

# **CITY OF MADISON**

Madison, Wisconsin

COMMUNICATION TO THOSE CHARGED  
WITH GOVERNANCE AND MANAGEMENT

As of and for the Year Ended December 31, 2015

# CITY OF MADISON

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**REQUIRED COMMUNICATION OF INTERNAL CONTROL RELATED MATTERS  
IDENTIFIED IN THE AUDIT TO THOSE CHARGED WITH GOVERNANCE**

To the Honorable Mayor, Common Council, and Management  
City of Madison  
Madison, Wisconsin

In planning and performing our audit of the financial statements of the City of Madison as of and for the year ended December 31, 2015, in accordance with auditing standards generally accepted in the United States of America, we considered its internal control over financial reporting (internal control) as a basis for designing our auditing procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of its internal control. Accordingly, we do not express an opinion on the effectiveness of its internal control.

A separate Report on Internal Control was issued to the Water Utility Board, Transit and Parking Commission, and Community Development Authority. The information contained in those reports is not included with this report.

Our consideration of internal control was for the limited purpose described in the first paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and, therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as discussed below, we identified certain deficiencies in internal control that we consider to be material weaknesses and a deficiency that we consider to be a significant deficiency.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the following deficiencies in the City's internal control to be material weaknesses:

- > Internal Control Over Financial Reporting
- > Financial Statement Restatement – Correction of Prior Period Error
- > Information Technology Controls – User Access

A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the following deficiency in the City's internal control to be a significant deficiency.

- > Information Technology Control Environment

The City's written response to the material weaknesses and significant deficiency identified in our audit has not been subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

This communication is intended solely for the information and use of management, the city council, and others within the organization and is not intended to be, and should not be, used by anyone other than these specified parties.

*Baker Tilly Virchow Krause, LLP*

Madison, Wisconsin  
July 15, 2016

Auditing standards require that we perform procedures to obtain an understanding of your government and its internal control environment as part of the annual audit. This includes an analysis of significant transaction cycles and an analysis of the year-end financial reporting process and preparation of your financial statements.

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## **INTERNAL CONTROL OVER FINANCIAL REPORTING**

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Properly designed systems of internal control provides your organization with the ability to process and record monthly and year end transactions and prepare annual financial reports.

Our audit includes a review and evaluation of the City's internal controls relating to financial reporting. Common attributes of a properly designed system of internal control for financial reporting are as follows:

- > There is adequate staffing to prepare financial reports throughout and at the end of the year.
- > Material misstatements are identified and corrected during the normal course of duties.
- > Complete and accurate financial statements including footnotes are prepared.
- > Complete and accurate schedules of expenditures of federal and state awards are prepared.
- > Financial reports are independently reviewed for completeness and accuracy.

Our evaluation of the City's internal controls relating to financial reporting has identified control deficiencies that are considered material weaknesses surrounding the preparation of complete and accurate financial statements and footnotes, adjusting journal entries identified by the auditors, and an independent review of financial reports.

As a result of these deficiencies, management has not prepared financial statements that are in conformity with generally accepted accounting principles. In addition, material misstatements in the water utility general ledger were identified during the financial audit. Management should consider what resources and changes are necessary to address and resolve the control deficiencies identified.

### ***Management Response***

- > City management has knowledgeable staff that is familiar with the requirements of generally accepted accounting principles (GAAP). Finance Department staff prepares fund financial statements, some footnote disclosures, and most conversion entries for reconciliation to the entity-wide financial statements.
- > Additionally, Finance staff accountants review auditor prepared draft reports to compare amounts, footnote disclosures, and other information. Furthermore, various City agency staff utilizes a financial statement checklist provided by our audit firm when reviewing the draft reports to ensure GAAP is being adhered to and that all required disclosures are present.
- > Finance Department staff work closely with our auditors to proactively consult on a variety of financial reporting issues throughout the year to prevent material misstatements to the financial statements.
- > Finance Department management staff did implement fund financial statement reviews in fiscal year 2013 to prevent material misstatements. There have been no material adjustments to the fund financial statements identified during the city-wide audit engagement for 2015.
- > The City did "go-live" with the first ERP system solution on 1/2/2015, and additionally upgraded to a new version release during October of 2015. This took much effort amongst the Finance Department staff to accomplish these software solution upgrades.

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**INTERNAL CONTROL OVER FINANCIAL REPORTING (cont.)**

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***Management Response*** (cont.)

Additionally, Finance Department staff drafted new sets of internal control procedural documents for auditor review in January and February of 2016 given new ERP system processes.

- > It is Finance Department management's goal to embark upon a detailed mapping project within the ERP software (GASB-34 Report Writer module), or within Microsoft Excel, in an attempt to begin preparing entity-wide financial statements for the 2017/2018 fiscal years.
- > Currently, Finance Department management staff is working to hire a professional Grants Manager/Internal Auditor to lead and facilitate the preparation of complete and accurate schedules of expenditures of federal and state awards.

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**FINANCIAL STATEMENT RESTATEMENT – CORRECTION OF PRIOR PERIOD ERROR**

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The City's internal controls over financial reporting should be designed to prepare financial statements in accordance with United States Generally Accepted Accounting Principles (GAAP). Subsequent discovery of material financial reporting errors related to the water utility and the required correction of previously issued financial statements indicate that a control did not function properly, and therefore, there is a material weakness in the City's financial reporting system.

As described in Note IV.I. of the City's 2015 financial statements, a restatement of the prior year financial statements was necessary to properly report expense activity for 2014 and 2013 for the water utility. The proper internal controls were not in place at the water utility to ensure that all activity was being properly reflected in the financial statements. A summary of the effects on the statements is included in Note IV.I.

***Management Response***

- > The Water Utility implemented additional internal controls beginning in 2015 which includes new transactional procedures, and increased financial work order reviews to ensure that expenses are recorded in the year they are incurred. In conjunction with implementing stronger internal controls, staff worked diligently to close out all appropriate work orders during the year. Approximately 406 work orders with a value of about \$50.4 million (90 work orders with a value of roughly \$6.7 million for 2014) were closed, placed into service, depreciated and/or expensed by year end, resulting in a net position restatement at December 31, 2014 totaling just over \$1.4 million.

Water Utility management will continue to oversee the newly implemented internal controls to ensure all activity is properly reflected within its financial statements.

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## **INFORMATION TECHNOLOGY CONTROLS – USER ACCESS**

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A properly designed system of internal control includes establishing proper information technology controls. This includes systems that are designed to limit the access or control of any one individual to your government's assets or accounting records, and to achieve a higher likelihood that errors or irregularities in your accounting processes would be discovered by your staff in a timely manner.

At this time, the proper information technology controls regarding user access are not in place. As a result, errors, irregularities or fraud could occur as part of the financial process that may not be discovered by someone in your organization. Therefore, we are reporting a material weakness related to information technology controls over user access.

### ***INFORMATION TECHNOLOGY CONTROLS – USER ACCESS***

Within the City's financial reporting system (MUNIS), certain users in the finance department have been granted administrator permissions that give them the ability to delete audit logs within MUNIS. In any system some user(s) must have administrator permissions. Industry best practices would be to separate this function from the finance department. Audit logs provide a detective control to identify problems or irregularities in the system. If administrators have the ability to delete these logs, it may make it difficult to detect system problems or irregularities. The City should change its user access so no user has the ability to alter or delete the system logs within MUNIS.

#### ***Management Response***

- > Within the MUNIS software, changes to data tables create an audit history indicating the field level change made and the user who performed the action. These audit records are secured from database removal by the establishment of system security permissions. The permissions are separated by functional areas, such as General Ledger, Accounts Payable, Purchasing, and Account Receivable. The exception to the audit table functional area is Payroll and Human Resources. Payroll and Human Resources audit records cannot be deleted from the system regardless of permissions.
- > There is a secondary audit level placed on the updating of the system security permissions themselves. These updates are also written to audit history, indicating any changes made to an individual's system security permissions.
- > The Finance Department has set system security permissions so that audit table purging cannot be performed by any individual who has direct supervisor responsibility within a functional area. Furthermore, there are two individuals within the City that have permissions granted for audit maintenance at both a functional and system security level.

We recommend that a designated employee review the controls over user access, the related risks, and potential controls to determine whether additional controls should be implemented. This determination should take into consideration a cost / benefit analysis.

