

# **CITY OF WATERLOO**

Waterloo, Wisconsin

**COMMUNICATION TO THOSE CHARGED  
WITH GOVERNANCE AND MANAGEMENT**

As of and for the Year Ended December 31, 2016

# CITY OF WATERLOO

## TABLE OF CONTENTS

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	<u>Page No.</u>
Required Communication of Internal Control Related Matters Identified in the Audit to Those Charged with Governance	1
Internal Control Over Financial Reporting	2
Internal Control Environment	2 – 3
Information Technology System Internal Controls	4
Other Communications to Those Charged with Governance	
Two Way Communication Regarding Your Audit	5 – 6
Communication of Other Control Deficiencies, Recommendations, and Informational Points to Management that are not Material Weaknesses or Significant Deficiencies	7 – 12
Required Communications by the Auditor to Those Charged with Governance	13 – 16
Management Representations	

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

To the City Council  
City of Waterloo  
Waterloo, Wisconsin

In planning and performing our audit of the financial statements of the City of Waterloo as of and for the year ended December 31, 2016, 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 Communication to Those Charged with Governance and Management was issued to the Waterloo Water and Light Commission. The information contained in that report 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.

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
- > Internal Control Environment
- > Information Technology System Internal Controls

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  
April 12, 2017

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 provide your organization with the ability to process and record accurate monthly and year-end transactions and annual financial reports.

Our audit includes a review and evaluation of the 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 the year and at year-end.
- > Material misstatements are identified and corrected during the normal course of duties.
- > Complete and accurate financial statements, including footnotes, are prepared.
- > Financial reports are independently reviewed for completeness and accuracy.

Our evaluation of the internal controls over financial reporting has identified control deficiencies that are considered material weakness surrounding the preparation of financial statements and footnotes, adjusting journal entries identified by the auditors, and an independent review of financial reports.

Management has not prepared financial statements that are in conformity with generally accepted accounting principles. In addition, material misstatements in the general ledger were identified during the financial audit.

This level of internal control over financial reporting can be a difficult task for governments that operate with only enough staff to process monthly transactions and reports, and often rely on their auditors to propose certain year-end audit entries and financial statements

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## **INTERNAL CONTROL ENVIRONMENT**

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A properly designed system of internal control includes adequate staffing as well as policies and procedures to properly segregate duties. 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, due to staffing and financial limitations, the proper internal controls are not in place to achieve adequate segregation of duties. As a result, errors, irregularities or fraud could occur as part of the financial reporting process that may not be discovered by someone in your organization. Therefore, we are reporting a material weakness related to the internal control environment.

There are also certain controls that are not currently in place related to significant transaction cycles. As a result, there is a risk that erroneous or unauthorized transactions or misstatements could occur without the knowledge of management or the governing body. Our recommendations for strengthening controls are listed below.

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## **INTERNAL CONTROL ENVIRONMENT (cont.)**

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### ***CONTROLS OVER ACCOUNTS PAYABLE/DISBURSEMENTS***

- > Persons processing accounts payable and those with access to the system should be separate from those ordering or receiving goods or services.
- > There should be an appropriate system for review and approval of vendors.
- > There is evidence that the council reviews check registers; however, there should be evidence to show that the check sequence has been accounted for by the council and that any gaps between approved check registers do not exist.

### ***CONTROLS OVER PAYROLL***

- > Persons preparing the payroll should be independent of other personnel duties and restricted from access to the payroll account.

### ***CONTROLS OVER PROPERTY TAXES***

- > Batch collections should be reconciled from the general ledger to the tax collection system by someone independent of the process.
- > Bank reconciliations for the tax account should be performed by someone independent of the tax collection process.

### ***CONTROLS OVER MONTHLY AND YEAR-END ACCOUNTING***

- > Account reconciliations prepared throughout the year should be performed by someone independent of processing transactions in the account.
- > Year-end reconciliations (retainages) should be reviewed and approved by someone other than the preparer.

### ***CONTROLS OVER ELECTRONIC FUND TRANSFERS***

- > A separate review/approval should be required for all wire transfers.

We recommend that a designated employee review the segregation of duties, risks, and these potential controls and determine whether additional controls should be implemented. This determination should take into consideration a cost / benefit analysis.

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## **INFORMATION TECHNOLOGY SYSTEM INTERNAL CONTROLS**

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- > The city lacks various controls surrounding its information technology related to the accounting functions. These include controls over passwords and proper system back-ups that are completed and tested on a regularly scheduled basis.
  
