

**OTSEGO COUNTY ROAD COMMISSION
FINANCIAL REPORT
DECEMBER 31, 2014**

OTSEGO COUNTY

BOARD OF COUNTY ROAD COMMISSIONERS

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Engineer - Manager

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OTSEGO COUNTY ROAD COMMISSION

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James M. Anderson, P.C.

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INDEPENDENT AUDITOR'S REPORT

June 3, 2015

Board of County Road Commissioners
Otsego County Road Commission
Gaylord, MI 49734

Report on the Financial Statements

I have audited the accompanying financial statements of the governmental activities and major fund of the Otsego County Road Commission, a component unit of the County of Otsego, Michigan as of and for the year ended December 31, 2014, which collectively comprise the Road Commission's basic financial statements, as listed in the table of contents, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes 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.

Auditor's Responsibility

My responsibility is to express opinions on these financial statements based on my audit. I conducted my audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that I plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, I express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of financial statements.

I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinions.

Opinions

In my opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities and major fund of the Otsego County Road Commission as of December 31, 2014, and the respective changes in financial position for the year then ended in accordance with accounting principles generally accepted in the United States of America.


Other Matters

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison information on pages 4-10 and 33-34 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. I have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to my inquiries, the basic financial statements, and other knowledge I obtained during my audit of the basic financial statements. I do not express an opinion or provide any assurance on the information because the limited procedures do not provide me with sufficient evidence to express an opinion or provide any assurance.

My audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Otsego County Road Commission's financial statements as a whole. The introductory section and statistical section are presented for purposes of additional analysis and are not a required part of the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In my opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole. The introductory and statistical sections have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, I do not express an opinion or provide any assurance on them.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, I have also issued my report dated June 3, 2015, on my consideration of the Otsego County Road Commission's internal control over financial reporting and on my tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of my testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Otsego County Road Commission internal control over financial reporting and compliance.



JAMES M. ANDERSON, P.C.
CERTIFIED PUBLIC ACCOUNTANT

OTSEGO COUNTY ROAD COMMISSION
MANAGEMENT'S DISCUSSION & ANALYSIS
DECEMBER 31, 2014

USING THIS ANNUAL REPORT

The Otsego County Road Commission's discussion and analysis is designed to: a) assist the reader in focusing on significant financial issues; b) provide an overview of the road commission's financial activity; c) identify changes in the road commission's financial position (its ability to address the next and subsequent year challenges); d) identify any material deviations from the approved budget; and e) identify any issues or concerns.

REPORTING THE ROAD COMMISSION AS A WHOLE

The statement of net position and the statement of activities report information about the commission as a whole and about its activities in a way that helps answer the question on whether the road commission as a whole is better off or worse off as of a result of the year's activities. These statements include all assets, deferred outflows of resources, liabilities and deferred inflows of resources using the accrual basis of accounting, which is similar to the accounting method, used by most private-sector companies. All of the year's revenues and expenses are taken into account regardless of when cash is received or paid.

The two statements mentioned above, report the road commission's net position and the changes in them. The reader can think of the road commission's net position (the difference between assets and liabilities) as one way to measure the road commission's financial health or financial position. Over time, increases or decreases in the road commission's net position are one indicator of whether its financial health is improving or deteriorating.

REPORTING THE ROAD COMMISSION'S MAJOR FUND

Our analysis of the road commission's major fund begins on page 5. The fund financial statements begin on page 11 and provide detailed information about the major fund. The road commission currently has only one fund, the general operations fund, in which all of the road commission's activities are accounted. The general operations fund is a governmental type.

Governmental funds focus on how money flows into and out of this fund and the balances left at year end that are available for spending. This fund is reported using an accounting method called modified accrual accounting, which measures cash and all other financial assets that can readily be converted to cash. The governmental fund statements provide a detailed short-term view of the road commission's general governmental operations and the basic service it provides. Governmental fund information helps the reader to determine whether there are more or fewer financial resources that can be spent in the near future to finance the road commission's services. We describe the relationship (or differences) between governmental activities (reported in the statement of net position and the statement of activities) and the governmental fund in a reconciliation following the fund financial statements.

OTSEGO COUNTY ROAD COMMISSION
MANAGEMENT'S DISCUSSION & ANALYSIS (CONTINUED)
DECEMBER 31, 2014

THE ROAD COMMISSION AS A WHOLE

The road commission's net position decreased \$278,530 or approximately 1.59% for the year ended December 31, 2014. The net position and change in net position are summarized below.

Net position as of the year ended December 31, 2014 and 2013 follows:

	<u>12/31/2014</u>	<u>12/31/2013</u>	<u>Increase/ Decrease</u>
Current and Other Assets	\$ 3,247,873	\$ 1,898,137	\$ 1,349,736
Capital Assets (Net)	<u>24,996,205</u>	<u>24,616,660</u>	<u>379,545</u>
Total Assets	<u>28,244,078</u>	<u>26,514,797</u>	<u>1,729,281</u>
Long-Term Debt Outstanding	9,178,431	8,411,568	766,863
Other Liabilities	<u>551,261</u>	<u>536,710</u>	<u>14,551</u>
Total Liabilities	<u>9,729,692</u>	<u>8,948,278</u>	<u>781,414</u>
Deferred Inflows of Resources	<u>1,226,397</u>	<u>-</u>	<u>1,226,397</u>
Net Position			
Invested in Capital Assets	24,047,671	23,331,018	716,653
Restricted	<u>(6,759,682)</u>	<u>(5,764,499)</u>	<u>(995,183)</u>
Total Net Position	<u>\$ 17,287,989</u>	<u>\$ 17,566,519</u>	<u>\$ (278,530)</u>

OTSEGO COUNTY ROAD COMMISSION
MANAGEMENT'S DISCUSSION & ANALYSIS (CONTINUED)
DECEMBER 31, 2014

A summary of changes in net position for the year ended December 31, 2014 and 2013 follows:

	<u>12/31/2014</u>	<u>12/31/2013</u>	Increase/ Decrease
Program Revenues			
Charges for Services	\$ 1,219,039	\$ 1,458,008	\$ (238,969)
Operating Grants and Contributions	5,056,014	4,365,281	690,733
Capital Grants and Contributions	1,338,210	3,913,417	(2,575,207)
General Revenues			
Gain (Loss) on Disposals	23,470	16,334	7,136
Interest Earnings	3,302	2,221	1,081
Other	155,509	14,281	141,228
Total Revenues	<u>7,795,544</u>	<u>9,769,542</u>	<u>(1,973,998)</u>
Program Expenses			
Public Works	8,029,815	8,238,986	(209,171)
Interest Expense	44,259	36,238	8,021
Total Program Expenses	<u>8,074,074</u>	<u>8,275,224</u>	<u>(201,150)</u>
Changes in Net Position	(278,530)	1,494,318	(1,772,848)
Net Position - Beginning of Year	<u>17,566,519</u>	<u>16,072,201</u>	<u>1,494,318</u>
Net Position - End of Year	<u>\$ 17,287,989</u>	<u>\$ 17,566,519</u>	<u>\$ (278,530)</u>

OTSEGO COUNTY ROAD COMMISSION
MANAGEMENT'S DISCUSSION & ANALYSIS (CONTINUED)
DECEMBER 31, 2014

THE ROAD COMMISSION'S FUND

The road commission's general operations fund is used to control the expenditures of Michigan Transportation Fund monies distributed to the county which are earmarked by law for road and highway purposes.

For the year ended December 31, 2014, the fund balance of the general operations fund decreased by \$124,607 as compared to an increase of \$62,346 in the fund balance for the year ended December 31, 2013. Total revenues were \$7,555,342 compared to \$10,230,184 in 2013. This is primarily due to decreases in federal grants and local funding.

Total expenditures were \$7,679,949, a decrease of \$2,487,889 as compared to last year. This change in expenditures is primarily due to decreases in Primary and Local Road Heavy Maintenance.