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## **INFORMATION TECHNOLOGY CONTROL ENVIRONMENT**

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As part of the audit, we reviewed the Information Technology (IT) control environment of the City based on AICPA guidelines. The IT areas reviewed included change management, user access to the network and the financial applications, user access provision and deactivation process, password settings, privileged access, access violation monitoring, data center security, data backup monitoring, and scheduled job processing.

**INFORMATION TECHNOLOGY CONTROL ENVIRONMENT (cont.)**

**OBSERVATIONS AND RECOMMENDATIONS**

The following is a table detailing our observations from the assessment and our recommendations.

IT Area	IT Finding	Recommendation to Address Finding
<i>Unique User Authentication</i>	<i>BT reviewed the MUNIS user list and the network user list and found some generic accounts such as MUNIS and ROOT. Some of these generic accounts are shared.</i>	<i>All users of financial applications and the network should have a login and password which is unique for each user. Account names and passwords should not be shared by anyone. Generic, shared, temporary and system accounts should be removed/disabled.</i>
<i>Elevated Privileges</i>	<i>Changes of the PLGEO, TRTAX, and CMSPCHG systems are approved and tested. However, the developer of the change is often the person who implements the change in the production environment.</i>	<i>Segregation of duties should be implemented within the change management process.</i>
<i>Change Control - Package Software</i>	<i>Tyler MUNIS - The frequent updates Tyler requires the City to perform on MUNIS make it difficult if not impossible for the City to properly test the updates prior to implementation in the production environment. Tyler can access the application server directly via GoToAssist and can implement updates without the knowledge of the City's IT department. Additionally, development and testing environments are on the production server.</i>	<i>We recommend that the City treat Tyler as a SaaS provider and request and review Tyler's SSAE 16 report to ensure that any control deficiencies in Tyler's IT control environment are mitigated by the City's controls. Additionally, we recommend the City investigate other vendor access management mechanisms.</i>
<i>Passwords</i>	<i>Passwords of RECTRAC and the legacy systems such as PLGEO, TRTAX, and CMSPCHG has weaker settings.</i>	<i>We recommend that the City change the application password settings to be the same as the City's network password settings wherever feasible.</i>
<i>User Access Review</i>	<i>IT generates user access permissions report and sends this report to the security contact of each agency/department. The objective is to have the security contact or the department head review the user list in their area. The documents are kept on SharePoint. However, not all security contacts/department heads review their user lists. To compensate for this control, IT routinely checks for users who have not accessed their account for over 60 days.</i>	<i>We recommend that business area managers or security contacts review their users' access once a year to ensure users don't have access beyond their job responsibilities (least privilege). Documentation of these reviews should be retained.</i>



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## INFORMATION TECHNOLOGY CONTROL ENVIRONMENT (cont.)

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### **OBSERVATIONS AND RECOMMENDATIONS (cont.)**

#### **Management Response**

##### **Recommendation:**

*All users of financial applications and the network should have a login and password which is unique for each user. Account name and password should not be shared by anyone. Generic, shared, temporary and system accounts should be removed/disabled.*

#### **Management Response**

- > Tyler Technologies has informed us the accounts of MUNIS and ROOT cannot be removed or disabled without causing irreparable harm to their software.

##### **Recommendation:**

*Segregation of duties should be implemented within the change management process.*

#### **Management Response**

- > IT staff utilize a change process that includes an electronic form as part of our call and change tracking system. Changes are detailed, routed to affected parties and approved by supervisory staff. Complete segregation of duties is not possible due to a small staff size. However, the change process combined with the supervisory oversight fulfills this need.

##### **Recommendation:**

*We recommend that the City treat Tyler as a SaaS provider and request and review Tyler's SSAE 16 report to ensure that any control deficiencies in Tyler's IT control environment are mitigated by the City's controls. Additionally, we recommend the City investigate other vendor access management mechanisms.*

#### **Management Response**

- > On April 12, 2016 the SSAE 16 report was requested from our ERP vendor, Tyler Technologies. Our City Attorney's Office is reviewing the Non-Disclosure Agreement requested by Tyler.

##### **Recommendation:**

*We recommend that the City change the application password settings to be the same as the City's network password settings wherever feasible.*

#### **Management Response**

- > This refers to the following legacy applications: ASPPROP, CMABS911, CMSPCHG, PLGEO, TRTAX, REDPP. Although these remaining six legacy applications are scheduled for replacement in our Capital Improvements Program, we researched the legacy platform (Progress). Even though these applications are up to twenty years old, we are implementing a programming solution that will provide for passing through active directory. This will be implemented this summer, for all but PLGEO, which is scheduled for decommissioning this fall.

##### **Recommendation:**

*We recommend that business area managers or security contacts review their users' access once a year to ensure users don't have access beyond their job responsibilities (least privilege). Documentation of these reviews should be retained.*

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## **INFORMATION TECHNOLOGY CONTROL ENVIRONMENT (cont.)**

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### ***OBSERVATIONS AND RECOMMENDATIONS (cont.)***

#### ***Management Response***

- > On an annual basis IT has been producing a report on access rights by individual. This is distributed to agency security contacts to review and identify any necessary changes. We have implemented a stronger follow up process with agencies in order to document their reviews.

**OTHER COMMUNICATIONS TO THOSE CHARGED WITH GOVERNANCE**

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## TWO WAY COMMUNICATION REGARDING YOUR AUDIT

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As part of our audit of your financial statements, we are providing communications to you throughout the audit process. Auditing requirements provide for two-way communication and are important in assisting the auditor and you with more information relevant to the audit.

As this past audit is concluded, we use what we have learned to begin the planning process for next year's audit. It is important that you understand the following points about the scope and timing of our next audit:

- a. We address the significant risks of material misstatement, or noncompliance whether due to fraud or error, through our detailed audit procedures.
- b. We will obtain an understanding of the five components of internal control sufficient to assess the risk of material misstatement of the financial statements or material noncompliance related to federal and state awards whether due to error or fraud, and to design the nature, timing, and extent of further audit procedures. We will obtain a sufficient understanding by performing risk assessment procedures to evaluate the design of controls relevant to an audit of financial statements and the federal and state awards and to determine whether they have been implemented. We will use such knowledge to:
  - > Identify types of potential misstatements or noncompliance.
  - > Consider factors that affect the risks of material misstatement or material noncompliance.
  - > Design tests of controls, when applicable, and substantive procedures.

Our audit will be performed in accordance with U.S. generally accepted auditing standards, *Government Auditing Standards*, OMB's *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance), and the *State Single Audit Guidelines*.

We will not express an opinion on the effectiveness of internal control over financial reporting or compliance with laws, regulations, and provisions of contracts or grant programs. For audits done in accordance with the Uniform Guidance, the *State Single Audit Guidelines*, and *Government Auditing Standards*, our report will include a paragraph that states that the purpose of the report is solely to describe (a) the scope of testing of internal control over financial reporting and compliance and the result of that testing and not to provide an opinion on the effectiveness of internal control over financial reporting or on compliance, (b) the scope of testing internal control over compliance for major programs and major program compliance and the result of that testing and to provide an opinion on compliance but not to provide an opinion on the effectiveness of internal control over compliance and, (c) that the report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering internal control over financial reporting and compliance and the Uniform Guidance and the *State Single Audit Guidelines* in considering internal control over compliance and major program compliance. The paragraph will also state that the report is not suitable for any other purpose.

- c. The concept of materiality recognizes that some matters, either individually or in the aggregate, are important for fair presentation of financial statements in conformity with generally accepted accounting principles or for reporting material noncompliance while other matters are not important. In performing the audit, we are concerned with matters that, either individually or in the aggregate, could be material to the financial statements or to the entity's federal and state awards. Our responsibility is to plan and perform the audit to obtain reasonable assurance that material misstatements or material noncompliance, whether caused by errors or fraud, are detected.
- d. Your financial statements contain components, as defined by auditing standards generally accepted in the United States of America, some of which we also audit.