- > The city's present software system lacks certain security features that, if operated improperly, would not allow for the identification of changes made to financial data after the original entry of such data. This is a control weakness that exists in many database software packages, including Microsoft Office Access, which is the basis for your software. Many of the system users may not possess the technical knowledge to operate the system in a manner that would impair the system's control integrity. However, it is possible that some users may possess the knowledge to circumvent the system's controls. Therefore, we believe that it is reasonably possible that a material error could occur resulting in a misstatement of the city's financial statements, and your controls would not prevent or detect the error. Accordingly, we are required to communicate this fact to you.

**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, 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 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 to determine whether they have been implemented. We will use such knowledge to:
  - > Identify types of potential misstatements.
  - > Consider factors that affect the risks of material misstatement.
  - > Design tests of controls, when applicable, and substantive procedures.

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.

- 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 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. Our responsibility is to plan and perform the audit to obtain reasonable assurance that material misstatements, 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, which we also audit.

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?

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

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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. If necessary, we may 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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## INFORMATIONAL POINTS

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### ***IMPACT FEE SPEND-DOWN REQUIREMENTS***

The city currently collects impact fees under Wisconsin State statute 66.0617. Revenues collected from impact fees are required to be placed in a segregated, interest-bearing account. Impact fee revenues and interest earned on impact fee revenues may only be expended on capital items for which the impact fees were imposed.

Statute 66.0617 was first amended by the 2005 Wisconsin Act 203 and later by the 2007 Wisconsin Act 44. These acts modified spend-down requirements as follows:

- > An impact fee that was collected before January 1, 2003, must be used for the purpose for which it was collected no later than December 31, 2012. If the fee was not used by that date, it was to be refunded to the current owner of the property, along with any accumulated interest.
- > Impact fees that are collected after April 10, 2006 and collected within seven (7) years of the effective date of the ordinance imposing the fees must be used within ten (10) years of collection with a possibility of extending the time for an additional three (3) years under extenuating circumstances or hardship.
- > An impact fee that is collected after April 10, 2006 and collected more than seven (7) years after the effective date of the ordinance must be used within a reasonable period of time after they are collected to pay the capital costs for which they were imposed, or they shall be refunded to the current property owner, along with any accumulated interest.

We recommend that management review the impact fee ordinance, collections, and eligible costs to ensure compliance with the spend-down requirements.

### ***WISCONSIN RETIREMENT SYSTEM AND GASB No. 68***

As you begin your second year reporting your pension activity under the requirements of GASB Statement No. 68, let's review how this information affects your financial statements.

Wisconsin Retirement System (WRS) pension information is reported on a one year lag in your financial statements, so current year balances are the WRS amounts reported for the plan year ended December 31, 2015. The following is a summary of the status of the WRS for the current and previous year (amounts are in billions).

	<u>Current Year 2015</u>	<u>Previous Year 2014</u>	<u>Change</u>
Total Pension Liability	\$ 90.1	\$ 89.7	\$ 0.4
Net Assets Available for Benefits	<u>88.5</u>	<u>92.1</u>	<u>(3.6)</u>
Net Pension Liability (Asset)	<u>\$ 1.6</u>	<u>\$ (2.4)</u>	<u>\$ 4.0</u>

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**INFORMATIONAL POINTS (cont.)**

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***WISCONSIN RETIREMENT SYSTEM AND GASB No. 68 (cont.)***

As noted above, for the current year, WRS reports a net pension liability compared to a net pension asset for the previous year. Although 2015 contributions to WRS from employers and employees was consistent with the 2014 amounts, net investment income for 2015 decreased from \$4.9 billion to a net loss of \$0.7 billion, a \$5.6 billion swing. This decrease in net investment income was primarily due to declines in investment returns and market values as a result of the 2015 market closing at its lowest point since 2008. In addition, benefit payments increased \$0.3 billion or 6.3% from 2014 to 2015 partially as a result of an additional 6,200 retirees receiving benefits. Your government's proportionate share of the current year net pension liability is reported in your government-wide financial statements.

It should be noted that since the net pension liability (asset) is heavily dependent upon the market value of the net assets available for benefits, increases and decreases in the market can and will significantly change the amounts reported on your financial statements in the future.

***REVISIONS TO ACTUARIAL STANDARDS IMPACT IMPLICIT OPEB LIABILITIES***

Current guidance for the accounting and financial reporting of other postemployment benefits (OPEBs) by governmental employers is outlined in GASB No. 45. The most common OPEB is retiree healthcare. This standard applies to both explicit benefits – those where the employer pays for all or a portion of the premiums – as well as implicit benefits. An implicit OPEB occurs when retirees are allowed to remain on the employer's health care plan at their own cost but pay the same blended premium as current employees. While the employer is not paying a portion of the retiree premium they may be paying a higher premium for their active employees than they otherwise would if age adjusted premiums were calculated for each group. This results in an implicit rate subsidy.