A summary of changes in the Operating Funds is as follows:

Revenues	<u>12/31/2014</u>	<u>12/31/2013</u>	<u>Increase/ Decrease</u>
Licenses and Permits	\$ 43,014	\$ 55,987	\$ (12,973)
Federal	1,259,327	2,558,429	(1,299,102)
State	4,187,721	4,365,281	(177,560)
Local	706,974	1,354,988	(648,014)
Charges for Services	1,176,025	1,402,021	(225,996)
Interest and Rents	3,302	2,221	1,081
Other	178,979	491,257	(312,278)
Total Revenues	<u>7,555,342</u>	<u>10,230,184</u>	<u>(2,674,842)</u>
Expenditures			
Public Works	7,622,945	9,791,577	(2,168,632)
Net Capital Outlay	(168,982)	310,023	(479,005)
Debt Service	225,986	66,238	159,748
Total Expenditures	<u>7,679,949</u>	<u>10,167,838</u>	<u>(2,487,889)</u>
Excess of Revenues Over (Under)	(124,607)	62,346	(186,953)
Expenditures			
Fund Balance - January 1	<u>1,543,154</u>	<u>1,480,808</u>	<u>62,346</u>
Fund Balance - December 31	<u>\$ 1,418,547</u>	<u>\$ 1,543,154</u>	<u>\$ (124,607)</u>

BUDGETARY HIGHLIGHTS

Prior to the beginning of any year, the road commission's budget is compiled based upon certain assumptions and facts available at that time. During the year, the road commission board acts to amend its budget to reflect changes in these original assumptions, facts and/or economic conditions that were unknown at the time the original budget was compiled. In addition, by policy, the board reviews and authorizes large expenditures when requested throughout the year. The revenue budget for 2014 was higher than the actual receipts by \$22,769. The net difference is primarily from unexpected reductions in MTF Allocations and local funding offset by state local agency payments which were not budgeted.

Road Commission expenditures were projected as \$7,578,111 while actual expenditures were \$7,679,949. This resulted in total expenditures being over budget by \$101,838. The net variance is 1.33% of the total expenditures.

OTSEGO COUNTY ROAD COMMISSION
MANAGEMENT'S DISCUSSION & ANALYSIS (CONTINUED)
DECEMBER 31, 2014

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital Assets

As of December 31, 2014, the road commission had \$24,996,205 invested in capital assets as follows:

	<u>12/31/2014</u>	<u>12/31/2013</u>	<u>Increase/ Decrease</u>
Capital Assets Not Being Depreciated:			
Land and Improvements	\$ 170,157	\$ 170,157	\$ -
Subtotal	<u>170,157</u>	<u>170,157</u>	<u>-</u>
Capital Assets Being Depreciated:			
Buildings	3,934,836	3,934,836	-
Road Equipment	6,049,367	5,841,862	207,505
Shop Equipment	101,193	97,786	3,407
Office Equipment	49,215	43,001	6,214
Engineers Equipment	13,562	16,975	(3,413)
Yard & Storage Equipment	1,800	1,800	-
Depletable Assets	4,760	4,760	-
Traffic Signals	44,756	44,756	-
Infrastructure - Bridges	1,780,315	1,780,315	-
Infrastructure - Roads	47,889,501	45,128,596	2,760,905
Subtotal	<u>59,869,305</u>	<u>56,894,687</u>	<u>2,974,618</u>
Total Capital Assets	<u>60,039,462</u>	<u>57,064,844</u>	<u>2,974,618</u>
Total Accumulated Depreciation	<u>35,043,257</u>	<u>32,448,184</u>	<u>2,595,073</u>
Total Net Capital Assets	<u>\$ 24,996,205</u>	<u>\$ 24,616,660</u>	<u>\$ 379,545</u>

Debt Related to capital assets - bonds and installment agreements	<u>\$ 1,103,915</u>
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Debt

At the year end, the road commission had \$795,000 and \$308,915 in bonds outstanding and installment purchase agreements, respectively. This represents a decrease of \$181,727 from 2013. The bonds are payable over 20 years with the final payment due June 1, 2031. The installment purchase agreements are payable over 3 years with the final payments due July 15, 2016. Other long-term debt accrued is the compensated absences.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET

With the recent rejection of Proposal 1, road agencies across the state will continue to pursue an additional source of road funding. With this issue unresolved, road commissions will be conservative moving forward and creative with their investments of limited funds. After a twenty two year period (1992), our office took the initiative to pursue a county wide millage of one mil over a ten year period. The millage campaign was successful and we look forward to investing 100% of all millage monies collected (approximately \$1,140,000 annually), towards our primary and local road system. This millage will allow us to upgrade several road locations that we would not have been able to invest into for quite some time. Unfortunately, this millage does not help fund the road commission's daily operations so we plan to move forward in our decision making with the above two issues in mind.

OTSEGO COUNTY ROAD COMMISSION
MANAGEMENT'S DISCUSSION & ANALYSIS (CONTINUED)
DECEMBER 31, 2014

With the use of federal transportation dollars and five local match partners, we were able to complete the upgrade to Milbocker Road and McCoy Road in 2014. This now provides the community an alternate truck route built to all season standards. In addition, this project will be of great benefit to the proposed Gaylord downtown street scape project if approved by the voters in August.

The final leg of Hayes Tower Road was also completed in 2014 with financial support from Hayes Township officials. This completes an all season upgrade to the entire nine mile length of Hayes Tower Road that began in 2004. Federal transportation dollars were also utilized to upgrade Old 27 South from Old State Road to the Village of Waters. Otsego Lake Township officials paid for sixty-five percent of our local match costs.

The cost for our forces to place a single application of chip seal and fog seal per mile is approximately \$20,000. For a third year in a row, Otsego Lake Township officials partnered with us for fifty percent of this cost including for the first time, the preparation costs with hot mix asphalt. We chip/fog sealed just over eleven miles of road and we anticipate this number to continue to be reduced as we become more conservative in our approach without positive news out of Lansing.

As our annual miles of chip sealing continue to decline, we have been successful with our partnering townships to overlay several local roads with hot mix asphalt. We feel it is a very good investment of our maintenance dollars, as this upgrade can extend the life of a road well beyond a chip seal application. We also continued our crack sealing program with an emphasis on protecting our investment into federally funded projects that have been completed in the last fifteen years.

Our sign department continues to be very proactive in replacing and upgrading traffic control signs to meet federal retro reflectivity standards. Cost savings are achieved when we strip and overlay existing signs that we have in stock and reapply with material that meets federal standards.

In regards to our capital outlay investment, we purchased a used Gradall unit to improve our ditching capabilities. We also purchased a new reclaimer in 2014 to restore existing shoulder material and to reduce the burden on our Turtle Lake pit gravel pile. A used boom truck was purchased to replace an outdated unit along with a used tractor/flail mower set-up. Other investments that will directly improve our daily efficiency include the purchase of a innovative hot patch truck insert unit and two new wing plows. By continuing to expand on our wing plow inventory, our drivers are able to reduce the time it takes to cover their beats in the winter. This is a direct savings on our winter maintenance costs and a safety benefit to motorists. We are continuing to upgrade our fleet of pick up trucks with the purchase of a new crew cab truck. The above investments have allowed our shop department to sell older equipment and trucks that have been replaced.

As operating costs continue to rise, it is imperative that we continue to review our own internal operations and investment strategies. Our strong working relationship with our townships, city and county officials has been vital in our pursuit to reverse the decline in the condition of our road system. Without a statewide road funding solution, we foresee the need to reduce our financial commitment to our local partners further limitations on our annual road maintenance program.

OTSEGO COUNTY ROAD COMMISSION
MANAGEMENT'S DISCUSSION & ANALYSIS (CONTINUED)
DECEMBER 31, 2014

CONTACTING THE ROAD COMMISSION'S FINANCIAL MANAGEMENT

This financial report is designed to provide the motoring public, citizens and other interested parties a general overview of the road commission's finances and to show the road commission's accountability for the money it receives. If you have any questions about this report or need additional financial information, contact the Otsego County Road Commission Administrative Offices at 669 W. McCoy Road, P.O. Box 537, Gaylord MI 49734-0537.

Tom Deans
Engineer Manager
Otsego County Road Commission

OTSEGO COUNTY ROAD COMMISSION
STATEMENT OF NET POSITION
DECEMBER 31, 2014

Assets	
Cash and Equivalents	\$ 417,353
Investments	51,156
Accounts receivable:	
Property taxes	1,141,288
Sundry	4,390
Due from other governmental units	977,755
Inventories	655,931
Capital Assets (Net of Accumulated Depreciation)	<u>24,996,205</u>
Total Assets	<u><u>\$ 28,244,078</u></u>
Liabilities	
Current Liabilities	
Accounts payable	\$ 11,594
Accrued liabilities	61,353
Due to other governmental units	6,443
Escrow	20,000
Advances from governmental units	263,337
Bond and installment agreements (Due within One Year)	188,534
Non Current Liabilities	
Installment Purchase Agreements	155,381
Bonds Payable	760,000
Vested Employee Benefits Payable	124,319
Post Employment Benefit Liabilities	<u>8,138,731</u>
Total Liabilities	<u>9,729,692</u>
Deferred Inflows of Resources	
Taxes levied for subsequent period	1,141,288
Other state grants	<u>85,109</u>
Total Deferred Inflows of Resources	<u>1,226,397</u>
Net Position	
Net Investment in Capital Assets	24,047,671
Restricted for County Roads	<u>(6,759,682)</u>
Total Net Position	<u><u>\$ 17,287,989</u></u>

See accompanying notes to the financial statements.