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## **TWO WAY COMMUNICATION REGARDING YOUR AUDIT (cont.)**

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- e. In connection with our audit, we intend to place reliance on the audit of the financial statements of the Olbrich Botanical Society and Olbrich Botanical Society Foundation, a component unit of the City of Madison, as of December 31, 2016 and for the year then ended completed by Smith and Gesteland. In addition, we intend to place reliance on the audit of the financial statements of the Madison Public Library Foundation, a component unit of the City of Madison, as of December 31, 2016 and for the year then ended completed by SVA Certified Public Accountants, S.C. We also intend to place reliance on the audit of the financial statements of the Madison Parks Foundation, a component unit of the City of Madison, as of December 31, 2016, and for the year then ended completed by Johnson Block and Company, Inc. All necessary conditions have been met to allow us to make reference to the component auditors.

We are very interested in your views regarding certain matters. Those matters are listed here:

- a. We typically will communicate with your top level of management unless you tell us otherwise.
- b. We understand that the city council has the responsibility to oversee the strategic direction of your organization, as well as the overall accountability of the entity. Management has the responsibility for achieving the objectives of the entity.
- c. We need to know your views about your organization's objectives and strategies, and the related business risks that may result in material misstatements.
- d. Which matters do you consider warrant particular attention during the audit, and are there any areas where you request additional procedures to be undertaken?
- e. Have you had any significant communications with regulators or grantor agencies?
- f. Are there other matters that you believe are relevant to the audit of the financial statements or the federal or state awards?

Also, is there anything that we need to know about the attitudes, awareness, and actions of the City concerning:

- a. The City's internal control and its importance in the entity, including how those charged with governance oversee the effectiveness of internal control?
- b. The detection or the possibility of fraud?

We also need to know if you have taken actions in response to developments in financial reporting, laws, accounting standards, governance practices, or other related matters, or in response to previous communications with us.

With regard to the timing of our audit, here is some general information. We will perform preliminary audit work during the months of October-December, and sometimes early January. Our final fieldwork is scheduled during the spring to best coincide with your readiness and report deadlines. After fieldwork, we wrap up our audit procedures at our office and may issue drafts of our report for your review. Final copies of our report and other communications are issued after approval by your staff. This is typically 6-12 weeks after final fieldwork, but may vary depending on a number of factors.

Keep in mind that while this communication may assist us with planning the scope and timing of the audit, it does not change the auditor's sole responsibility to determine the overall audit strategy and the audit plan, including the nature, timing, and extent of procedures necessary to obtain sufficient appropriate audit evidence.

We realize that you may have questions on what this all means, or wish to provide other feedback. We welcome the opportunity to hear from you.

**COMMUNICATION OF OTHER CONTROL DEFICIENCIES, RECOMMENDATIONS AND  
INFORMATIONAL POINTS TO MANAGEMENT THAT ARE NOT MATERIAL  
WEAKNESSES OR SIGNIFICANT DEFICIENCIES**

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## **PRIOR YEAR'S POINTS**

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### ***ENTITY-WIDE CONTROLS***

A formal fraud risk evaluation process should be in place. This is a control process that should exist and be performed by either a newly created audit committee or the Board of Estimates.

#### ***Status (12/31/15)***

This recommendation still pertains.

### ***INTERNAL CONTROL ENVIRONMENT***

A portion of the internal control environment is oversight by the governing body. For the City of Madison, the Board of Estimates (BOE) is charged with the responsibility for financial oversight. During 2012, the BOE received a financial status update during the budgeting process. We recommend that budget versus actual information be made available on a regular basis to allow for regular review by those charged with governance. There are many different levels and types of oversight and review possible. City management and the BOE should determine what level of information should be made available, what level of review is appropriate, and how often the reviews should occur.

In addition, financial budgets have not been formally adopted for all governmental funds. Adopting a budget for all funds and making the budget versus actual information available to the BOE will assist them in their governance responsibilities.

#### ***Status (12/31/15)***

During 2015, BOE was provided financial information on a periodic basis. The mayor also met with the finance director and with the department heads as part of the budget process. We recommend the City continue to evaluate the appropriate level of review and involvement of the BOE. However, as noted in the financial statements, there are numerous governmental funds for which financial budgets were not formally adopted. We recommend that individual budgets be formally adopted for all funds.

### ***INTERNAL CONTROLS OVER FINANCIAL REPORTING***

Adjusting journal entries and supporting documentation for transit utility journal entries should be reviewed and approved by an appropriate person who is not the original preparer.

#### ***Status (12/31/15)***

This point has been resolved.

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## **INFORMATIONAL POINTS**

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### ***CYBER RISK ASSESSMENT***

Cybersecurity is a growing challenge for many governments as threats and vulnerabilities constantly evolve. Information security is a significant issue for many organizations and is no longer considered to be strictly an Information Technology (IT) issue. The potential impacts of a security breach can be financial, operational, and reputational. Cyber risk should be a high priority and evaluated on a regular basis.

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## **INFORMATIONAL POINTS (cont.)**

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### ***CYBER RISK ASSESSMENT (cont.)***

Security breaches can come in a number of forms, which are continually evolving with advances in and increased use of technology. It is important for governments to assess what types of information they have that are vulnerable to cyber-attack. Items to consider include processing, collecting, and/or storing personal information about employees, taxpayers, and/or customers. Social security numbers, bank accounts, addresses, medical information, birth dates, and credit cards are all common examples of information existing in systems of governmental entities. In addition, general ledger data and other supporting files can be compromised. Several instances of ransomware have been reported in governmental entities like yours during the last year. Ransomware restricts access to your files and demands a ransom to the malware operator in order to release the restriction. It is important to take inventory of all the information that flows through your systems in order to properly secure your data.

We recommend performing a cyber risk assessment to align the internal controls and processes with the organizational objectives, initiatives, resources, and risk appetites with regards to cyber risk. We have cybersecurity experts on staff that are available to assist with this assessment.

#### ***Management Response***

- > On an annual basis we have been engaging third-party vendors to conduct cyber security assessments and will continue to do so.

### ***HIPAA RISK ASSESSMENT***

With data breaches on the rise, the US Department of Health and Human Services (HHS) Office of Civil Rights (OCR) has ramped up auditing and enforcement of Health Insurance Portability and Accountability Act (HIPAA) compliance in recent years. What they have found is that many organizations are not doing enough to protect Electronic Protected Health Information (ePHI).

One of the most common findings identified by HHS OCR is the lack of a thorough and documented risk assessment. The HIPAA Security Rule requires that organizations in accordance with the Code of Federal Regulations 45 §164.308(a)(1)(ii)(A) "Conduct an accurate and thorough assessment of the potential risks and vulnerabilities to the confidentiality, integrity, and availability of electronic protected health information ...". HHS OCR has indicated this risk assessment should be documented and performed at least annually.

Breach notification to HHS OCR is required when ePHI is exposed. When HHS OCR investigates such breaches, the documentation for the organization's latest risk assessment is often one of the first requests by HHS OCR for their review.

We recommend you perform and document the required HIPAA risk assessment. We are available to assist you with this process.

#### ***Management Response***

- > This effort is led by our City Attorney's Office and the City Risk Manager. As of 2016, respective agencies are gathering data in order to provide a formal HIPAA risk assessment



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**INFORMATIONAL POINTS (cont.)**

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***GOVERNMENT FRAUD PREVENTION AND DETECTION: NOW IS THE TIME TO ACT***

When it comes to preventing and detecting fraud in government, being proactive is critical. In fact, government is the second most likely industry to be impacted by fraud. According to the audit standards, the primary responsibility for the prevention and detection of fraud rests with both those charged with governance of the entity and management. To get started, your government should conduct a fraud risk assessment to identify where and how fraud might occur and what individuals may be in a position to commit fraud. Once you've identified your entity's fraud risk areas, the next step is to develop a fraud risk assessment and investigation policy.

As you begin your fraud risk assessment or develop tools to prevent and detect fraud, it is important to keep in mind the following information provided by the Association of Certified fraud Examiners:

- > Misappropriation of assets accounts for 80 percent of fraud
- > The primary internal control weaknesses observed are lack of internal controls, lack of management review, override of existing internal controls and poor tone at the top
- > A tip is the most effective tool to catch a fraudster followed by management review
- > The professional requirements and objectives of a financial audit are different than a forensic audit. Due to the nature of a financial audit, less than 10 percent of frauds have been discovered as a result of a financial audit conducted by an independent accounting firm.

