of federal awards. All entries will be reviewed by an additional individual prior to the submission of the SEFA.

Anticipated Completion Date: March 2018

\_\_\_\_\_  
(Signature)

\_\_\_\_\_  
Controller  
(Title)

10/9/2018

\_\_\_\_\_  
(Date)

City of Hammond  
Controller's Office  
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SANITARY DEPARTMENT  
CITY OF HAMMOND  
AUDIT RESULT AND COMMENT

***DELINQUENT WASTEWATER ACCOUNTS***

The same comment also appeared in prior Reports B47291, B47309, and B49726.

Delinquent wastewater fees and penalties had not been certified to the County Auditor nor recorded with the County Recorder.

Indiana Code 36-9-23-33 states in part:

". . . (c) . . . the officer charged with the collection of fees and penalties assessed under this chapter shall enforce their payment. As often as the officer determines is necessary in a calendar year, the officer shall prepare either of the following:

- (1) A list of the delinquent fees and penalties that are enforceable under this section, which must include the following:
  - (A) The name or names of the owner or owners of each lot or parcel of real property on which fees are delinquent.
  - (B) A description of the premises, as shown by the records of the county auditor.
  - (C) The amount of the delinquent fees, together with the penalty.
  - (D) An individual instrument for each lot or parcel of real property on which the fees are delinquent."

(d) The officer shall record a copy of each list or each individual instrument with the county recorder . . .

(f) . . . Using the lists and instruments prepared under subsection (c) and recorded under subsection (d), the officer shall, not later than ten (10) days after the list or each individual instrument is recorded under subsection (c), certify to the county auditor a list of the unpaid liens for collection with the next May installment of property taxes. . . ."

SANITARY DEPARTMENT  
CITY OF HAMMOND  
EXIT CONFERENCE

The contents of this report were discussed on October 9, 2018, with Thomas M. McDermott, Jr., Mayor; Heather Garay, City Controller; Robert Markovich, Common Council member; Pete Torres, Common Council member; Anthony Higgs, Common Council member; Scott Rakos, Common Council member; Phil Taillon, Chief of Staff; Marty J. Wielgos, Sanitary District Manager; Rachel Montes, Sanitary District Business Manager; Patrick Moore, Sanitary District Board of Commissioners member; and Joseph P. Allegretti, Sanitary District Attorney.

WATER DEPARTMENT  
CITY OF HAMMOND

WATER DEPARTMENT  
CITY OF HAMMOND  
FEDERAL FINDING

***FINDING 2017-001***

Subject: Financial Transactions and Reporting  
Audit Findings: Material Weakness, Noncompliance

*Repeat Finding*

This is a repeat finding from the immediately prior audit. The prior audit finding numbers were 2016-001 and 2016-002.

*Condition*

There were several deficiencies in the internal control system of the City related to financial transactions and reporting. The internal controls implemented by the City related to cash and investments, receipts, disbursements, and financial reporting, including the financial statement and the Schedule of Expenditures of Federal Awards (SEFA), were not effective. Furthermore, the internal controls were not monitored and evaluated for effectiveness.

*Cash and Investments (Bank Reconciliations) - City*

The control over cash and investments and trust bank reconciliations was not effective and did not ensure that bank reconciliations were prepared and reviewed in a timely manner, or that reconciling items were corrected in a timely manner.

Reconciliations of the record balances to the depository balances were not prepared and reviewed in a timely manner. Trust account reconciliations were also not completed in a timely manner. January through October trust account reconciliations were not completed until November of 2017.

As of December 31, 2017, the City had accumulated reconciling adjustments to the payroll account, which had not been corrected. A \$16,065,281 transfer due from the payroll bank account to the general bank account had been carried since December 31, 2014. Additional reconciling items in the payroll account included accumulated balances, receipts, and disbursements of payroll and payroll withholding amounts totaling \$19,695,009. The net effect of these reconciling items was a decrease in the balance of the payroll bank account of \$3,629,728. The City refunded the 2012 Potash Bond in 2017. A fund was not created for the new 2017 Potash Refunding Bond in the financials. The trust account for the bond had an ending cash and investment balance of \$7,107,175, as of December 31, 2017.

*Receipts, Disbursements, and Financial Reporting - City and Port Authority*

The City and Port Authority implemented internal controls over receipts, disbursements, and financial reporting; however, the controls were not effective and did not ensure that transactions were properly recorded in the ledgers and reported in the financial statement.