When GASB 45 was drafted it allowed community rated plans, such as the State of Wisconsin ETF Plan (the "Plan"), to use unadjusted premiums to the extent allowed by actuarial standards. As such, employers participating in the Plan and not providing explicit retiree benefits have not been required to calculate or record an implicit OPEB liability. However, revisions to Actuarial Standard of Practice (ASOP) No. 6 now provide very limited circumstances in which the use of unadjusted premiums by actuaries will be considered appropriate. In fact, the Plan has indicated that unadjusted premiums will not be able to be used under the new rules. The revisions to ASOP No. 6 are effective for actuarial studies with a measurement date on or after March 31, 2015. This will impact financial reporting periods after December 31, 2015. As a participant in the Plan, which has not calculated or recorded an OPEB liability in the past, the city evaluated the implicit rate subsidy under GASB 45 as of December 31, 2016 and determined that it was immaterial.

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**CURRENT YEAR POINTS**

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***ADVANCES***

Two of the city's tax incremental financing (TIF) districts are currently relying upon other funds of the city. While it is not unusual for active TIF districts to rely upon or borrow from other funds during their earlier years, it also requires careful monitoring through what is called TIF projections. Performing TIF projections is not something that is within the scope of an audit. The distinction is that an audit looks back to determine the current status of a TIF, while a projection attempts to estimate the long-term viability of a TIF, including whether or not it will be able to meet its debt obligations during its life.

We recommend the city continue to update its TIF projections, including the amounts other funds have advanced or borrowed to the TIFs.

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**CURRENT YEAR POINTS (cont.)**

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**ADVANCES (cont.)**

As of December 31, 2016, the following TIF Districts had an advance recorded from other funds:

412 TIF No. 2	\$1,132,514
413 TIF No. 3	<u>180,171</u>
Total	<u>\$1,312,685</u>

These monies were advanced from 410 TIF District No. 1.

It should be noted that the advance total at December 31, 2014 for the TIF's was \$727,358, resulting in a \$585,327 increase since that time.

As allowable under TIF statutes, the common council and joint review board, in 2011, approved sharing increments from TIF District No. 1 (donor district) to TIF District No. 2 (donee district). Transfers were approved to begin in 2012. As of December 31, 2016, no transfers have been made, but this is something the city could consider going forward.

Your community's long-term success is important. As a governing body, your involvement and understanding of your community's financial activities will help you make informed decisions regarding the future of your community.

**TIF CAPITAL EXPENDITURES**

As of December 31, 2016, 412 TIF No. 2 is at >30% of their budgeted capital expenditures per the project plan. The city is now required to have a 30% TIF audit for TIF No. 2.

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**PRIOR YEAR POINTS**

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**AMBULANCE ALLOWANCE**

The city provides ambulance services to its citizens and has hired a third party to complete the billing and collection for those services. Many of the outstanding balances are not likely to be fully collected, based on Medicare or Medicaid disallowances. The city should periodically monitor the allowance for uncollectible ambulance accounts for reasonableness and make adjustments as needed.

**Status (12/31/16)**

This recommendation still pertains.

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**PRIOR YEAR POINTS (cont.)**

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***BUDGET REQUIREMENTS***

Wisconsin state statutes regarding municipal budgeting specify the information that should be incorporated into the city's class 1 notice regarding the budget public hearing and the budget document adopted by the city.

The city's budget notice should include the following items:

- A. Summary budget for the proposed budget, the budget in effect and the percentage changed between the budget of the current year and the proposed budget. A summary budget would include:
  - 1. All expenditures by major expenditure category for general fund.
  - 2. All revenues by major revenue source for general fund.
  - 3. Any financing source and use not included in 1. and 2. above.
  - 4. All beginning and year-end fund balances for all funds.
  - 5. Total revenues and expenditures for each fund.
  - 6. Summary totals of revenues and expenditures (all funds).
  - 7. Local property taxes for each fund and the total for all funds.
  - 8. List of budget increases and decreases due to new or discontinued activities.
- B. The place where the budget, in detail, is available for public inspection.
- C. The time and place for holding the public hearing.