If your government has not gone through a fraud risk assessment or does not have a plan to prevent and detect fraud, we recommend that this be done and then updated on a regular basis. We are available to assist you with this process.

***GASB UPDATES***

The following is a schedule of GASB projects:

<b>Task or Event</b>	<b>Effective Date</b>	<b>Impact</b>
GASB 72 – Fair Value Measurement and Application	For financial statements for periods beginning after June 15, 2015	Items that are now subject to fair value measurement that weren't before: private equity/hedge funds, real estate investments, many investments that were previously carried at cost or under the equity method, derivatives will now be measured using exit price, donated long term assets. Does not affect money markets, investments in 2a7-like pools, or assets held by the government that enhance the ability to provide services.
GASB 73 – Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB 68, and Amendments to Certain Provisions of GASB Statements 67 and 68	For fiscal years beginning after June 15, 2016 for pensions that are not within the scope of GASB 68. For fiscal years beginning after June 15, 2015 for pensions within the scope of GASB 67 and 68.	Part I extends the approach of GASB 68 to all pensions (with some modifications). Part II clarifies certain requirements of GASB 67 and 68.

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**INFORMATIONAL POINTS (cont.)**


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**GASB UPDATES (cont.)**

<b>Task or Event</b>	<b>Effective Date</b>	<b>Impact</b>
GASB 74 – Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans and GASB 75 – Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions	GASB 74: For fiscal years beginning after June 15, 2016  GASB 75: For fiscal years beginning after June 15, 2017	These standards have similarities to the previous OPEB standards, most notably the definition of an OPEB and the option of the alternative measurement method for small governments. However, the calculation and reporting of the OPEB liability and various required disclosures will change under the new standards, becoming similar to the pension standards.
GASB 76 – The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments	For reporting periods beginning after June 15, 2015	Officially established accounting principles – GASB statements (Category A) and GASB Technical Bulletins, implementation guides and literature of the AICPA cleared by the GASB (Category B)
GASB 77 – Tax Abatement Disclosures	For financial statements for periods beginning after December 15, 2015	Tax abatements are a reduction in tax revenue that has the following characteristics: (1) An agreement between one or more governments and an individual or entity in which: (a) one or more governments promise to forgo tax revenues to which they are otherwise entitled and; (b) the individual or entity promises to take specific action after the agreement has been entered into that contributes to economic development or otherwise benefits the governments or the citizens of those governments.  This definition is limited and excludes many incentive and other programs because they do not meet one or more of the requirements.
GASB 78 – Pensions Provided through Certain Multiple-Employer Defined Benefit Pension Plans	For reporting periods beginning after December 15, 2015	This addresses a specific issue regarding the ability of state and local governmental employers to obtain necessary information related to pensions that are provided through certain multiple-employer benefit pension plans that are not a state or local governmental pension plan.
GASB 79 – Certain External Investment Pools and Pool Participants	For reporting periods beginning after June 15, 2015, except for certain provisions on portfolio quality, custodial credit risk, and shadow pricing, which are effective for reporting periods beginning after December 15, 2015	It establishes criteria for an external investment pool to qualify for making the election to measure all its investments at amortized costs for financial reporting purposes.

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**INFORMATIONAL POINTS (cont.)**


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**GASB UPDATES (cont.)**

<b>Task or Event</b>	<b>Effective Date</b>	<b>Impact</b>
Current Agenda Project: Blending Requirements for Certain Component Units	Proposed effective date – June 30, 2017 (Exposure Draft issued in June 2015)	The objective of this project is to improve financial reporting by addressing issues related to inconsistent presentation of certain component units in financial reporting of governments.
Current Agenda Project: Pension Issues	Proposed effective date – June 30, 2017 (Exposure Draft issued in December 2015)	The object of this project is to consider the need for revisions to certain of the requirements in GASB 67 and 68, as a result of issues raised by stakeholders.
Current Agenda Project: Irrevocable Split-Interest Agreements	Proposed effective date – December 31, 2017 (Exposure Draft issued in June 2015)	The objective of this project is to determine what accounting and financial reporting guidance, if any, should be established for irrevocable split-interest agreements held for the benefit of governmental entities.
Current Agenda Project: Fiduciary Activities	Proposed effective date – December 31, 2018 (Exposure draft issued December 2015)	This project is to develop guidance regarding whether and how governments should report fiduciary activities in their general purpose external financial reports.
Current Agenda Project: Asset Retirement Obligations	Proposed effective date – December 31, 2018 (Exposure Draft issued in December 2015)	The objective of this project is to improve financial reporting by developing requirements on recognition and measurement for asset retirement obligations, other than landfills.
Current Agenda Project: Leases	The GASB Board is scheduled to issue an Exposure Draft in January 2016	The objective of this project is to reexamine issues associated with lease accounting, considering improvements to existing guidance.
Current Agenda Project: Certain Extinguishments Using Existing Resources	The GASB Board is scheduled to issue an Exposure Draft in August 2016	The project will consider improvements to the existing guidance related to debt extinguishments using existing resources. Debt extinguishments connected with troubled debt restructurings and bankruptcy, which are addressed in other pronouncements, are not included.

The GASB has a project on hold (conceptual framework for recognition) pending the reexamination of the financial reporting model.

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## **INFORMATIONAL POINTS (cont.)**

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### ***GASB UPDATES (cont.)***

The GASB revisits GASB standards ten (10) years after issuance. The GASB is currently revisiting GASB Statement No. 34, *Basic Financial Statements – and Management’s Discussion and Analysis for State and Local Governments*, as well as reporting model-related pronouncements including Statements Nos. 37, 41, and No. 46 and Interpretation No. 6, *Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statements*. The GASB has indicated that they are revisiting the following major provisions of these standards: management’s discussion and analysis, government-wide financial statements, fund financial statements, capital asset reporting, budgetary comparisons, special purpose government reporting, and related notes to financial statements. In addition, the GASB is revisiting debt extinguishments, which includes a reexamination of GASB Statement Nos. 7, 23, and 62. We will share updates with you as they become available.

Full lists of projects, as well as many resources, are available on GASB’s website which is located at [www.gasb.org](http://www.gasb.org).

### ***INTERPRETING YOUR FINANCIAL STATEMENTS POST-GASB No. 68***

Now that your financial statements reflect the requirements of GASB Statement No. 68, what has changed and how do you interpret this new information? In summary, GASB Statement No. 68 required governmental entities participating in the Wisconsin Retirement System (WRS) to report their proportionate share of the net pension asset of WRS as of a specific date along with their proportionate share of pension expenses incurred by the WRS for the period ending on that date. That date is referred to as the “Measurement Date”. For WRS, this date was December 31, 2014 and annually thereafter.

As of December 31, 2014, WRS reported total resources available to provide pension benefits of \$92.1 billion. They also reported a total liability for pensions of \$89.7 billion. This resulted in a net pension asset of \$2.4 billion. This is the amount from which your proportionate share that is reported on your Statement of Net Position as a net pension asset is determined. The City and CDA reported a net pension asset of \$30,529,475 and \$392,124, respectively. This asset is not convertible into cash or available to spend on other activities but rather will become part of your pension expense in future years on the Statement of Activities as it changes from one year to the next based on the activity of WRS. As such it is reported as a restricted long-term or non-current asset and is also reflected as restricted net position because it represents funds held in trust by the WRS that can only be used for the payment of pension benefits.

Additionally, there are other amounts classified as deferred outflows or inflows of resources related to the WRS that are now reported on your Statement of Net Position. These amounts reflect the differences in expected or projected results used by the actuary to determine the total pension liability versus the actual results obtained. The most prominent and volatile of these amounts is the difference between the projected earnings of the investments to the actual earnings of the investments. Depending upon market conditions, actual earnings on investments, which include changes in the market value of those investments, can change significantly from one year to the next. In order to smooth out the effects of these differences, these amounts reported as deferred outflows or inflows of resources are amortized to pension expense over a period of time (approximately 5 years).

One additional item reported as a deferred outflow of resources is required by this new standard. Any pension contributions (employer amounts and employee amounts paid by the employer) attributable to periods after the Measurement Date (December 31, 2014) are to be removed from the current year’s pension expense and applied to the following year’s pension expense on the Statement of Activities.

Amounts reported as deferred outflows of resources increases your reported total net position. These amounts increase the reported unrestricted net position.