OTSEGO COUNTY ROAD COMMISSION
STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2014

Program Expenses

Primary Road Maintenance	\$ 1,390,174
Local Road Maintenance	1,617,090
State Trunkline Maintenance	1,025,521
Net Equipment Expense	431,735
Net Administrative Expense	400,320
Infrastructure Depreciation	2,209,578
Compensated Absences	48,476
Post Employment Benefits	906,921
Interest Expense	44,259
	8,074,074
Total Program Expenses	8,074,074

Program Revenue

Charges for Services	
Licenses and Permits	43,014
Charges for Services	1,176,025
Operating Grants and Contributions	
Michigan Transportation Funds	4,349,040
Interest Earnings	3,302
Contributions from Local Units	706,974
Capital Grants and Contributions	
Federal Grants	1,259,327
State Grants	78,883
	7,616,565
Total Program Revenues	7,616,565

Net Program Revenues (Expenses)	(457,509)
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General Revenues

Gain (Loss) on Disposal of Assets	23,470
Other	155,509
	178,979
Total General Revenues	178,979

Change in Net Position	(278,530)
Net Position - Beginning Balance	17,566,519
Net Position - Ending Balance	\$ 17,287,989

See accompanying notes to the financial statements.

OTSEGO COUNTY ROAD COMMISSION
BALANCE SHEET
DECEMBER 31, 2014

	Governmental Fund Type
	General Operating
Assets	
Imprest cash	\$ 200
Cash demand and time deposits	417,153
Investments	51,156
Accounts receivable:	
Property taxes	1,141,288
Sundry	4,390
Due from other governmental units	977,755
Inventories	655,931
	\$ 3,247,873
	\$ 3,247,873
Liabilities	
Accounts payable	\$ 11,594
Accrued liabilities	61,353
Due to other governmental units	6,443
Escrow	20,000
Advances from governmental units	263,337
	362,727
	362,727
Deferred Inflows of Resources	
Taxes levied for subsequent period	1,141,288
Other state grants	325,311
	1,466,599
	1,466,599
Fund Balances	
Non-Spendable	655,931
Unassigned	762,616
	1,418,547
	1,418,547
Total Liabilities, Deferred Inflows of Resources and Fund Balances	\$ 3,247,873
	\$ 3,247,873

See accompanying notes to the financial statements.

OTSEGO COUNTY ROAD COMMISSION
RECONCILIATION OF THE BALANCE SHEET FUND BALANCE TO
THE STATEMENT OF NET POSITION
FOR THE YEAR ENDED DECEMBER 31, 2014

Total governmental fund balance	\$ 1,418,547
Amounts reported for governmental activities in the statement of net position are different because:	
Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds.	24,996,204
Other long-term assets are not available to pay for current period expenditures and therefore are not reported in the funds.	(9,366,965)
Receivables from the State of Michigan treated as a deferred inflow on the Balance Sheet are treated as current year revenues on the State- ment of Net Position.	<u>240,202</u>
Net position of governmental activities	<u>\$ 17,287,989</u>

See accompanying notes to the financial statements.

OTSEGO COUNTY ROAD COMMISSION
STATEMENT OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCE
DECEMBER 31, 2014

	Governmental Fund Type
	General Operating
Revenues	
Licenses and Permits	\$ 43,014
Federal Sources	1,259,327
State Sources	4,187,721
Contributions from Local Units	706,974
Charges for Services	1,176,025
Interest and Rents	3,302
Other	178,979
	7,555,342
Expenditures	
Public Works	7,622,945
Net Capital Outlay	(168,982)
Debt Service	225,986
	7,679,949
Excess of Revenues Over (Under) Expenditures	(124,607)
Fund Balance - Beginning of Year	1,543,154
Fund Balance - End of Year	\$ 1,418,547

See accompanying notes to the financial statements.

OTSEGO COUNTY ROAD COMMISSION
RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCE OF GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2014

Net Change in fund balance - total governmental funds	\$ (124,607)
Amounts reported for governmental activities in the statement are different because:	
Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives as depreciation expense. This is the amount by which capital outlays exceeded depreciation in the current period. Equipment retirement is recorded as an expenditure credit in governmental funds, but not recorded as an expense in the statement of activities.	379,545
Bond proceeds provide current financial resources to governmental funds, but entering into bond/lease purchase agreements increases long-term liabilities in the statement of net position. Repayment of notes/leases payable is an expenditure in governmental funds, but reduces the long-term liabilities in the statement of net position.	181,727
Some revenues in the Statement of Activities are not considered available resources in the Statement of revenues, expenditures and changes in fund balance.	240,202
Some expenses reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds. (Increase in compensated absences, post employment benefits and decrease in interest expense).	<u>(955,397)</u>
Change in net position of governmental activities.	<u>\$ (278,530)</u>

See accompanying notes to the financial statements.

OTSEGO COUNTY ROAD COMMISSION
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2014

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies of the Otsego County Road Commission conform to generally accepted accounting principles as applicable to governmental units. The following is a summary of the significant policies.

DESCRIPTION OF ROAD COMMISSION OPERATIONS - The Otsego County Road Fund, referred to as the Road Commission, is a Component Unit of the County of Otsego, Michigan, and is used to control the expenditure of revenues from the State distribution of gas and weight taxes, federal financial assistance, reimbursements from the Department of State Highways for work performed by the County on State trunkline and contributions from other local units of government for work performed by the Road Commission work force.

The Road Commission which is established pursuant to the County Road Law (MCL224.1) operates under an elected Board of three (3) County Road Commissioners who establish policies and review operations of the Road Commission. A different Road Commissioner is elected biannually to serve a six year term.

FINANCIAL REPORTING ENTITY - The Road Commission is required by Public Act 51 of the State of Michigan to have a separate audit performed of its operations. This financial report has been prepared to meet this State requirement.

The criteria established by the Governmental Accounting Standards Board (GASB) Statement No. 14 "The Financial Reporting Entity" for determining the reporting entity includes oversight responsibility, fiscal dependency and whether the financial statements would be misleading if the component unit data were not included. Based on the above criteria, these financial statements present the Otsego County Road Commission, a discretely presented component unit of Otsego County, and include the basic financial statements of the Road Commission

BASIS OF PRESENTATION – GOVERNMENT-WIDE FINANCIAL STATEMENTS

The government-wide financial statements (i.e., the Statement of Net Position and the Statement of Changes in Net Position) report information on all the Otsego County Road Commission. There is only one fund reported in the government-wide financial statements.

The Statement of Net Position presents the Road Commission's assets and liabilities with the difference being reported as either invested in capital assets, net of related debt or restricted net position.

The Statement of Activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function or segment. Program revenues include: (1) charges to customers or applicants who purchase, use or directly benefit from goods, services or privileges provided by a given function or segment; and (2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Taxes and other items not properly included among program revenues are reported instead as general revenue.

OTSEGO COUNTY ROAD COMMISSION
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2014

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

BASIS OF PRESENTATION – FUND FINANCIAL STATEMENTS

Separate financial statements are provided for the operating fund (governmental fund). The operating fund is an independent fiscal and accounting entity with a self-balancing set of accounts. Fund accounting segregates funds according to their intended purpose and is used to aid management in demonstrating compliance with finance-related legal and contractual provisions.

MEASUREMENT FOCUS/BASIS OF ACCOUNTING – GOVERNMENT-WIDE FINANCIAL STATEMENTS

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenue is recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenue in the year which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Amounts reported as program revenue include: charges to customer or applicants for goods or services or privileges provided; Michigan transportation funds; and State/Federal contracts and township contributions. Internally dedicated resources are reported as general revenue rather than as program revenue. Likewise, general revenue includes all taxes.

MEASUREMENT FOCUS/BASIS OF ACCOUNTING – FUND FINANCIAL STATEMENTS

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenue is recognized as soon as it is both measurable and available. Revenue is considered to be available if it is collected within the current period or soon enough thereafter to pay liabilities for the current period. For this purpose, the government considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

Michigan transportation funds, grants, permits, township contributions and interest associated with current fiscal period are all considered to be susceptible to accrual and have been recognized as revenue of the current fiscal period. All other revenue items are considered to be available only when cash is received by the government.

OTSEGO COUNTY ROAD COMMISSION
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2014

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

BUDGETS AND BUDGETARY ACCOUNTING

The County Road Commission follows the requirements of the Uniform Budgeting and Accounting Act, Michigan Public Act 621 of 1978, in the preparation and execution of its annual general appropriations act. Any violations are disclosed in audits of the County Road Commission financial statements as required by law.