The budget document is required to include these items:

- A. List all existing indebtedness.
- B. Actual revenues and expenditures of the preceding year.
- C. Actual revenues and expenditures for not less than the first six months of the current year and estimated revenues and expenditures for the balance of the year.
- D. All anticipated revenue from all sources and all proposed appropriations for the ensuing year (proposed budget).
- E. All anticipated unexpended or unappropriated balances and surpluses for each fund.

We recommend that the city review state statutes pertaining to municipal budgets. When preparing the city budget, you should include the items mentioned above.

***Status (12/31/16)***

This recommendation still pertains.

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## **PRIOR YEAR POINTS (cont.)**

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### ***UNCOLLATERALIZED DEPOSITS***

Governmental Accounting Standards Board (GASB) Statement No. 40 requires disclosures about deposits and investments. One of the main purposes of GASB Statement No. 40 is to indicate to users of financial statements the custodial risks involved with an entity's deposits and investments. These disclosures are included in the notes to your financial statements.

Here are the current rules.

- > In-state accounts (deposits are held in an institution in the same state where the government is located)
  - 1) Up to \$250,000 for the combined amount of all time (CDs) and savings deposits (includes NOW accounts and money market deposit accounts)
  - 2) Up to \$250,000 for all demand deposit accounts (defined as "deposits payable on demand and for which the depository institution does not reserve the right to require advanced notice of withdrawal")
- > Out-of-state accounts (deposits are held in an institution outside of the state where the government is located)
  - 1) Up to \$250,000 for the combined total of all deposit accounts

### ***Status (12/31/16)***

As of December 31, 2016, the city had \$2,358,216 of uncollateralized deposits with its banks. We recommend that the city evaluate this to determine if further action is necessary. We also recommend the city review their collateral agreements with the banks to ensure the safety of its deposits.

### ***DECENTRALIZED CASH COLLECTIONS***

Many governments collect cash at numerous decentralized locations that are separate from the primary system of accounting procedures and controls. The opportunity for theft is often higher at those locations because one person is frequently involved in most, if not all, aspects of a transaction (i.e. lack of segregation of duties).

Examples in your government that fit this situation include: library, police and parks.

Management is responsible for designing and implementing controls and procedures to detect and prevent fraud. As a result, we recommend that management review its decentralized cash collection procedures and controls on a periodic basis and make changes as necessary to strengthen the internal control environment. Reviewing the adequacy of the controls is a responsibility of the governing body.

Below are example procedures and controls to help mitigate the risk of loss at decentralized cash collection points:

- > Implement a centralized receipting process with adequate segregation of duties
- > For cash collections, ensure pre-numbered receipts are being used and all receipts in the sequence are being reviewed by someone other than the person receipting the cash and receipts tie to deposits
- > Perform surprise procedures at decentralized locations (cash counts, walkthrough of processes, etc.)



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**PRIOR YEAR POINTS (cont.)**

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***DECENTRALIZED CASH COLLECTIONS (cont.)***

- > Require regular cash deposits to minimize collection on-hand
- > Limit the number of separate bank accounts
- > Segregate duties as much as possible – the person receipting cash should be separate from the person preparing deposits and the person reconciling bank accounts should be separate from the cash collection activity
- > Perform a month-to-month or year-to-year comparison to look for unusual changes in collections
- > If collecting from a drop box site, consider sending two people to collect the funds, especially during peak times

As always, the cost of controls and staffing must be weighed against the benefits of safeguarding your assets.

***Status (12/31/16)***

This recommendation still pertains.

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

To the City Council  
City of Waterloo  
Waterloo, 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 Waterloo for the year ended December 31, 2016 and have issued our report thereon dated April 12, 2017. This letter presents communications required by our professional standards.

***OUR RESPONSIBILITY UNDER AUDITING STANDARDS  
GENERALLY ACCEPTED IN THE UNITED STATES OF AMERICA***

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. 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 those charged with governance of their responsibilities.

As part of the audit we obtained an understanding of the entity and its environment, including internal control, sufficient to assess the risks of material misstatement of the financial statements and to design the nature, timing and extent of further audit procedures. The audit was not designed to provide assurance on internal control or to identify deficiencies in internal control.

***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 during our meeting with you on May 15, 2016 and in our letter about planning matters dated March 31, 2016.

To the City Council  
City of Waterloo

**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 Waterloo are described in Note I to the financial statements. No new accounting policies were adopted and the application of existing policies were not changed during 2016. We noted no transactions entered into by the City of Waterloo 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:

Management's estimate of the net pension liability, deferred outflows and deferred inflows related to pension are based upon information provided by the Wisconsin Retirement System. These also impact pension expense.

Management's estimate of the allowance for ambulance receivables is based on payment history for this type of receivable.