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## **INFORMATIONAL POINTS (cont.)**

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### ***INTERPRETING YOUR FINANCIAL STATEMENTS POST-GASB No. 68 (cont.)***

It should be noted that all of these changes affect your government-wide financial statements and any proprietary fund financial statement you have that have pensionable wages but **do not** affect your governmental fund financials statements. Nor does the implementation of this new standard affect how you fund or pay for your pension contributions to the WRS. The process of funding and paying these pension benefits remains unchanged.

The accounting and reporting of pensions has become more complex with the implementation of GASB Statement No. 68. Please contact your Baker Tilly professional to discuss or clarify how this new accounting standard affects your financial statement.

### ***OTHER POST EMPLOYMENT BENEFIT (OPEB) REPORTING CHANGES ON THE HORIZON***

GASB Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, addresses reporting by OPEB plans that administer benefits on behalf of governments. GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, addresses reporting by governments that provide OPEB to their employees and for governments that finance OPEB for employees of other governments. The new OPEB standards parallel the pension standards GASB Nos. 67 and 68. Together, the pension and OPEB standards provide consistent and comprehensive guidance for all postemployment benefits.

OPEB plans will implement the new standards beginning with the year end December 31, 2017. Governments that provide OPEB benefits to their employees will need to implement these standards beginning with the year end December 31, 2018.

This standard has similarities to the previous OPEB standards, most notably the definition of an OPEB and the option of the alternative measurement method for small governments. However, the calculation and reporting of the OPEB liability and various required disclosures will change under the new standards, becoming similar to the pension standards.

To implement this standard, your government will need to plan ahead for obtaining a new actuarial study. The selection of a measurement date and timing for the study will be important to consider well in advance of implementation. We are available to further discuss this standard, the timing, and impact on your government.

### ***TAX INCREMENT FINANCING LAW CHANGES***

In 2014, the Wisconsin Legislature appointed the Legislative Council Study Committee on the Review of Tax Increment Financing to study and review Wisconsin's Tax Incremental Financing (TIF) laws and to make recommendations for modifications and improvements. The Committee recommended eight bills, four of which were adopted by the Legislature and signed by the Governor in March 2016. Following is a summary of the new laws:

- > 2015 Wisconsin Act 254 permits a Tax Incremental District (TID) project plan to be amended, or its maximum lifespan to be extended by an additional three years, or both, if at any time during the life of the TID, the annual and total amount of tax increments to be generated are adversely impacted by Wisconsin Act 145. Act 145 increased state aid to technical college districts in order to reduce the total statewide levy of technical college districts.
- > 2015 Wisconsin Act 255 removes the restriction that vacant property may not comprise more than 25 percent of the area of a newly created TID and excludes all tax-exempt city-owned property from the calculation of a TID's initial tax incremental base value.

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## **INFORMATIONAL POINTS (cont.)**

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### ***TAX INCREMENT FINANCING LAW CHANGES (cont.)***

- > 2015 Wisconsin Act 256 makes several technical changes to the TIF law, deleting certain obsolete provisions and clarifying/modifying others, such as maintenance of industrial zoning, public hearing notice for TID amendments and Joint Review Board review period. It also specifies that the municipality's equalized value for the preceding year, as used in the calculation of the levy limit exception for the year that a TID terminates, excludes the value of any TID value increments (TID OUT Value).
- > 2015 Wisconsin Act 257 makes several changes to improve reporting and transparency regarding the performance of TIF districts, including requiring a community to submit an annual report by July 1 describing the status of each existing TID to each overlying taxing jurisdiction as well as to the Wisconsin Department of Revenue (DOR). There will be a \$100 per day fine imposed for reports that are past due. In addition, the joint review board must meet annually to review the annual report and status of each TID. Baker Tilly will be working with the DOR in upcoming months to fully understand the impact of the reporting changes. We anticipate that there will be additional information your government will need to provide as part of this new reporting process. We will communicate additional information as it is known.

Acts 254, 255, 256 and certain sections of Act 257 are effective immediately and apply to all TIDs that are created or amended after October 1, 2015. The effective date for the annual reporting requirements stated in Act 257 is October 1, 2016. Accordingly, this new reporting requirement will be effective for your 2016 annual report due by July 1, 2017. More information related to these new laws is available on the DOR and Wisconsin State Statute's websites.

### ***DEPARTMENTAL CONTROLS***

As part of our annual audit process, we focus our efforts on the primary accounting systems, internal controls, and procedures used by the City. This is in keeping with our goal to provide an audit opinion which states that the financial statements of the City are correct in all material respects.

In some cases, the primary system of accounting procedures and controls of the City are supported by smaller systems which are decentralized, and reside within a department or location. In many cases, those systems are as simple as handling cash collections and remitting those collections to the city treasurer. (For example, this would be the case in a typical municipal swimming pool.) In other cases, the department may send invoices or statements of amounts due, and track collections of those amounts in a standalone accounts receivable system. (For example, this would be the case in a typical municipal court.)

Generally, the more centralized a function is, the easier it is to design and implement accounting controls that provide some level of checks and balances. That is because you are able to divide certain tasks over the people available to achieve a higher degree of segregation of duties. For those tasks that are decentralized, it is usually very difficult to provide for proper segregation of duties. Therefore, with one person being involved in most or all aspects of a transaction, you lose the ability to rely on the controls to achieve the safeguarding of assets and reliability of financial records.

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**INFORMATIONAL POINTS** (cont.)

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***DEPARTMENTAL CONTROLS*** (cont.)

As auditors, we are required to communicate with you on a variety of topics. Since there is now more emphasis on internal controls and management's responsibilities, we believe it is appropriate to make sure that you are informed about the lack of segregation of duties that may occur at departments or locations that handle cash or do miscellaneous billing. Examples in the City that fit this situation may include the following:

Attorney	Parking Utility
Engineering	Parks
Fire Department	Planning, Community, and Economic Development
Fleet Services	Senior Center
Library	Streets Division
Madison Metro Transit	Swimming pool
Monona Terrace	Traffic Engineering
Municipal Court	

As you might expect, similar situations are common in most governments.

As auditors, we are required to focus on the financial statements at a highly summarized level and our audit procedures support our opinion on those financial statements. Departments or locations that handle relatively smaller amounts of money are not the primary focus of our audit. Yet, because of the lack of segregation of duties, the opportunity for loss is higher there than in centralized functions that have more controls.

Because management is responsible for designing and implementing controls and procedures to detect and prevent fraud, we believe that is important for us to communicate this information to you. We have no knowledge of any fraud that has occurred or is suspected to have occurred within the departments mentioned above. However, your role as the governing body is to assess your risk areas and determine that the appropriate level of controls and procedures are in place. As always, the costs of controls and staffing must be weighed against the perceived benefits of safeguarding your assets.

Without adding staff or splitting up the duties, your own day-to-day contact and knowledge of the operation are also important mitigating factors.

**REQUIRED COMMUNICATIONS BY THE AUDITOR TO THOSE CHARGED WITH GOVERNANCE**



To the Honorable Mayor, Common Council, and Management  
City of Madison  
Madison, Wisconsin

Thank you for using Baker Tilly Virchow Krause, LLP as your auditor.

We have completed our audit of the financial statements of the City of Madison for the year ended December 31, 2015 and have issued our report thereon dated July 15, 2016. This letter presents communications required by our professional standards.

***OUR RESPONSIBILITY UNDER AUDITING STANDARDS GENERALLY ACCEPTED IN THE UNITED STATES OF AMERICA, GOVERNMENT AUDITING STANDARDS, THE UNIFORM GUIDANCE, AND THE STATE SINGLE AUDIT GUIDELINES***

The objective of a financial statement audit is the expression of an opinion on the financial statements. We conducted the audit in accordance with auditing standards generally accepted in the United States of America, *Government Auditing Standards*, OMB's *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance), and the *State Single Audit Guidelines*. These standards require that we plan and perform our audit to obtain reasonable, rather than absolute, assurance about whether the financial statements prepared by management with your oversight are free of material misstatement, whether caused by error or fraud. Our audit included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit does not relieve management or the city council of their responsibilities.