CASH, CASH EQUIVALENTS AND INVESTMENTS

Cash and cash equivalents are considered to be cash on hand, demand deposits and short-term investments with a maturity of three months or less when acquired. Investments are stated at fair value.

INVENTORY

Inventories consisting of equipment parts and supplies of \$161,468 and road materials of \$494,463, are recognized using the consumption method (inventories are recorded as expenditures when they are used). Inventories are recorded at average cost which approximates market.

CAPITAL ASSETS

Capital assets, which include property, plant, equipment, infrastructure assets (e.g., roads, bridges and similar items), are reported in the operating fund in the government-wide financial statements. Capital assets are defined by Otsego County Road Commission as assets with an initial individual cost of more than \$1,000 and an estimated useful life in excess of two years. Such assets are recorded at historical cost or estimated historical cost purchase or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation.

GASB 34 requires major networks and major subsystems of infrastructure assets acquired, donated, constructed, or substantially rehabilitated since fiscal years ending after June 30, 1980 be inventoried and capitalized by the fourth anniversary of the mandated date of adoption of the other provisions of GASB 34. The Otsego County Road Commission has capitalized the current year's infrastructure, as required by GASB 34, and has reported the infrastructure in the statement of net position.

PROPERTY TAXES RECEIVABLE

The property tax is levied each December 1st on the taxable valuation of property located in the County as of the preceding December 31st. The 2014 taxable valuation for the Otsego County Road Commission amounted to \$1,141,288,013 net of amounts for incorporated cities and villages (distributed based on SEV by statute), on which ad valorem taxes of 1.0 mills were levied for the Road Commission for road construction purposes.

2014 was the first year of a 10 year approved millage. It is the road commission's intent to budget and report the revenue in the year subsequent to the levy. Therefore, the 2014 levy is included is the deferred inflows of resources in the government wide financial statements.

OTSEGO COUNTY ROAD COMMISSION
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2014

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

ADVANCES FROM THE STATE OF MICHIGAN

The State of Michigan advances funds on a State maintenance agreement it has with the Otsego County Road Commission for specified maintenance which the Road Commission will perform during the year and for equipment purchases. These advances are considered current liabilities because they are subject to repayment annually upon audit by the State of Michigan.

ACCRUED VACATION AND SICK - In accordance with contracts negotiated with the various employee groups of the Road Commission, employees have a vested right upon termination to receive compensation for accumulated sick and vacation leave under formulas and conditions specified in the contracts.

EQUIPMENT RENTALS - The Michigan Department of Transportation requires that the cost of operating equipment, including depreciation, be allocated to the various activities. The effect of this allocation is deducted from equipment expenditures for the Statement of Revenues, Expenditures, and Changes in Fund Balance.

DEPRECIATION - Depreciation is computed on the sum-of-the-years-digits method for road equipment and straight-line method for all other capital assets. The depreciation rates are designed to amortize the cost of the assets over their estimated useful lives as follows:

Building	30 to 50 years
Road Equipment	5 to 8 years
Shop Equipment	10 years
Engineering Equipment	4 to 10 years
Office Equipment	4 to 10 years
Infrastructure-Roads	8 to 30 years
Infrastructure-Bridges	12 to 50 years

LONG-TERM OBLIGATIONS - In the government-wide financial statements, long-term debt and other long term obligations are reported as liabilities in operating fund statement of net position.

ESTIMATES - The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

DEFERRED OUTFLOWS OF RESOURCES - In addition to assets, the statement of net position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, deferred outflows of resources, represents a consumption of net position that applies to a future period(s) and so will not be recognized as an outflow of resources (expense/expenditure) until then. The Road Commission has no items that qualify for reporting in this category.

DEFERRED INFLOWS OF RESOURCES - In addition to liabilities, the statement of net position and governmental funds balance sheet will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, deferred inflows of resources, represents an acquisition of net position that applies to a future period(s) and so will not be recognized as an inflow of resources (revenue) until that time. The Road Commission has property taxes levied for a subsequent period and other state grants that qualify for reporting in this category.

OTSEGO COUNTY ROAD COMMISSION
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2014

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

FUND BALANCE - Fund balance is essentially the difference between the assets and liabilities reported in a governmental fund. There are five separate components of fund balance, each of which identifies the extent to which the Road Commission is bound to honor constraints on the specific purpose for which amounts can be spent.

1. Non-spendable fund balance (inherently non-spendable)
2. Restricted fund balance (externally enforceable limitations on use)
3. Committed fund balance (self-imposed limitations on use)
4. Assigned fund balance (limitation resulting from intended use)
5. Unassigned fund balance (the residual classification of the general fund)

As a general rule, when multiple categories of fund balance are available for expenditure, the Road Commission will start with the most restricted category and spend those funds first before moving down to the next category with available funds.

NOTE B - CASH AND INVESTMENTS

Michigan compiled Laws 129.91, authorizes the Road Commission to deposit and invest in the accounts of Federally insured banks, credit unions, savings and loan associations; bonds, securities and other direct obligations of the United States, or any agency or instrumentality of the United States; United States government or Federal agency obligation repurchase agreements, bankers' acceptance of United States banks; commercial paper rated within the two highest classifications, which mature not more than 270 days after the date of purchase, obligations of the State of Michigan or its political subdivisions which are rated as investment grade; and mutual funds composed of investment vehicles which are legal for direct investment by local units of government in Michigan. Financial institutions eligible for deposit of public funds must maintain an office in Michigan.

The investment policy adopted by the board in accordance with Public Act 20 of 1943, as amended, has authorized investment in the instruments described in the preceding paragraph. The Road Commission's deposits and investment policy are in accordance with statutory authority.

At year end, the Road Commission's deposits and investments were reported in the basic financial statements in the following categories:

Imprest Cash	\$ 200
Cash Demand and Time Deposits	35,000
County Pooled Cash and investments	<u>433,309</u>
Total	<u>\$ 468,509</u>

OTSEGO COUNTY ROAD COMMISSION
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2014

NOTE B - CASH AND INVESTMENTS (CONTINUED)

Deposits

At year-end the carrying amount of the County Road Commissions deposits were \$35,000 and the bank balance was \$174,062. According to the Federal Deposit Insurance Corporation, approximately 100% of the total bank balance was covered by federal depository insurance. The County Treasurer maintains a pooled cash and investment account for the County which includes \$433,309 of road commission funds. The amount of FDIC insurance for these funds is unknown.

Investments Authorized by the Road Commission's Investment Policy

The Road Commission's investment policy only authorizes investment in all those that are authorized by law. The Road Commission has limited their investments to municipal money markets.

Disclosures Relating to Interest Rate Risk

Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. One of the ways that the Road Commission manages its exposure to interest rate risk is by participating in mutual funds which hold diverse investments that are authorized by law for direct investment.

Concentration of Credit Risk

Generally, credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. The investment policy of the Road Commission contains no limitations on the amounts that can be invested in any one issuer beyond that stipulated by Michigan law.

Custodial Credit Risk

Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover its deposits or will not be able to recover collateral securities that are in the possession of an outside party. Michigan law and the Road Commission's investment policy do not contain legal or policy requirements that would limit the exposure to custodial credit risk for deposits.

The custodial credit risk for investments is the risk that, in the event of the failure of the counter party (e.g., broker-dealer) to a transaction, a government will not be able to recover the value of its investment or collateral securities that are in the possession of another party. Michigan law and the Road Commission's investment policy do not contain legal or policy requirements that would limit the exposure to custodial credit risk for investments. With respect to investments, custodial credit risk generally applies only to direct investments in marketable securities. Custodial credit risk does not apply to a local government's indirect investment in securities through the use of mutual funds or government investment pools.

OTSEGO COUNTY ROAD COMMISSION
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2014

NOTE C - CAPITAL ASSETS

The following is a summary of changes in the Capital Assets Account Group.