The City and Port Authority opened new bank accounts during 2017 and recorded bank-to-bank transfers of \$35,335,252 and \$18,600,000 as receipts and disbursements, respectively. The receipts and disbursements reported in the financial statement were overstated by the amount of the bank-to-bank transfers.

WATER DEPARTMENT  
CITY OF HAMMOND  
FEDERAL FINDING  
(Continued)

The City advance refunded the 2012 Potash Bond in 2017. The bond proceeds were placed in trust to retire the 2012 bonds as they become due. A fund was not created for the 2017 Potash Refunding Bond Trust in either the ledger or the financial statement. The cash and investment balance and receipts were understated in the financial statement by \$7,107,175.

*Disbursements - Sanitary District*

The Accounts Payable Clerk prepared the checks and recorded the invoices to the accounting system without oversight or review.

The Payroll Manager was responsible for the entire payroll process and was able to make payroll rate changes in the computer system. The Sanitary District Manager implemented a procedure to select up to 15 employees each pay period whose payroll records were audited by an accountant. That audit did not include a verification of the pay distribution to the proper funds and accounts.

*Financial Reporting - Water Utility*

The Office Manager prepared and reported the cash and investment balances, receipts, and disbursements in the Indiana Gateway for Government Units financial reporting system, which was the source for the City's financial statement, without any prior review or oversight. The reports were submitted to the Water Board for review; however, the Water Board approved the reports after the information had been submitted.

*Schedule of Expenditures of Federal Awards (SEFA)*

The City did not have a proper system of internal controls in place to prevent, or detect and correct, errors on the SEFA. Due to the lack of controls, the SEFA presented for audit included the following errors:

1. Insurance in effect during the year of \$2,000,000 was reported for the Beach Monitoring and Notification Program Implementation Grants. No supporting documentation for the entry was provided.
2. The state Maternal and Child Health Services Block Grant to the States expenditures of \$1,605 were reported in error.
3. The Urban and Community Forestry Program expenditures of \$30,000 were omitted.
4. The Crime Victim Compensation Grant expenditures of \$1,271 were omitted.
5. The State Clean Diesel Grant Program expenditures of \$55,000 were omitted.

Audit adjustments were proposed, accepted by the City, and made to the SEFA presented in this report.

*Context*

The lack of controls and the noncompliance were systemic issues throughout the audit period.

WATER DEPARTMENT  
CITY OF HAMMOND  
FEDERAL FINDING  
(Continued)

*Criteria*

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. . . ."

"Evaluations are used to determine whether each of the five components of internal control is present and functioning. These evaluations may be conducted on an ongoing or periodic basis. The criteria used are developed by the oversight body, elected officials, management, governing boards, or recognized standard-setting bodies or regulators. . . .

A baseline of the current state of the internal control system is compared against the original design of the internal control system. The baseline consists of issues and deficiencies identified in the internal control system. The results of the monitoring process are evaluated and documented. . . .

Management remediates identified issues. . . ."

Indiana Code 5-13-6-1(e) states: "All local investment officers shall reconcile at least monthly the balance of public funds, as disclosed by the records of the local officers, with the balance statements provided by the respective depositories."

All financial transactions pertaining to the unit must be recorded in the records of the unit at the time of the transaction. (Accounting and Uniform Compliance Guidelines Manual for Cities and Towns, Chapter 1)

All documents and entries to records must be made in a timely manner to ensure that accurate financial information is available to allow the unit to make informed management decisions and to help ensure compliance with IC 5-15-1-1. (Accounting and Uniform Compliance Guidelines Manual for Cities and Towns, Chapter 1)

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. . . ."

WATER DEPARTMENT  
CITY OF HAMMOND  
FEDERAL FINDING  
(Continued)

2 CFR 200.510(a) states:

*"Financial statements.* The auditee must prepare financial statements that reflect its financial position, results of operations or changes in net assets, and, where appropriate, cash flows for the fiscal year audited. The financial statements must be for the same organizational unit and fiscal year that is chosen to meet the requirements of this part. However, non-Federal entity-wide financial statements may also include departments, agencies, and other organizational units that have separate audits in accordance with § 200.514 Scope of audit, paragraph (a) and prepare separate 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 that 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."

WATER DEPARTMENT  
CITY OF HAMMOND  
FEDERAL FINDING  
(Continued)

*Cause*

Management of the City had not established a proper and effective system of internal control. Management had not conducted a risk assessment related to the City's financial reporting and transactions.