We considered the City of Madison's internal control over financial reporting to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City of Madison's internal control over financial reporting. We also considered internal control over compliance with types of requirements that could have a direct and material effect on a major federal and major state program to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for a major federal and state program and to test and report on internal control over compliance in accordance with the Uniform Guidance and the *State Single Audit Guidelines*, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance.

As part of obtaining reasonable assurance about whether the City of Madison's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit. Also, in accordance with the Uniform Guidance and the *State Single Audit Guidelines*, we examined, on a test basis, evidence about the City of Madison's compliance with the types of compliance requirements described in the *OMB Compliance Supplement* and the *State Single Audit Guidelines* that could have a direct and material effect on each of its major federal and state programs for the purpose of expressing an opinion on the City of Madison's compliance with those requirements. While our audit provides a reasonable basis for our opinion on compliance, it does not provide a legal determination on the City of Madison's compliance with those requirements.

We have issued a separate document which contains the results of our audit procedures to comply with the Uniform Guidance and the *State Single Audit Guidelines*.

To the Honorable Mayor, Common Council, and Management  
City of Madison

#### ***OTHER INFORMATION IN DOCUMENTS CONTAINING AUDITED FINANCIAL STATEMENTS***

Our responsibility does not extend beyond the audited financial statements identified in this report. We do not have any obligation to and have not performed any procedures to corroborate other information contained in client prepared documents, such as official statements related to debt issues.

#### ***PLANNED SCOPE AND TIMING OF THE AUDIT***

We performed the audit according to the planned scope and timing previously communicated to you in our communication to those charged with governance dated June 29, 2015.

#### ***QUALITATIVE ASPECTS OF THE ENTITY'S SIGNIFICANT ACCOUNTING PRACTICES***

##### ***Accounting Policies***

Management is responsible for the selection and use of appropriate accounting policies. In accordance with the terms of our engagement letter, we will advise management about the appropriateness of accounting policies and their application. The significant accounting policies used by the City of Madison are described in Note I to the financial statements. As described in Note I to the financial statements, the City of Madison changed accounting policies related to financial reporting for pensions by adopting Statement of Governmental Accounting Standards (GASB) Statement No. 68, *Accounting and Financial Reporting for Pensions – an Amendment of GASB Statement No. 27* and GASB Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date – an Amendment of GASB Statement No. 68* in 2015. Accordingly, the accounting change has been retrospectively applied to prior periods presented as if the policy has always been used. The business-type activities and the water utility net position was restated to correct errors in previously reported construction work in progress and revenues. We noted no transactions entered into by the City of Madison during the year that were both significant and unusual, and of which, under professional standards, we are required to inform you, or transactions for which there is a lack of authoritative guidance or consensus.

##### ***Accounting Estimates***

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimates affecting the financial statements were:

1. The estimate of the self-insurance claims liability, which is based on a historical claims analysis and report prepared by the insurance actuaries.
2. The estimate of the Other Postemployment Benefits (OPEBs) liability, which is based upon information provided to actuaries contracted with by the City.
3. The estimate of allowance for doubtful loans receivables, ambulance receivables and municipal court receivables is based on historical revenues, historical loss levels, and an analysis of individual account collections.
4. Management's estimate of the net pension asset and related deferred outflows and inflows of resources is based on actuarial information obtained from the Wisconsin Retirement System.

We evaluated the key factors and assumptions used to develop all of these estimates in determining that they are reasonable in relation to the financial statements taken as a whole.

##### ***Financial Statement Disclosures***

The disclosures in the notes to the financial statements are neutral, consistent, and clear.

To the Honorable Mayor, Common Council, and Management  
City of Madison

***DIFFICULTIES ENCOUNTERED IN PERFORMING THE AUDIT***

We encountered no significant difficulties in dealing with management in performing our audit.

***CORRECTED AND UNCORRECTED MISSTATEMENTS***

Professional standards require us to accumulate all known and likely misstatement identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management.

A summary of uncorrected financial statement misstatements follows this required communication. Management has determined that their effects are immaterial, both individually and in the aggregate, to the financial statements taken as a whole.

We prepare certain GASB No. 34 conversion entries which are summarized in the "Reconciliation of the Balance Sheet of Governmental Funds to the Statement of Net Position" and the "Reconciliation of the Statement of Revenues, Expenditures, and Changes in Fund Balances of Governmental Funds to the Statement of Activities" in the financial statements.

***DISAGREEMENTS WITH MANAGEMENT***

For purposes of this letter, professional standards define a disagreement with management as a matter, whether or not resolved to our satisfaction, concerning a financial accounting, reporting, or auditing matter that could be significant to the financial statements or the auditors' report. We are pleased to report that no such disagreements arose during the course of our audit.

***CONSULTATIONS WITH OTHER INDEPENDENT ACCOUNTANTS***

In some cases, management may decide to consult with other accountants about auditing and accounting matters. If a consultation involves application of an accounting principle to the governmental unit's financial statements or a determination of the type of auditors' opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

***MANAGEMENT REPRESENTATIONS***

We have requested certain representations from management that are included in the management representation letter. This letter follows this required communication.

***INDEPENDENCE***

We are not aware of any relationships between Baker Tilly Virchow Krause, LLP and the City of Madison that, in our professional judgment, may reasonably be thought to bear on our independence.

To the Honorable Mayor, Common Council, and Management  
City of Madison

***INDEPENDENCE*** (cont.)

Relating to our audit of the financial statements of the City of Madison for the year ended December 31, 2015, Baker Tilly Virchow Krause, LLP hereby confirms that we are, in our professional judgment, independent with respect to the City in accordance with the Code of Professional Conduct issued by the American Institute of Certified Public Accountants, and provided no services to the City other than audit services provided in connection with the audit of the current year's financial statements and nonaudit services which in our judgment do not impair our independence.

- > Financial statement preparation
- > Adjusting journal entries
- > Compiled regulatory reports
- > Financial analysis of anaerobic digester
- > Annual tax update

None of these nonaudit services constitute an audit under generally accepted auditing standards, including *Government Auditing Standards*.

***OTHER AUDIT FINDINGS OR ISSUES***

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the City of Madison's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

***OTHER MATTERS***

We applied certain limited procedures to the required supplementary information (RSI) that supplements the basic financial statements. Our procedures consisted of inquiries of management regarding the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We did not audit the RSI and do not express an opinion or provide any assurance on the RSI.

We were engaged to report on the supplementary information which accompanies the financial statements but is not RSI. With respect to the supplementary information accompanying the financial statements, we made certain inquiries of management and evaluated the form, content, and methods of preparing the information to determine that the information complies with accounting principles generally accepted in the United States of America, the method of preparing it has not changed from the prior period, and the information is appropriate and complete in relation to our audit of the financial statements. We compared and reconciled the supplementary information to the underlying accounting records used to prepare the financial statements or to the financial statements themselves.

We were not engaged to report on other information which accompanies the financial statements but are not RSI. We did not audit or perform other procedures on this other information and we do not express an opinion or provide any assurance on it.

To the Honorable Mayor, Common Council, and Management  
City of Madison

***RESTRICTION ON USE***

This report is intended solely for the information and use of the mayor, common council, and management and is not intended to be, and should not be, used by anyone other than the specified parties.

We welcome the opportunity to discuss the information included in this letter and any other matters. Thank you for allowing us to serve you.