	<u>Balance 1/1/2014</u>	<u>Additions</u>	<u>Deletions</u>	<u>Balance 12/31/2014</u>
Capital Assets Not Being Depreciated:				
Land and Improvements	\$ 170,157	\$ -	\$ -	\$ 170,157
Subtotal	<u>170,157</u>	<u>-</u>	<u>-</u>	<u>170,157</u>
Capital Assets Being Depreciated:				
Buildings	3,934,836	-	-	3,934,836
Road Equipment	5,841,862	210,875	3,370	6,049,367
Shop Equipment	97,786	4,954	1,547	101,193
Office Equipment	43,001	6,214	-	49,215
Engineers Equipment	16,975	-	3,413	13,562
Yard & Storage Equipment	1,800	-	-	1,800
Depletable Assets	4,760	-	-	4,760
Traffic Signals	44,756	-	-	44,756
Infrastructure - Bridges	1,780,315	-	-	1,780,315
Infrastructure - Roads	<u>45,128,596</u>	<u>2,760,905</u>	<u>-</u>	<u>47,889,501</u>
Total	<u>56,894,687</u>	<u>2,982,948</u>	<u>8,330</u>	<u>59,869,305</u>
Less Accumulated Depreciation:				
Buildings	1,548,880	87,899	-	1,636,779
Road Equipment	5,087,471	295,249	-	5,382,720
Shop Equipment	91,262	2,416	1,547	92,131
Office Equipment	38,043	4,426	-	42,469
Engineers Equipment	15,268	465	3,413	12,320
Yard & Storage Equipment	1,800	-	-	1,800
Traffic Signals	35,013	2,984	-	37,997
Infrastructure - Bridges	624,076	70,946	-	695,022
Infrastructure - Roads	<u>25,006,371</u>	<u>2,135,648</u>	<u>-</u>	<u>27,142,019</u>
Total	<u>32,448,184</u>	<u>2,600,033</u>	<u>4,960</u>	<u>35,043,257</u>
Net Capital Assets Being Depreciated	<u>24,446,503</u>	<u>382,915</u>	<u>3,370</u>	<u>24,826,048</u>
Total Net Capital Assets	<u>\$ 24,616,660</u>	<u>\$ 382,915</u>	<u>\$ 3,370</u>	<u>\$ 24,996,205</u>

OTSEGO COUNTY ROAD COMMISSION
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2014

NOTE D - PENSION PLAN

DEFINED BENEFIT PENSION PLAN

Plan Description - The Otsego County Road Commission participates in a defined benefit retirement plan administered by the Municipal Employee's Retirement System (MERS). The plan covers substantially all full-time employees.

The Municipal Employees Retirement System of Michigan (MERS) is a multiple-employer statewide public employee retirement plan created by the State of Michigan to provide retirement, survivor and disability in the most efficient and effective manner possible. As such, MERS is a non-profit entity qualified under section 401 (a) of the Internal Revenue Code, which has the responsibility of administering the law in accordance with the expressed intent of the Legislature and bears a fiduciary obligation to the State of Michigan, the tax payers and the public employees who are its beneficiaries.

The passage of HB-5525/Act No. 220, with enactment on May 28, 1996, allowed the members of MERS to vote on and determine if MERS should become an independent public corporation. The vote resulted in approval to become independent of State control and MERS began to operate as an independent public corporation effective August 15, 1996. MERS issues a financial report, available to the public, that includes financial statements and required supplementary information for the system. A copy of the report may be obtained by writing to MERS at 1134 Municipal Way, Lansing, Michigan 48917.

All full-time Road Commission employees and Commissioners are eligible to participate in the system. Benefits vest after ten years of service. Employees who retire at or after age 60 with 10 years credited service are entitled to an annual retirement benefit, payable monthly for life in an amount equal to 2.0 percent of the member's five-year final average compensation. The system also provides death and disability benefits which are established by State Statute.

OTSEGO COUNTY ROAD COMMISSION
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2014

NOTE D - PENSION PLAN (CONTINUED)

Actuarial Accrued Liability - The actuarial accrued liability was determined as part of an actuarial valuation of the plan as of December 31, 2014. Significant actuarial assumptions used in determining the investment of present and future assets of 8.0%, (b) projected salary increase of 4.5% per year compounded annually, attributable to inflation, and on age, attributable to seniority/merit.

All entries are based on the actuarial methods and assumptions that were used in the December 31, 2014 actuarial valuation to determine the annual employer contribution amounts. The entry age normal actuarial method used to determine the entries at disclosure.

GASB 25 INFORMATION (as of 12/31/14)

Actuarial Accrued Liability:

Retirees and beneficiaries currently receiving benefits	\$ 6,643,460
Vested former member's	275,909
Active members	<u>3,770,552</u>
Total actuarial accrued liability	10,689,921
Net position available for benefits, at actuarial value (Market value is \$6,196,252)	<u>6,567,637</u>
Unfunded (over funded) actuarial accrued liability	<u>\$ 4,122,284</u>

For the calendar year 2016, the Annual Required Contribution (ARC) is \$379,116.

OTSEGO COUNTY ROAD COMMISSION
 NOTES TO FINANCIAL STATEMENTS (CONTINUED)
 DECEMBER 31, 2014

NOTE D - PENSION PLAN (CONTINUED)

Contributions Required and Contributions Made - MERS funding policy provides for periodic employer contributions at actuarially determined rates that, expressed as percentages of annual covered payroll, are designed to accumulate sufficient assets to pay benefits when due. The normal cost and amortization payment for the fiscal year ended December 31, 2014 were determined using the entry age normal actuarial funding method. Unfunded actuarial accrued liabilities, if any, were amortized as a level percent of payroll over a period of 26 years. The following table provides a schedule of contribution amounts and percentages for recent years.

ARC and Annual Pension Cost

Year Ended December 31	Annual Required Contribution	Additional Contributions	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation
2012	\$ 319,412	\$ 120,000	\$ 439,412	100%	\$ -0-
2013	316,457	120,000	436,457	100%	-0-
2014	366,158	120,000	486,151	100%	-0-

The Road Commission was required to contribute \$366,151 and elected to pay an additional \$120,000 for the year ended December 31, 2014. Payments were based on contribution calculations made by MERS.

Aggregate Accrued Liabilities - Comparative Schedule

Actuarial Valuation Date December 31	Actuarial Value of Assets	Actuarial Accrued Liability (AAL)	Unfunded AAL (UAAL)	Funded Ratio	Covered Payroll	UAAL as a % of Covered Payroll
2012	\$ 6,368,969	\$10,240,166	\$ 3,871,197	62%	\$ 1,369,588	283%
2013	6,446,234	10,612,828	4,166,594	61%	1,399,784	298%
2014	6,567,637	10,689,921	4,122,284	61%	1,409,673	292%

For actuarial valuation purposes, the actuarial value of assets is determined on the basis of a calculation method that assumes the fund earns the expected rate of return (8%), and includes an adjustment to reflect market value.

NOTE E - STATE EQUIPMENT PURCHASE ADVANCE

State equipment purchase advance is determined by a formula applied to the book value of equipment of the previous fiscal year. This amount is adjusted each fiscal year in accordance with the formula and would be refunded to the State Department of Transportation upon termination of the State Highway Maintenance Contract.

OTSEGO COUNTY ROAD COMMISSION
 NOTES TO FINANCIAL STATEMENTS (CONTINUED)
 DECEMBER 31, 2014

NOTE F - LONG TERM DEBT

The following is a summary of pertinent information concerning the County Road Commission's long-term debt.

	<u>Balance</u> <u>12/31/2013</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance</u> <u>12/31/2014</u>	<u>Due</u> <u>Within</u> <u>One Year</u>
General Obligation:					
Installment Purchase					
Agreements	\$ 460,642	\$ -0-	\$ 151,727	\$ 308,915	\$ 153,534
Bonds payable	825,000	-0-	30,000	795,000	35,000
Compensated absences	<u>75,843</u>	<u>(1) 48,476</u>	<u>-0-</u>	<u>124,319</u>	<u>-0-</u>
Totals	<u>\$ 1,361,485</u>	<u>\$ 48,476</u>	<u>\$ 181,727</u>	<u>\$ 1,228,234</u>	<u>\$ 188,534</u>

(1) The change in compensated absences is shown as a net reduction.

Installment Purchase Agreements

On July 15, 2013 the Otsego County Road Commission entered into an Installment Purchase Agreement with Grand Traverse Diesel Services Inc for the purchase of two 2014 Western Star 4700 SF Plow Trucks in the amount of \$251,908. The agreement requires three annual payments of \$87,690.78 starting July 15, 2014 with interest accruing at 2.20%.

On December 13, 2013, the road commission entered into a second installment purchase agreement with Truck and Trailer Specialists of Boyne Falls, Inc for the purchase of two 2013 Westernstar 4900 SB Plow Trucks in the amount of \$208,734. The Agreement requires three annual principal payments of \$69,578 starting July 15, 2014 plus interest paid annually at a rate of 2.20%.

Annual Debt Service Requirements:

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2015	\$ 153,534	\$ 6,796	\$ 160,330
2016	<u>155,381</u>	<u>3,418</u>	<u>158,799</u>
	<u>\$ 308,915</u>	<u>\$ 10,214</u>	<u>\$ 319,129</u>

Bonds Payable

The Otsego County Building Authority issued the 2011 Series Bonds on behalf of the Otsego Road Commission for the purpose of constructing a new salt storage facility. The bonds were issued in denominations of \$5,000 totaling \$885,000. The bonds mature annually starting June 1, 2012 and each June 1st thereafter with the final maturities on June 1, 2031. The interest notes on the bonds range from 3.25% to 5.0%.