*Effect*

The failure to establish controls enabled misstatements and irregularities to occur on the financial statement and the SEFA. The failure to monitor the internal control system placed the City at risk that controls were either not designed properly or not operating effectively to provide reasonable assurance that controls would have prevented, or detected and corrected, material misstatements in a timely manner.

*Recommendation*

We recommended that the City's management design and implement a proper system of internal controls, which would segregate key functions and also perform periodic monitoring of its system of internal controls. We also recommended that the City reconcile bank accounts in accordance with state statute, monitor the recording of receipts and disbursements, and ensure the accuracy of the SEFA.

*Views of Responsible Officials*

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



Heather Garay, J.D.  
Controller

October 9, 2018

## CORRECTIVE ACTION PLAN

### **Section II – Financial Statement Findings**

#### Finding 2017-001 – **FINANCIAL TRANSACTIONS AND REPORTING**

Contact Person Responsible for Corrective Action: Heather Garay, City Controller

Contact Phone Number: 219-853-6324

#### Corrective Action Plan:

##### Cash and Investments (Bank Reconciliations) – City

- a. We partially concur with the finding.

The City reconciles all bank accounts on a monthly basis. The bank reconciliations are then reviewed by the City Controller. The outstanding amount in the payroll account has carried from 2014 and is related to a bank to bank transfer for the payroll sweeping account. The City will work with a consultant and the financial software provider to attempt to resolve the outstanding payroll transfers from 2014. All other bank accounts are balanced monthly. The City began preparing bank reconciliations for all trust accounts in 2017. The trust activity was reconciled for the entire year for 2017 and are now reconciled and reviewed monthly.

Anticipated Completion Date: December 2018

##### Receipts, Disbursements, and Financial Reporting - City and Port Authority

- b. We concur with the finding.

The City and Port Authority operate on the same financial software. The reports generated by the financial software are unable to distinguish between expenditure and non-expenditure transactions related to bank to bank transfers. 2017 had a significant number of these transactions related to transferring funds to new bank accounts to earn better interest rates and as required by bond agreements. The City and Port Authority will work with their software provider to exclude non-expenditure transfers from reports used for the preparation of the annual financial report.

The City has implemented new controls for the administration of trust accounts which include instructions to set-up the funds and accounts timely, the reconciliation of trust accounts and reporting of activity.

Anticipated Completion Date: March 2019

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**Heather Garay, J.D.**  
Controller

Disbursements - Sanitary District  
c. We concur with the finding.

Due to the timing of the 2016 audit, this finding was not resolved in 2017 but has been resolved in 2018.

Completion Date: 2018

Financial Reporting – Water Utility  
d. We partially concur with the finding.

The Water Utility established a corrective action plan in February 2018 to address the 2016 audit finding. It stated that financials would be reviewed and approved by the Water Utility COO and Board of Directors prior to submitting them to the controller for inclusion in the annual financial report. The anticipated completion date was December 2018. The Water Utility began sending these reports to the board and COO for approval in February 2018. The financials were submitted to the Controller prior to the next board meeting and were then approved by the board a few days later. No adjustments were required following the boards review and the financial report was submitted with the original entries. Going forward, the board will review and approve the financials prior to submission the Controller.

Anticipated Completion Date: March 2019

Schedule of Expenditures of Federal Awards (SEFA)  
e. We concur with the finding.

The Controller will work with other departments to develop a procedure for the proper reporting and verification of federal awards. All entries will be reviewed by an additional individual prior to the submission of the SEFA.

Anticipated Completion Date: March 2018

\_\_\_\_\_  
(Signature)

\_\_\_\_\_  
Controller  
(Title)

10/9/2018

\_\_\_\_\_  
(Date)

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WATER DEPARTMENT  
CITY OF HAMMOND  
EXIT CONFERENCE

The contents of this report were discussed on October 9, 2018, with Thomas M. McDermott, Jr., Mayor; Heather Garay, City Controller; Robert Markovich, Common Council member; Pete Torres, Common Council member; Anthony Higgs, Common Council member; Scott Rakos, Common Council member; Phil Taillon, Chief of Staff; Edward Krusa, Chief Executive Operator of the Water Utility; Deborah L. Van Meter, Water Utility Office Manager; Sharon M. Daniels, President of the Waterworks Board of Directors; Paul A. Walker, Waterworks Board of Directors member; and Mark McLaughlin, Deputy Executive Operator of the Water Utility.