*Baker Tilly Virchow Krause, LLP*

Madison, Wisconsin  
July 15, 2016

**SUMMARY OF UNCORRECTED FINANCIAL STATEMENT MISSTATEMENTS**

## CITY OF MADISON

### SUMMARY OF UNCORRECTED FINANCIAL STATEMENT MISSTATEMENTS December 31, 2015

	Financial Statements Effect – Debit (Credit) to Financial Statement Total									
	Current Assets	Noncurrent Assets	Total Assets/Deferred Outflows	Current Liabilities	Noncurrent Liabilities	Total Liabilities/ Deferred Inflows	Total Net Position/ Fund Balances	Total Revenues	Total Expenses/ Expenditures	Change in Net Position/ Fund Balances
Capital Projects Fund	\$ -	\$ -	\$ (385,072)	\$ -	\$ -	\$ 51,556	\$ 333,516	\$ -	\$ 61,794	\$ 61,794
Stormwater Utility	-	-	-	-	(20,921)	(20,921)	20,921	-	20,921	20,921
Sewer Utility	-	-	-	-	(75,814)	(75,814)	75,814	-	75,814	75,814
Remaining funds	-	-	(114,280)	-	-	668,837	(554,557)	(668,436)	51,682	(616,754)

## **MANAGEMENT REPRESENTATIONS**





## Finance Department

David P. Schmiedicke, Finance Director

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[www.cityofmadison.com/finance](http://www.cityofmadison.com/finance)

July 15, 2016

Baker Tilly Virchow Krause, LLP  
Ten Terrace Court  
P.O. Box 7398  
Madison, WI 53707-7398

Dear Baker Tilly Virchow Krause, LLP:

We are providing this letter in connection with your audit of the financial statements of the City of Madison as of December 31, 2015 and for the year then ended for the purpose of expressing opinions as to whether the financial statements present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the City of Madison and the respective changes in financial position and cash flows, where applicable, in conformity with accounting principles generally accepted in the United States of America. We confirm that we are responsible for the fair presentation of the previously mentioned financial statements in conformity with accounting principles generally accepted in the United States of America. We are also responsible for adopting sound accounting policies, establishing and maintaining internal control over financial reporting, and preventing and detecting fraud.

Certain representations in this letter are described as being limited to matters that are material. Items are considered material, regardless of size, if they involve an omission or misstatement of accounting information that, in the light of surrounding circumstances, makes it probable that the judgment of a reasonable person relying on the information would be changed or influenced by the omission or misstatement. An omission or misstatement that is monetarily small in amount could be considered material as a result of qualitative factors.

We confirm, to the best of our knowledge and belief, the following representations made to you during your audit.

### *Financial Statements*

1. We have fulfilled our responsibilities, as set out in the terms of the audit engagement letter.
2. The financial statements referred to above are fairly presented in conformity with accounting principles generally accepted in the United States of America. We have engaged you to advise us in fulfilling that responsibility. The financial statements include all properly classified funds of the primary government and all component units required by accounting principles generally accepted in the United States of America to be included in the financial reporting entity.
3. We acknowledge our responsibility for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

4. We acknowledge our responsibility for the design, implementation, and maintenance of internal control to prevent and detect fraud.
5. Significant assumptions we used in making accounting estimates, if any, are reasonable.
6. Related party relationships and transactions, including revenues, expenditures/expenses, loans, transfers, leasing arrangements, and guarantees, and amounts receivable from or payable to related parties have been appropriately accounted for and disclosed in accordance with the requirements of accounting principles generally accepted in the United States of America.
7. All events subsequent to the date of the financial statements and for which accounting principles generally accepted in the United States of America require adjustment or disclosure have been adjusted or disclosed. No other events, including instances of noncompliance, have occurred subsequent to the balance sheet date and through the date of this letter that would require adjustment to or disclosure in the aforementioned financial statements or in the schedule of findings and questioned costs.
8. All material transactions have been recorded in the accounting records and are reflected in the financial statements and the schedule of expenditures of federal and state awards.
9. We believe the effects of the uncorrected financial statement misstatements summarized in the attached schedule are immaterial, both individually and in the aggregate, to the basic financial statements as a whole. In addition, you have recommended adjusting journal entries, and we are in agreement with those adjustments.
10. There are no known or possible litigation, claims, and assessments whose effects should be considered when preparing the financial statements. There are no unasserted claims or assessments that our lawyer has advised us are probable of assertion and must be disclosed in accordance with accounting principles generally accepted in the United States of America.
11. Guarantees, whether written or oral, under which the City is contingently liable, if any, have been properly recorded or disclosed.

*Information Provided*

12. We have provided you with:
  - a. Access to all information, of which we are aware, that is relevant to the preparation and fair presentation of the financial statements, such as financial records and related data, documentation, and other matters and all audit or relevant monitoring reports, if any, received from funding sources.
  - b. Additional information that you have requested from us for the purpose of the audit.
  - c. Unrestricted access to persons within the entity from whom you determined it necessary to obtain audit evidence.
  - d. Minutes of the meetings of common council or summaries of actions of recent meetings for which minutes have not yet been prepared.
13. We have disclosed to you results of our assessment of the risk that the financial statements may be materially misstated as a result of fraud.
14. We have no knowledge of any fraud or suspected fraud that affects the entity and involves:
  - a. Management,
  - b. Employees who have significant roles in internal control, or
  - c. Others where the fraud could have a material effect on the financial statements.
15. We have no knowledge of any allegations of fraud or suspected fraud affecting the entity received in communications from employees, former employees, regulators, or others.

16. We have no knowledge of known instances of noncompliance or suspected noncompliance with provisions of laws, regulations, contracts, or grant agreements, or abuse, whose effects should be considered when preparing financial statements.

17. We have disclosed to you all known related parties and all the related party relationships and transactions of which we are aware.

*Other*

18. There have been no communications from regulatory agencies concerning noncompliance with, or deficiencies in, financial reporting practices.

19. We have a process to track the status of audit findings and recommendations.

20. We have identified to you any previous financial audits, attestation engagements, and other studies related to the audit objectives and whether related recommendations have been implemented.

21. We have provided our views on reported findings, conclusions, and recommendations, as well as our planned corrective actions, for our report.

22. The City has no plans or intentions that may materially affect the carrying value or classification of assets, liabilities, or equity.

23. We are responsible for compliance with federal, state, and local laws, regulations, and provisions of contracts and grant agreements applicable to us, including tax or debt limits, debt contracts, and IRS arbitrage regulations; and we have identified and disclosed to you all federal, state, and local laws, regulations and provisions of contracts and grant agreements that we believe have a direct and material effect on the determination of financial statement amounts or other financial data significant to the audit objectives, including legal and contractual provisions for reporting specific activities in separate funds.

24. There are no:

- a. Violations or possible violations of budget ordinances, federal, state, and local laws or regulations (including those pertaining to adopting, approving and amending budgets), provisions of contracts and grant agreements, tax or debt limits, and any related debt covenants whose effects should be considered for disclosure in the financial statements or as a basis for recording a loss contingency, or for reporting on noncompliance, except those already disclosed in the financial statement, if any.
- b. Other liabilities or gain or loss contingencies that are required to be accrued or disclosed by accounting principles generally accepted in the United States of America.
- c. Nonspendable, restricted, committed, or assigned fund balances that were not properly authorized and approved.
- d. Rates being charged to customers other than the rates as authorized by the applicable authoritative body.
- e. Violations of restrictions placed on revenues as a result of bond resolution covenants such as revenue distribution or debt service funding.

25. In regards to the nonattest services performed by you listed below, we have 1) accepted all management responsibility; 2) designated an individual with suitable skill, knowledge, or experience to oversee the services; 3) evaluated the adequacy and results of the services performed, and 4) accepted responsibility for the results of the services.

- a. Financial statement preparation
- b. Adjusting journal entries
- c. Compiled regulatory reports
- d. Financial analysis of anaerobic digester
- e. Annual tax update

None of these nonattest services constitute an audit under generally accepted auditing standards, including *Government Auditing Standards*.

26. The City of Madison has satisfactory title to all owned assets, and there are no liens or encumbrances on such assets nor has any asset been pledged as collateral.
27. The City of Madison has complied with all aspects of contractual agreements that would have a material effect on the financial statement in the event of noncompliance.
28. The financial statements include all component units as well as joint ventures with an equity interest, and properly disclose all other joint ventures and other related organizations, if any.
29. The financial statements properly classify all funds and activities.
30. All funds that meet the quantitative criteria in GASB Statement No. 34 and No. 37 for presentation as major are identified and presented as such and all other funds that are presented as major are particularly important to financial statement users.
31. Components of net position (net investment in capital assets; restricted; and unrestricted) and components of fund balance (nonspendable, restricted, committed, assigned and unassigned) are properly classified and, if applicable, approved.
32. The City of Madison has no derivative financial instruments such as contracts that could be assigned to someone else or net settled, interest rate swaps, collars or caps.
33. Provisions for uncollectible receivables, if any, have been properly identified and recorded.
34. Expenses have been appropriately classified in or allocated to functions and programs in the statement of activities, and allocations have been made on a reasonable basis.
35. Revenues are appropriately classified in the statement of activities within program revenues and general revenues.
36. Interfund, internal, and intra-entity activity and balances have been appropriately classified and reported.
37. Deposits and investment securities are properly classified as to risk, and investments are properly valued. Collateralization agreements with financial institutions, if any, have been properly disclosed.
38. Provision, when material, has been made to reduce excess or obsolete inventories to their estimated net realizable value.
39. Capital assets, including infrastructure and intangible assets, are properly capitalized, reported, and, if applicable, depreciated/amortized. Any known impairments have been recorded and disclosed.