Annual Debt Service Requirements:

<u>Year</u>	<u>Amount</u>
2015	\$ 69,163
2016	67,938
2017	66,712
2018	65,488
2019	69,175
2020	67,775
2021	66,325
2022	69,563
2023	67,538
2024-2031	<u>539,010</u>
Total Payments	1,148,687
Less Interest & Fees	<u>(353,687)</u>
Net Balance Due	<u>\$ 795,000</u>

OTSEGO COUNTY ROAD COMMISSION
 NOTES TO FINANCIAL STATEMENTS (CONTINUED)
 DECEMBER 31, 2014

NOTE F - LONG TERM DEBT (CONTINUED)

COMPENSATED ABSENCES - Substantially all employees of the Road Commission can accumulate vacation hours. The accumulated hours at December 31, 2014 at current wage rates amounted to \$124,319 and is reflected in the Long-Term Debt Group. Sick leave is not vested and accordingly is not accrued.

NOTE G - EXCESS EXPENDITURES OVER APPROPRIATIONS

Public Act 621 of 1978, section 18 (1), as amended, provides that a County Road Commission shall not incur expenditures in excess of amounts appropriated. As presented in the financial statements for the year ended December 31, 2014 the County Road Commission incurred expenditures in certain areas which were in excess of the amounts appropriated as follows:

<u>Function</u>	<u>Total Appropriations</u>	<u>Amount of Expenditures</u>	<u>Budget Variance</u>
Primary Road:			
Preservation - Structural Improvements	\$ 1,842,747	\$ 2,293,224	\$ (450,477)
Maintenance	\$ 1,294,800	\$ 1,390,174	\$ (95,374)
Local Road:			
Maintenance	\$ 1,381,320	\$ 1,617,090	\$ (235,770)
Equipment Expense - Net	\$ 273,165	\$ 428,935	\$ (155,770)

NOTE H - RISK MANAGEMENT

Otsego County Road Commission is a member of the Michigan County Road Commission Self-Insurance Pool established pursuant to the laws of the State of Michigan which authorize contracts between municipal corporations (inter-local agreements) to form group self-insurance pools, and to prescribe conditions to the performance of these contracts.

The Pool was established for the purpose of making a self-insurance pooling program available which includes, but is not limited to, general liability coverages, auto liability coverages, property insurance coverages, stop loss insurance protection, claims administration, and risk management and loss control services pursuant to Michigan Public Act 138 of 1982.

The Otsego Road Commission pays an annual premium to the Pool for property (buildings and contents) coverage, automobile and equipment liability, errors or omissions liability and bodily injury, property damage and personal injury liability. The agreement for the information of the Pool provides that the Pool will be self-sustaining through member premiums and will purchase both specific and aggregate stop-loss insurance to the limits determined necessary by the Pool Board.

The Road Commission is also self-insured for worker's compensation as a member of the County Road Association Self Insurance Fund.

At December 31, 2014, there were no claims which exceeded insurance coverage. The Road Commission had no significant reduction in insurance coverage from the previous years.

OTSEGO COUNTY ROAD COMMISSION
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2014

NOTE I - FEDERAL FINANCIAL ASSISTANCE

It is required by the Michigan Department of Transportation that Road Commissioners report total federal financial assistance for Highway Research, Planning and construction pertaining to their County. However, only the federal financial assistance applicable to negotiated account expenditures is required to be audited for compliance under the Single Audit Act through Road Commission procurement. The reason for this requirement is that the Road Commission is required to have accounting and administrative control over the force account portion while the balance is administered by the Michigan Department of Transportation.

During the year ended December 31, 2014, the Road Commission recorded \$1,259,327 of Department of Transportation Federal Highway grant money expended on public road improvement projects where work was performed by independent contractors or under non-negotiated contracts between the Road Commission and the Michigan Department of Transportation.

NOTE J - OTHER POST EMPLOYMENT HEALTH CARE BENEFITS

Otsego County Road Commission provides hospitalization and medical coverage for eligible retirees and their spouses through the road commission's group health insurance plan, which covers both active and retired members. The following are the Governmental Accounting Standards Board Statement #45 required disclosures which have been implemented prospectively by the road commission.

- . Employees hired prior to December 31, 2008, and retire with 20 years of employment and age 55 years, or greater, will receive health insurance comparable to that provided to the current employees until age 65 years and supplemental health insurance for the employee and spouse for their lifetimes.

The plan does not issue a separate stand-alone financial statement.

Funding Policy - The Road Commission's annual other post employment benefit (OPEB) cost is calculated based on the *annual required contribution of the employer* (ARC). The Road Commission has elected to calculate the ARC and related information using the alternative measurement method permitted by GASB Statement 45 for employers in plans with fewer than one hundred total plan members. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal costs each year and to amortize any unfunded actuarial liabilities over a period not to exceed thirty years. The Road Commission has no obligation to make contributions in advance of when the premiums are due for payment (i.e., may be financed on a "pay-as-you-go" basis). The only current contributions being made are to pay the actual current premiums of the retirees. That amount was less than the annual required contribution and is reflected in the schedule that follows. Administrative costs of the plan are paid for by the Road Commission.

OTSEGO COUNTY ROAD COMMISSION
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2014

NOTE J - OTHER POST EMPLOYMENT HEALTH CARE BENEFITS (CONTINUED)

Funding Progress - For the year ended December 31, 2014, the Road Commission has determined an estimated cost of providing post-employment benefits through the alternative measurement method of calculation as of December 31, 2014. The calculation computes an annual required contribution, which represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and to cover the amortization of any unfunded actuarial liabilities from the past, over a period not to exceed 30 years.

The Road Commission's computed contribution and actual funding is summarized as follows:

Annual required contribution/Annual OPEB cost (ARC)	\$ 932,139
Interest on beginning of year net OPEB obligation	<u>289,272</u>
Annual OPEB Costs	1,221,411
Amounts contributed:	
Payments of current premiums	<u>314,490</u>
Net OPEB obligation	906,921
OPEB obligation - Beginning of year	<u>7,231,810</u>
OPEB obligation - End of year	<u><u>\$ 8,138,731</u></u>

The annual OPEB costs, the percentage contributed to the plan, and the net OPEB obligation for the fiscal year ended December 31, 2012, 2013, and 2014, were as follows:

	<u>2012</u>	<u>2013</u>	<u>2014</u>
Annual OPEB costs	\$ 1,542,163	\$ 1,588,361	\$ 1,221,411
Actual Contribution	387,209	344,371	314,490
Percentage contributed	25.10 %	21.68 %	25.75 %
Net OPEB obligation	5,987,820	7,231,810	8,138,731

The funded status of the plan as of the most recent valuation date is as follows:

Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (b/a)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll (b-a)/c
12/31/2008	\$ -0-	\$ 13,237,628	\$ 13,237,628	0.0%	\$ 1,593,543	830%
12/31/2011	\$ -0-	\$ 13,009,780	\$ 13,009,780	0.0%	\$ 1,397,173	931%
12/31/2014	\$ -0-	\$ 9,281,304	\$ 9,281,304	0.0%	\$ 1,526,387	608%

The year ended December 31, 2008 was the first year that an actuarial valuation was done, so no information is available for years prior to that. Also, information related to funding progress with multi year trend information indicating whether the actuarial value of plan assets is increasing or decreasing over time relative to the AAL for benefits is not presented since there currently are no plan assets.

OTSEGO COUNTY ROAD COMMISSION
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2014

NOTE J - OTHER POST EMPLOYMENT HEALTH CARE BENEFITS (CONTINUED)

Actuarial Methods and Assumptions - Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations. The following simplifying assumptions were made:

Assumptions About Employees and Members: Based on historical average retirement age of the covered group, active plan members were assumed to retire at various ages between 55 and 65 or the first year thereafter in which the member would qualify for benefits. Marital status as of the calculation date was assumed to continue throughout retirement. Life expectancy was based on mortality tables published in the 1994 Group Annuity Mortality Table. The probability of remaining employed until the assumed retirement age and employees' expected future working lifetimes were developed using specific age-based turnover data.

Assumptions About Healthcare Costs: The 2014 health insurance premiums for retirees were used to calculate the present value of total benefits to be paid. The expected rate of increase in health insurance premiums were based on the 2013 version of the National Health Expenditures (NHE) released in 2014, Centers for Medicare & Medicaid Services, Office of the Actuary.