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PORT AUTHORITY  
CITY OF HAMMOND

PORT AUTHORITY  
CITY OF HAMMOND  
FEDERAL FINDING

***FINDING 2017-001***

Subject: Financial Transactions and Reporting  
Audit Findings: Material Weakness, Noncompliance

*Repeat Finding*

This is a repeat finding from the immediately prior audit. The prior audit finding numbers were 2016-001 and 2016-002.

*Condition*

There were several deficiencies in the internal control system of the City related to financial transactions and reporting. The internal controls implemented by the City related to cash and investments, receipts, disbursements, and financial reporting, including the financial statement and the Schedule of Expenditures of Federal Awards (SEFA), were not effective. Furthermore, the internal controls were not monitored and evaluated for effectiveness.

*Cash and Investments (Bank Reconciliations) - City*

The control over cash and investments and trust bank reconciliations was not effective and did not ensure that bank reconciliations were prepared and reviewed in a timely manner, or that reconciling items were corrected in a timely manner.

Reconciliations of the record balances to the depository balances were not prepared and reviewed in a timely manner. Trust account reconciliations were also not completed in a timely manner. January through October trust account reconciliations were not completed until November of 2017.

As of December 31, 2017, the City had accumulated reconciling adjustments to the payroll account, which had not been corrected. A \$16,065,281 transfer due from the payroll bank account to the general bank account had been carried since December 31, 2014. Additional reconciling items in the payroll account included accumulated balances, receipts, and disbursements of payroll and payroll withholding amounts totaling \$19,695,009. The net effect of these reconciling items was a decrease in the balance of the payroll bank account of \$3,629,728. The City refunded the 2012 Potash Bond in 2017. A fund was not created for the new 2017 Potash Refunding Bond in the financials. The trust account for the bond had an ending cash and investment balance of \$7,107,175, as of December 31, 2017.

*Receipts, Disbursements, and Financial Reporting - City and Port Authority*

The City and Port Authority implemented internal controls over receipts, disbursements, and financial reporting; however, the controls were not effective and did not ensure that transactions were properly recorded in the ledgers and reported in the financial statement.

The City and Port Authority opened new bank accounts during 2017 and recorded bank-to-bank transfers of \$35,335,252 and \$18,600,000 as receipts and disbursements, respectively. The receipts and disbursements reported in the financial statement were overstated by the amount of the bank-to-bank transfers.

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(Continued)

The City advance refunded the 2012 Potash Bond in 2017. The bond proceeds were placed in trust to retire the 2012 bonds as they become due. A fund was not created for the 2017 Potash Refunding Bond Trust in either the ledger or the financial statement. The cash and investment balance and receipts were understated in the financial statement by \$7,107,175.

*Disbursements - Sanitary District*

The Accounts Payable Clerk prepared the checks and recorded the invoices to the accounting system without oversight or review.

The Payroll Manager was responsible for the entire payroll process and was able to make payroll rate changes in the computer system. The Sanitary District Manager implemented a procedure to select up to 15 employees each pay period whose payroll records were audited by an accountant. That audit did not include a verification of the pay distribution to the proper funds and accounts.

*Financial Reporting - Water Utility*

The Office Manager prepared and reported the cash and investment balances, receipts, and disbursements in the Indiana Gateway for Government Units financial reporting system, which was the source for the City's financial statement, without any prior review or oversight. The reports were submitted to the Water Board for review; however, the Water Board approved the reports after the information had been submitted.

*Schedule of Expenditures of Federal Awards (SEFA)*

The City did not have a proper system of internal controls in place to prevent, or detect and correct, errors on the SEFA. Due to the lack of controls, the SEFA presented for audit included the following errors:

1. Insurance in effect during the year of \$2,000,000 was reported for the Beach Monitoring and Notification Program Implementation Grants. No supporting documentation for the entry was provided.
2. The state Maternal and Child Health Services Block Grant to the States expenditures of \$1,605 were reported in error.
3. The Urban and Community Forestry Program expenditures of \$30,000 were omitted.
4. The Crime Victim Compensation Grant expenditures of \$1,271 were omitted.
5. The State Clean Diesel Grant Program expenditures of \$55,000 were omitted.

Audit adjustments were proposed, accepted by the City, and made to the SEFA presented in this report.

*Context*

The lack of controls and the noncompliance were systemic issues throughout the audit period.

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(Continued)

*Criteria*

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. . . ."