40. Tax-exempt bonds issued have retained their tax-exempt status.
41. We have appropriately disclosed the City of Madison's policy regarding whether to first apply restricted or unrestricted resources when an expense is incurred for purposes for which both restricted and unrestricted net position are available and have determined that net position were properly recognized under the policy. We have also disclosed our policy regarding which resources (i.e. restricted, committed, assigned or unassigned) are considered to be spent first for expenditures for which more than one resource classification is available.
42. We acknowledge our responsibility for the required supplementary information (RSI). The RSI is measured and presented within prescribed guidelines and the methods of measurement and presentation have not changed from those used in the prior period. We have disclosed to you any significant assumptions and interpretations underlying the measurement and presentation of the RSI.
43. With respect to the supplementary information, (SI):
- a. We acknowledge our responsibility for presenting the SI in accordance with accounting principles generally accepted in the United States of America, and we believe the SI, including its form and content, is fairly presented in accordance with accounting principles generally accepted in the United States of America. The methods of measurement and presentation of the SI have not changed from those used in the prior period, and we have disclosed to you any significant assumptions or interpretations underlying the measurement and presentation of the supplementary information.
  - a. If the SI is not presented with the audited financial statements, we will make the audited financial statements readily available to the intended users of the supplementary information no later than the date we issue the supplementary information and the auditor's report thereon.
44. We assume responsibility for, and agree with, the findings of specialists in evaluating the incurred but not recorded liability and post employment benefits accrued and have adequately considered the qualifications of the specialists in determining the amounts and disclosures used in the financial statements and underlying accounting records. We did not give or cause any instructions to be given to specialists with respect to the values or amounts derived in an attempt to bias their work, and we are not otherwise aware of any matters that have had impact on the independence or objectivity of the specialists.
45. We agree with the restatement presented in the current year's financial statements.
46. We assume responsibility for, and agree with, the information provided by the Wisconsin Retirement System as audited by the Legislative Audit Bureau relating to the net pension asset/liability and related deferred outflows and deferred inflows and have adequately considered the reasonableness of the amounts and disclosures used in the financial statements and underlying accounting records. We also assume responsibility for the census data that has been reported to the plan.
47. With respect to federal and state award programs:
- a. We are responsible for understanding and complying with and have complied with the requirements of the Single Audit Act Amendments of 1996, OMB Circular A 133, *Audits of States, Local Governments, and Non-Profit Organizations*, *State Single Audit Guidelines*, including requirements relating to preparation of the schedule of expenditures of federal and state awards (SEFSA).

- b. We acknowledge our responsibility for presenting the SEFSA in accordance with the requirements of OMB Circular A-133 §310.b and the *State Single Audit Guidelines*, and we believe the SEFSA, including its form and content, is fairly presented in accordance with OMB Circular A-133 §310.b and the *State Single Audit Guidelines*. The methods of measurement and presentation of the SEFSA have not changed from those used in the prior period and we have disclosed to you any significant assumptions and interpretations underlying the measurement and presentation of the SEFSA.
- c. If the SEFSA is not presented with the audited financial statements, we will make the audited financial statements readily available to the intended users of the SEFSA no later than the date we issue the SEFSA and the auditors' report thereon.
- d. We have identified and disclosed to you all of our government programs and related activities subject to OMB Circular A-133 and the *State Single Audit Guidelines* and included in the SEFSA, expenditures made during the audit period for all awards provided by federal agencies in the form of grants, federal cost reimbursement contracts, loans, loan guarantees, property (including donated surplus property), cooperative agreements, interest subsidies, insurance, food commodities, direct appropriations, and other direct assistance.
- e. We are responsible for understanding and complying with, and have complied with the requirements of laws, regulations, and the provisions of contracts and grant agreements related to each of our federal and state programs and have identified and disclosed to you the requirements of laws, regulations, and the provisions of contracts and grant agreements that are considered to have a direct and material effect on each major federal and state program.
- f. We are responsible for establishing and maintaining, and have established and maintained, effective internal control over compliance for federal and state programs that provide reasonable assurance that we are administering our federal and state awards in compliance with laws, regulations, and the provisions of contracts and grant agreements that could have a material effect on our federal and state programs. We believe the internal control system is adequate and is functioning as intended. Also, no changes have been made in the internal control over compliance or other factors to the date of this letter that might significantly affect internal control, including any corrective action taken with regard to control deficiencies reported in the schedule of findings and questioned costs.
- g. We have made available to you all contracts and grant agreements (including amendments, if any) and any other correspondence with federal or state agencies or pass-through entities relevant to the programs and related activities.
- h. We have received no requests from a federal or state agency to audit one or more specific programs as a major program.
- i. We have complied with the direct and material compliance requirements including when applicable, those set forth in the OMB Compliance Supplement and the *State Single Audit Guidelines*, relating to federal and state awards and have identified and disclosed to you all amounts questioned and any known noncompliance with the direct and material compliance requirements of federal and state awards.
- j. We have disclosed any communications from grantors and pass-through entities concerning possible noncompliance with the direct and material compliance requirements, including communications received from the end of the period covered by the compliance audit to the date of the auditors' report.
- k. We have disclosed to you the findings received and related corrective actions taken for previous audits, attestation agreements, and internal or external monitoring that directly relate to the objectives of the compliance audit, if any, including findings received and corrective actions taken from the end of the period covered by the compliance audit to the date of the auditors' report.

- l. Amounts claimed or used for matching were determined in accordance with relevant guidelines in OMB Circular A-87, *Cost Principles for State, Local, and Tribal Governments*, and OMB's *Uniform Administrative Requirements for Grants and Cooperative Agreements to State and Local Governments*.
- m. We have disclosed to you our interpretation of compliance requirements that may have varying interpretations.
- n. We have made available to you all documentation related to the compliance with the direct and material compliance requirements, including information related to federal and state program financial reports and claims for advances and reimbursements.
- o. We have disclosed to you the nature of any subsequent events that provide additional evidence about conditions that existed at the end of the reporting period affecting noncompliance during the reporting period.
- p. We are not aware of any instances of noncompliance with direct and material compliance requirements that occurred subsequent to the period covered by the auditors' report.
- q. No changes have been made in internal control over compliance or other factors that might significantly affect internal control, including any corrective action we have taken regarding significant deficiencies or material weaknesses in internal control over compliance, subsequent to the date as of which compliance was audited.
- r. Federal and state program financial reports and claims for advances and reimbursements are supported by the books and records from which the financial statements have been prepared.
- s. The copies of federal and state program financial reports provided you are true copies of the reports submitted, or electronically transmitted, to the respective federal and state agency or pass-through entity, as applicable.
- t. We have monitored subrecipients to determine that they have expended pass-through assistance in accordance with applicable laws and regulations and have met the requirements of OMB Circular A-133 and the *State Single Audit Guidelines*.
- u. We have taken appropriate action, including issuing management decisions, on a timely basis after receipt of subrecipients' auditors' reports that identified noncompliance with laws, regulations, or the provisions of contracts or grant agreements to ensure that subrecipients have taken the appropriate and timely corrective action on findings.
- v. We have considered the results of subrecipient audits and made any necessary adjustments to our books and records.
- w. We have charged costs to federal and state awards in accordance with applicable cost principles.
- x. We are responsible for and have accurately prepared the summary schedule of prior audit findings to include all findings required to be included by OMB Circular A-133 and the *State Single Audit Guidelines* and we have provided you with all information on the status of the follow-up on prior audit findings by federal and state awarding agencies and pass-through entities, including all management decisions.
- y. We are responsible for and have accurately prepared the auditee section of the Data Collection Form as required by OMB Circular A-133.
- z. We are responsible for preparing and implementing a corrective action plan for each audit finding.

Sincerely,

City of Madison

Signed:

John A. McDermott

Signed:

[Signature]

Signed:

David P. Blumenthal

Signed:

Paul R. Ryan