Other Assumptions and Methods: The inflation rate was assumed to be 4.0%. Based on the historical and expected returns of the Commission's investments, the investment rate of return was assumed to be 4%. The value of Plan assets was set at market value. A simplified version of the entry age actuarial cost method was used in the actuarial valuation. The UAAL is amortized over a thirty-year period as a level percent of projected payroll on an open basis. Payroll was assumed to grow over the long-term at the same rate as inflation.

OTSEGO COUNTY ROAD COMMISSION
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2014

NOTE K - FUND BALANCE CLASSIFICATIONS

The governmental fund financial statements present fund balances based on classifications that comprise a hierarchy that is based primarily on the extent to which Otsego County Road Commission is bound to honor constraints on the specific purposes for which amounts in the respective governmental funds can be spent. The classifications used in the governmental fund financial statements are as follows:

Non-spendable - assets that are not available in a spendable form such as inventory, prepaid expenditures, and long-term receivables not expected to be converted to cash in the near term. It also includes funds that are legally or contractually required to be maintained intact such as the corpus of a permanent fund or foundation.

Restricted - amounts that are required by external parties to be used for a specific purpose. Constraints are externally imposed by creditors, grantors, contributors or laws, regulations or enabling legislation.

Committed - amounts constrained on use imposed by formal action of the government's highest level of decision-making authority (i.e., Board, Council, etc.).

Assigned - amounts intended to be used for specific purposes. The governing body, the budget or finance committee or a delegated municipality official, determines this.

Unassigned - all other resources; the remaining fund balance after non-spendable, restrictions, commitments, and assignments. This class only occurs in the General Fund, except for cases of negative fund balances. Negative Fund Balances are always reported as unassigned, no matter which fund the deficit occurs in.

Fund Balance Classification Policies and Procedures

For committed fund balance, Otsego County Road Commission's highest level of decision-making authority is the County Road Board. The formal action that is required to be taken to establish, modify, or rescind a fund balance commitment is by vote and approval by the County Road Board.

For assigned fund balance, the Road Commission Manager is authorized to assign amounts to a specific purpose. Such assignments cannot exceed the available fund balance in any particular fund.

For the classification of fund balances, the Otsego County Road Commission considers restricted amounts to have been spent when expenditures are incurred for the purposes for which both restricted and unrestricted fund balance is available. Also for the classification of fund balances, the road commission considers committed, assigned, or unassigned amounts to have been spent when an expenditure is incurred for purposes for which amounts in any of those unrestricted fund balance classifications could be used.

REQUIRED SUPPLEMENTAL INFORMATION

OTSEGO COUNTY ROAD COMMISSION
STATEMENT OF REVENUES -
BUDGETARY COMPARISON SCHEDULE
TWELVE MONTHS ENDED DECEMBER 31, 2014

	<u>Original Budget</u>	<u>Final Amended Budget</u>	<u>Actual</u>	<u>Variance Favorable (Unfavorable)</u>
Licenses and Permits	\$ 52,956	\$ 26,785	\$ 43,014	\$ 16,229
Federal Sources				
Surface Transportation Program	1,323,555	1,123,555	910,545	(213,010)
High Priority	-	-	33,250	33,250
Other	-	-	315,532	315,532
State Sources				
Michigan Transportation Fund				
Engineering	10,000	10,000	10,000	-
Allocation	3,350,000	3,362,575	3,172,105	(190,470)
Urban	340,000	341,000	321,389	(19,611)
Snow Removal	-	-	224,115	224,115
Local Agency Payment	-	233,060	313,134	80,074
Economic Development Fund				
Forest Road	85,109	85,109	-	(85,109)
Urban F	-	80,075	78,883	(1,192)
Other	-	68,095	68,095	-
Contributions from Local Units				
Townships	816,000	821,061	706,974	(114,087)
Charges for Services				
State Trunkline Maintenance/ Non-Maintenance	1,100,000	1,215,041	1,176,025	(39,016)
Salvage Sales	-	-	9,388	9,388
Interest and Rents	2,500	3,605	3,302	(303)
Other Revenue				
Gain (loss) Sale of Equipment	-	-	23,470	23,470
Other	375,000	208,150	146,121	(62,029)
Total Revenue	<u>\$ 7,455,120</u>	<u>\$ 7,578,111</u>	<u>\$ 7,555,342</u>	<u>\$ (22,769)</u>

OTSEGO COUNTY ROAD COMMISSION
STATEMENT OF EXPENDITURES -
BUDGETARY COMPARISON SCHEDULE
TWELVE MONTHS ENDED DECEMBER 31, 2014

	<u>Original Budget</u>	<u>Final Amended Budget</u>	<u>Actual</u>	<u>Variance Favorable (Unfavorable)</u>
Primary Road				
Preservation - Structural Improvements	\$ 1,685,000	\$ 1,842,747	\$ 2,293,224	\$ (450,477)
Maintenance	1,223,256	1,294,800	1,390,174	(95,374)
Local Road				
Preservation - Structural Improvements	1,081,130	900,000	467,681	432,319
Maintenance	1,313,541	1,381,320	1,617,090	(235,770)
State Trunkline Maintenance/ Non-Maintenance	1,100,000	1,215,051	1,025,521	189,530
Administrative Expense - Net	533,222	533,222	400,320	132,902
Equipment Expense - Net	430,669	273,165	428,935	(155,770)
Capital Outlay - Net	(183,500)	(89,379)	(168,982)	79,603
Long-Term Debt Payments	180,000	181,727	181,727	-
Interest Expense	46,000	44,259	44,259	-
Contingency	45,802	1,199	-	1,199
Total Expenditures	<u>\$ 7,455,120</u>	<u>\$ 7,578,111</u>	<u>\$ 7,679,949</u>	<u>\$ (101,838)</u>

SUPPLEMENTAL SCHEDULES

OTSEGO COUNTY ROAD COMMISSION
ANALYSIS OF CHANGES OF FUND BALANCES
FOR THE YEAR ENDED DECEMBER 31, 2014

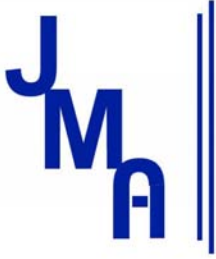
	<u>Primary Road Fund</u>	<u>Local Road Fund</u>	<u>County Road Fund</u>	<u>Totals</u>
Total Revenues	\$ 4,271,285	\$ 1,569,603	\$ 1,714,454	\$ 7,555,342
Total Expenditures	<u>4,057,548</u>	<u>2,414,813</u>	<u>1,207,588</u>	<u>7,679,949</u>
Excess of Revenues Over (Under) Expenditures	213,737	(845,210)	506,866	(124,607)
Optional Transfers and Adjustments	(213,737)	845,210	(631,473)	-
Fund Balance - January 1, 2014	-	-	1,543,154	1,543,154
Fund Balance - December 31, 2014	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 1,418,547</u>	<u>\$ 1,418,547</u>

OTSEGO COUNTY ROAD COMMISSION
ANALYSIS OF REVENUES
FOR THE YEAR ENDED DECEMBER 31, 2014

	<u>Primary Road Fund</u>	<u>Local Road Fund</u>	<u>County Road Fund</u>	<u>Totals</u>
Licenses and Permits	\$ -	\$ -	\$ 43,014	\$ 43,014
Federal Sources				
Surface Transportation Program	910,545	-	-	910,545
High Priority	33,250	-	-	33,250
Other	315,532	-	-	315,532
State Sources				
Michigan Transportation Fund				
Engineering	6,198	3,802	-	10,000
Allocation	1,965,966	1,206,139	-	3,172,105
Urban	219,762	101,627	-	321,389
Snow Removal	-	224,115	-	224,115
Local Agency Payment	-	-	313,134	313,134
Economic Development Fund				
Urban F	78,883	-	-	78,883
Other	68,095	-	-	68,095
Contributions from Local Units				
Townships	673,054	33,920	-	706,974
Charges for Services				
State Trunkline Maintenance/ Non-Maintenance	-	-	1,176,025	1,176,025
Salvage Sales	-	-	9,388	9,388
Interest and Rents	-	-	3,302	3,302
Other Revenue				
Gain (Loss) on sale of equipment	-	-	23,470	23,470
Other	-	-	146,121	146,121
Total Revenue	<u>\$ 4,271,285</u>	<u>\$ 1,569,603</u>	<u>\$ 1,714,454</u>	<u>\$ 7,555,342</u>

OTSEGO COUNTY ROAD COMMISSION
ANALYSIS OF EXPENDITURES
FOR THE YEAR ENDED DECEMBER 31, 2014

	<u>Primary Road Fund</u>	<u>Local Road Fund</u>	<u>County Road Fund</u>	<u>Totals</u>
Primary Road				
Preservation - Structural Improvements	\$ 2,293,224	\$ -	\$ -	\$ 2,293,224
Maintenance	1,390,174	-	-	1,390,174
Local Road				
Preservation - Structural Improvements	-	467,681	-	467,681
Maintenance	-	1,617,090	-	1,617,090
State Trunkline Maintenance/ Non-Maintenance	-	-	1,025,521	1,025,521
Administrative Expense - Net	255,633	144,687	-	400,320
Equipment Expense - Net	118,517	185,355	125,063	428,935
Capital Outlay - Net	-	-	(168,982)	(168,982)
Long-Term Debt Payments	-	-	181,727	181,727
Interest Expense	-	-	44,259	44,259
Total Expenditures	<u>\$ 4,057,548</u>	<u>\$ 2,414,813</u>	<u>\$ 1,207,588</u>	<u>\$ 7,679,949</u>



James M. Anderson, P.C.