"Evaluations are used to determine whether each of the five components of internal control is present and functioning. These evaluations may be conducted on an ongoing or periodic basis. The criteria used are developed by the oversight body, elected officials, management, governing boards, or recognized standard-setting bodies or regulators. . . .

A baseline of the current state of the internal control system is compared against the original design of the internal control system. The baseline consists of issues and deficiencies identified in the internal control system. The results of the monitoring process are evaluated and documented. . . .

Management remediates identified issues. . . ."

Indiana Code 5-13-6-1(e) states: "All local investment officers shall reconcile at least monthly the balance of public funds, as disclosed by the records of the local officers, with the balance statements provided by the respective depositories."

All financial transactions pertaining to the unit must be recorded in the records of the unit at the time of the transaction. (Accounting and Uniform Compliance Guidelines Manual for Cities and Towns, Chapter 1)

All documents and entries to records must be made in a timely manner to ensure that accurate financial information is available to allow the unit to make informed management decisions and to help ensure compliance with IC 5-15-1-1. (Accounting and Uniform Compliance Guidelines Manual for Cities and Towns, Chapter 1)

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. . . ."

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FEDERAL FINDING  
(Continued)

2 CFR 200.510(a) states:

*"Financial statements.* The auditee must prepare financial statements that reflect its financial position, results of operations or changes in net assets, and, where appropriate, cash flows for the fiscal year audited. The financial statements must be for the same organizational unit and fiscal year that is chosen to meet the requirements of this part. However, non-Federal entity-wide financial statements may also include departments, agencies, and other organizational units that have separate audits in accordance with § 200.514 Scope of audit, paragraph (a) and prepare separate 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 that 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."

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(Continued)

*Cause*

Management of the City had not established a proper and effective system of internal control. Management had not conducted a risk assessment related to the City's financial reporting and transactions.

*Effect*

The failure to establish controls enabled misstatements and irregularities to occur on the financial statement and the SEFA. The failure to monitor the internal control system placed the City at risk that controls were either not designed properly or not operating effectively to provide reasonable assurance that controls would have prevented, or detected and corrected, material misstatements in a timely manner.

*Recommendation*

We recommended that the City's management design and implement a proper system of internal controls, which would segregate key functions and also perform periodic monitoring of its system of internal controls. We also recommended that the City reconcile bank accounts in accordance with state statute, monitor the recording of receipts and disbursements, and ensure the accuracy of the SEFA.

*Views of Responsible Officials*

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



Heather Garay, J.D.  
Controller

October 9, 2018

## CORRECTIVE ACTION PLAN

### **Section II – Financial Statement Findings**

#### Finding 2017-001 – **FINANCIAL TRANSACTIONS AND REPORTING**

Contact Person Responsible for Corrective Action: Heather Garay, City Controller

Contact Phone Number: 219-853-6324

#### Corrective Action Plan:

##### Cash and Investments (Bank Reconciliations) – City

- a. We partially concur with the finding.

The City reconciles all bank accounts on a monthly basis. The bank reconciliations are then reviewed by the City Controller. The outstanding amount in the payroll account has carried from 2014 and is related to a bank to bank transfer for the payroll sweeping account. The City will work with a consultant and the financial software provider to attempt to resolve the outstanding payroll transfers from 2014. All other bank accounts are balanced monthly. The City began preparing bank reconciliations for all trust accounts in 2017. The trust activity was reconciled for the entire year for 2017 and are now reconciled and reviewed monthly.

Anticipated Completion Date: December 2018

##### Receipts, Disbursements, and Financial Reporting - City and Port Authority

- b. We concur with the finding.

The City and Port Authority operate on the same financial software. The reports generated by the financial software are unable to distinguish between expenditure and non-expenditure transactions related to bank to bank transfers. 2017 had a significant number of these transactions related to transferring funds to new bank accounts to earn better interest rates and as required by bond agreements. The City and Port Authority will work with their software provider to exclude non-expenditure transfers from reports used for the preparation of the annual financial report.

The City has implemented new controls for the administration of trust accounts which include instructions to set-up the funds and accounts timely, the reconciliation of trust accounts and reporting of activity.

Anticipated Completion Date: March 2019

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Hammond, Indiana 46320

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**Heather Garay, J.D.**  
Controller

Disbursements - Sanitary District  
c. We concur with the finding.

Due to the timing of the 2016 audit, this finding was not resolved in 2017 but has been resolved in 2018.