We evaluated the key factors and assumptions used to develop 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.

**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 misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management.

Management has corrected all such misstatements.

The following is a summary of material financial statement misstatements (audit adjustments):

	<u>Amount</u>
Record grants receivable	\$ 198,310
Closeout Honorary fire department fund	186,318

To the City Council  
City of Waterloo

***CORRECTED AND UNCORRECTED MISSTATEMENTS (cont.)***

In addition, we prepared 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 Waterloo that, in our professional judgment, may reasonably be thought to bear on our independence.

Relating to our audit of the financial statements of the City of Waterloo 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 of Waterloo in accordance with the Code of Professional Conduct issued by the American Institute of Certified Public Accountants. We provided no services to the City of Waterloo 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, including:

- > Financial statement preparation
- > Adjusting journal entries
- > Compiled regulatory reports
- > Civic Systems software

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

To the City Council  
City of Waterloo

***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 Waterloo'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, 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.

***RESTRICTION ON USE***

This information is intended solely for the use of the city 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 work with you.

*Baker Tilly Virchow Krause, LLP*

Madison, Wisconsin  
April 12, 2017

## **MANAGEMENT REPRESENTATIONS**



136 North Monroe Street  
Waterloo, WI 53594  
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April 12, 2017

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 Waterloo as of December 31, 2016 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 discretely presented component unit, each major fund, and the aggregate remaining fund information of the City of Waterloo 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. 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.
7. All material transactions have been recorded in the accounting records and are reflected in the financial statements.
8. All known audit and bookkeeping adjustments have been included in our financial statements, and we are in agreement with those adjustments.
9. 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.
10. Guarantees, whether written or oral, under which the City of Waterloo is contingently liable, if any, have been properly recorded or disclosed.

*Information Provided*

11. 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.
  - 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 City Council or summaries of actions of recent meetings for which minutes have not yet been prepared.
12. We have not completed an assessment of the risk that the financial statements may be materially misstated as a result of fraud.
13. 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.
14. 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.
15. 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.

16. There are no known related parties or related party relationships and transactions of which we are aware.

*Other*

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

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

19. 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.

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

21. 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.

22. 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.

23. 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. Civic Systems software

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

24. The City of Waterloo 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.

25. The City of Waterloo has complied with all aspects of contractual agreements that would have a material effect on the financial statement in the event of noncompliance.
26. The financial statements include all component units. There are no joint ventures with an equity interest, or other joint ventures or other related organizations that should be reported.
27. The financial statements properly classify all funds and activities.
28. 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.
29. 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.
30. The City of Waterloo has no derivative financial instruments such as contracts that could be assigned to someone else or net settled, interest rate swaps, collars or caps.
31. Provisions for uncollectible receivables, if any, have been properly identified and recorded.
32. 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.
33. Revenues are appropriately classified in the statement of activities within program revenues and general revenues.
34. Interfund, internal, and intra-entity activity and balances have been appropriately classified and reported.
35. Deposits and investments are properly classified, valued, and disclosed (including risk disclosures, collateralization agreements, valuation methods, and key inputs, as applicable).
36. Capital assets, including infrastructure and intangible assets, are properly capitalized, reported, and, if applicable, depreciated/amortized. Any known impairments have been recorded and disclosed.
37. Tax-exempt bonds issued have retained their tax-exempt status.
38. We have appropriately disclosed the City of Waterloo'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 (that is, restricted, committed, assigned or unassigned) are considered to be spent first for expenditures for which more than one resource classification is available.
39. 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.

40. With respect to the supplementary information, (SI):

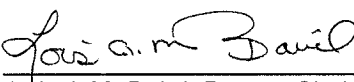
- a. We acknowledge our responsibility for presenting the SI in accordance with accounting principles generally accepted in the United States of America, and we believe the SI, including its form and content, is fairly presented in accordance with accounting principles generally accepted in the United 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.

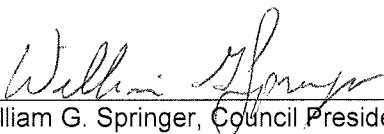
41. We assume responsibility for, and agree with, the information provided by the Wisconsin Retirement System as audited by the Legislative Audit Bureau relating to the net pension asset/liability and related deferred outflows and deferred inflows and have adequately considered the reasonableness of 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.

Sincerely,

City of Waterloo

Signed:   
Morton J. Hansen, City Clerk/Treasurer

Signed:   
Lois A.M. Baird, Deputy Clerk/Treasurer

Signed:   
William G. Springer, Council President