CERTIFIED PUBLIC ACCOUNTANT

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INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

June 3, 2015

Board of County Road Commissioners
Otsego County Road Commission
Gaylord, MI 49734

I have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities, and major fund of the Otsego County Road Commission, a Special Revenue Fund of the County of Otsego, Michigan, as of and for the year ended December 31, 2014, and the related notes to the financial statements, which collectively comprise the Otsego County Road Commission's basic financial statements and have issued my report thereon dated June 3, 2015.

Internal Control over Financial Reporting

In planning and performing my audit of the financial statements, I considered the Otsego County Road Commission's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing my opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Otsego County Road Commission's internal control. Accordingly, I do not express an opinion on the effectiveness of the Otsego County Road Commission's internal control.

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 a 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. 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.

My consideration of internal control was for the limited purpose described in the first paragraph of this section 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. Given these limitations, during my audit I did not identify any deficiencies in internal control that I consider to be material weaknesses. However, material weaknesses may exist that have not been identified. I did identify certain deficiencies in internal control, described below that I consider to be significant deficiencies.

Financial Statement Preparation

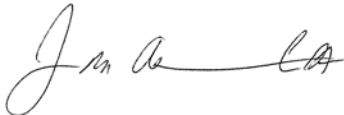
All Michigan governments are required to prepare financial statements in accordance with generally accepted accounting principals (GAAP). This is a responsibility of the Road Commission's management. The preparation of financial statements in accordance with GAAP requires internal controls over both (1) recording, processing, and summarizing accounting data (i.e., maintaining internal books and records), and (2) reporting government-wide and fund financial statements, including the related footnotes (i.e., external financial reporting). As is the case with most small and medium-sized entities, the Road Commission has historically relied on its independent external auditor to assist in the preparation of the government-wide financial statement and footnotes as part of its external financial reporting process. Accordingly, the Road Commission's ability to prepare financial statements in accordance with GAAP is based, in part, on its reliance on its external auditors, who cannot, by definition, be considered a part of the government's internal controls. This condition was caused by the Road Commission's determination that it is more cost effective to outsource the preparation of its annual financial statements to the auditors than to incur the time and expense of obtaining the necessary training and expertise required for the Road Commission to perform this task internally.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Otsego County Road Commission's financial statements are free from material misstatement, I 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 my audit, and accordingly, I do not express such an opinion. The results of my tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of my testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

A handwritten signature in cursive script, appearing to read "J M Anderson".

JAMES M. ANDERSON, P.C.
CERTIFIED PUBLIC ACCOUNTANT



James M. Anderson, P.C.

CERTIFIED PUBLIC ACCOUNTANT

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June 3, 2015

Board of County Road Commissioners
Otsego County Road Commission
Gaylord, MI 49734

I have audited the financial statements of the governmental activity and major fund of the Otsego County Road Commission for the year ended December 31, 2014, and have issued my report thereon dated June 3, 2015. Professional standards require that I provide you with the following information related to my audit.

My Responsibility Under U.S. Generally Accepted Auditing Standards and *Government Auditing Standards*

As stated in my engagement letter dated April 19, 2015, my responsibility, as described by professional standards, is to plan and perform my audit to obtain reasonable, but not absolute, assurance about whether the financial statements are free of material misstatement and are fairly presented in accordance with U.S. generally accepted accounting standards. Because an audit is designed to provide reasonable, but not absolute assurance and because I did not perform a detailed examination of all transactions, there is a risk that material misstatements may exist and not be detected by me.

As part of my audit, I considered the internal control of the Otsego County Road Commission. Such considerations were solely for the purpose of determining my audit procedures and not to provide any assurance concerning such internal control.

As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, I performed tests of the Otsego County Road Commission's compliance with certain provisions of laws, regulations, contracts, and grants. However, the objective of my tests was not to provide an opinion on compliance with such provisions.

Significant Accounting Policies

Management is responsible for the selection and use of appropriate accounting policies. In accordance with the terms of my engagement letter, I will advise management about the appropriateness of accounting policies and their application. The significant accounting policies used by the Otsego County Road Commission are described in Note A to the financial statements. No new accounting policies were adopted and the application of existing policies was not changed during the year. I noted no transactions entered into by the road commission during the year that were both significant and unusual, and of which, under professional standards, I am 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.

Audit Adjustments

For purposes of this letter, professional standards define an audit adjustment as a proposed correction of the financial statements that, in my judgment, may not have been detected except through my auditing procedures. An audit adjustment may or may not indicate matters that could have a significant effect on Otsego County Road Commission financial reporting process (that is, cause future financial statements to be materially misstated). In my judgment, none of the adjustments I proposed, whether recorded or unrecorded by the Otsego County Road Commission, either individually or in the aggregate, indicate matters that could have a significant effect on Otsego County Road Commission's financial reporting process.

Disagreements with Management

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

Consultations with Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. 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, my professional standards require the consulting accountant to check with me to determine that the consultant has all the relevant facts. To my knowledge, there were no such consultations with other accountants.

Issues Discussed Prior to Retention of Independent Auditors

I generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the Otsego County Road Commission's auditor. However, these discussions occurred in the normal course of my professional relationship and my responses were not a condition to my retention.

Difficulties Encountered in Performing the Audit

I encountered no significant difficulties in dealing with management in performing my audit.

COMMENTS AND RECOMMENDATIONS

The following is a summary of my observations and suggestions for improvements I believe should be brought to your attention.

Budgets

The Road Commission follows the procedures in establishing the budgetary data reflected in the financial statements in accordance with the Uniform Budgeting and Accounting Act (Act No. 621, Public Act of 1978) as prescribed by the State of Michigan.

Public Act 621 of 1978, section 18 (1), as amended, provides that County Road Commission shall not incur expenditures in excess of amounts appropriated. As presented in the financial statements for the year ended December 31, 2014, the County Road Commission incurred expenditures, which were in excess of the amount appropriated as follows:

<u>Function</u>	<u>Total Appropriations</u>	<u>Amount of Expenditures</u>	<u>Budget Variance</u>
Primary Road:			
Preservation - Structural Improvements	\$ 1,842,747	\$ 2,293,224	\$ (450,477)
Maintenance	\$ 1,294,800	\$ 1,390,174	\$ (95,374)
Local Road:			
Maintenance	\$ 1,381,320	\$ 1,617,090	\$ (235,770)
Equipment Expense - Net	\$ 273,165	\$ 428,935	\$ (155,770)

GASB #45 - Other Post Employment Benefits

The Road Commission offers health insurance for qualifying retirees after the age of 55. During the 2014 audit, the road commission calculated the potential present value of the future benefits. As of December 31, 2014, the accrued liability is \$9,281,304 and the Net OPEB Obligation is \$8,138,731. According to GASB #45, the OPEB obligation was accrued with a corresponding expense reducing the net position by the same which created a year end unrestricted deficit. I recommend the Board of Road Commissioners consider creating a Trust Account and funding method to build up a fund to be used for these future costs.

Parts Inventory

The road commission has had a practice of purchasing equipment parts for current repairs and future repairs and charging the entire amount to equipment rather than inventorying the excess. This results in an understated inventory on the balance sheet. I recommend that this practice be discontinued and the excess inventory be adjusted and included in the inventory status report and reconciled to the general ledger.

Conclusion

I would like to express my appreciation, as well as that of my staff, for the excellent cooperation received while performing the audit. If I can be of any assistance in implementing the above recommendations, please contact me.

This report is intended solely for the use of management, the Board of Commissioners and the Michigan Department of Treasury, and is not intended to be and should not be used by anyone other than these specified parties.

A handwritten signature in cursive script, appearing to read "James M. Anderson".

James M. Anderson, P.C.
Certified Public Accountant