Completion Date: 2018

Financial Reporting – Water Utility  
d. We partially concur with the finding.

The Water Utility established a corrective action plan in February 2018 to address the 2016 audit finding. It stated that financials would be reviewed and approved by the Water Utility COO and Board of Directors prior to submitting them to the controller for inclusion in the annual financial report. The anticipated completion date was December 2018. The Water Utility began sending these reports to the board and COO for approval in February 2018. The financials were submitted to the Controller prior to the next board meeting and were then approved by the board a few days later. No adjustments were required following the boards review and the financial report was submitted with the original entries. Going forward, the board will review and approve the financials prior to submission the Controller.

Anticipated Completion Date: March 2019

Schedule of Expenditures of Federal Awards (SEFA)  
e. We concur with the finding.

The Controller will work with other departments to develop a procedure for the proper reporting and verification of federal awards. All entries will be reviewed by an additional individual prior to the submission of the SEFA.

Anticipated Completion Date: March 2018

\_\_\_\_\_  
(Signature)

\_\_\_\_\_  
Controller  
(Title)

10/9/2018

\_\_\_\_\_  
(Date)

City of Hammond  
Controller's Office  
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PORT AUTHORITY  
CITY OF HAMMOND  
EXIT CONFERENCE

The contents of this report were discussed on October 9, 2018, with Thomas M. McDermott, Jr., Mayor; Heather Garay, City Controller; Robert Markovich, Common Council member; Pete Torres, Common Council member; Anthony Higgs, Common Council member; Scott Rakos, Common Council member; Phil Taillon, Chief of Staff; Milan A. Kruszynski, Director of the Port Authority; and Richard Szany, Port Authority Finance Director.

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FIRE DEPARTMENT  
CITY OF HAMMOND

FIRE DEPARTMENT  
CITY OF HAMMOND  
AUDIT RESULT AND COMMENT

***PAYROLL DEFICIENCY - LEAVE POLICIES***

A similar comment also appeared in 12 prior reports, including the 4 most recent Reports B45294, B47291, B47309, and B49726, entitled *PAYROLL DEFICIENCIES*.

The City abided by negotiated Union agreements for sick and injured leaves and benefits for firefighters. The Union agreement was effective for the period of January 1, 2017 through December 31, 2020. The agreement did not contain the details of the leave and benefits policies. The City amended the Fire Department Rules and Regulations Section 3, item C (Calling off sick policy), which stated the regular biweekly salary and all insurance benefits would be paid while on sick leave. However, it did not address the number of days or hours of sick leave the police officers were entitled to. We could not determine what the policies entailed; therefore, we could not determine if the City complied with the approved policies.

Each unit must adopt a written policy regarding the accrual and use of leave time and compensatory time and the payment of overtime. Negotiated labor contracts approved by the governing body would be considered as written policy. The policy must conform to the requirements of all state and federal regulatory agencies. (Accounting and Uniform Compliance Guidelines Manual for Cities and Towns, Chapter 1)

FIRE DEPARTMENT  
CITY OF HAMMOND  
EXIT CONFERENCE

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POLICE DEPARTMENT  
CITY OF HAMMOND

POLICE DEPARTMENT  
CITY OF HAMMOND  
AUDIT RESULT AND COMMENT

***PAYROLL DEFICIENCY - LEAVE POLICIES***

A similar comment also appeared in 11 prior reports, including the 4 most recent Reports B45294, B47291, B47309, and B49726, entitled *PAYROLL DEFICIENCIES*.

The City abided by negotiated Union agreements for sick and injured leaves and benefits for police officers. The Union agreement was effective for the period of January 1, 2017 through December 31, 2020. The agreement did not contain the details of the leave and benefits policies. The City amended the Police Department General Order #02-01 and approved General Order #18-02, which stated the regular biweekly salary and all insurance benefits would be paid while on sick leave. However, it did not address the number of days or hours of sick leave the police officers were entitled to. We could not determine what the policies entailed; therefore, we could not determine if the City complied with the approved policies.

Each unit must adopt a written policy regarding the accrual and use of leave time and compensatory time and the payment of overtime. Negotiated labor contracts approved by the governing body would be considered as written policy. The policy must conform to the requirements of all state and federal regulatory agencies. (Accounting and Uniform Compliance Guidelines Manual for Cities and Towns, Chapter 1)

POLICE DEPARTMENT  
CITY OF HAMMOND  
EXIT CONFERENCE

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