Otsego County Road Commission

BASIC FINANCIAL STATEMENTS

December 31, 2017

OTSEGO COUNTY ROAD COMMISSION

BOARD OF COUNTY ROAD COMMISSIONERS

David Matelski
Chairman

William Holewinski Vice Chairman	Troy Huff Member
Jason Melancon Manager	Rebecca Jerry Board Secretary/ Finance Director

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CERTIFIED PUBLIC ACCOUNTANTS

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KENNETH A. TALSMA, CPA, PRINCIPAL
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MEMBER AICPA
DIVISION FOR CPA FIRMS
MEMBER MACPA
OFFICES IN
MICHIGAN & WISCONSIN

INDEPENDENT AUDITOR'S REPORT

Board of County Road Commissioners
Otsego County Road Commission
669 West McCoy Road
Gaylord, Michigan 49734

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities and major fund of the Otsego County Road Commission (a component unit of Otsego County, Michigan) as of and for the year ended December 31, 2017, and related notes to the financial statements, which collectively comprise the Road Commission's basic financial statements as listed in the table of contents.

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

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our 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 we 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, we 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 the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

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Opinions

In our 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, 2017, 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

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, schedule of funding progress, budgetary comparison schedules on pages 4 through 8, pages 31 through 33 and pages 34 through 35 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. We 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 inquires of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquires, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Otsego County Road Commission's basic financial statements. The schedules of analysis are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The schedules are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedules are fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Board of County Road Commissioners
Otsego County Road Commission

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our reports dated April 20, 2018 on our consideration of the Otsego County Road Commission's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of these reports is to describe the scope of our 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. These reports are an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Otsego County Road Commission's internal control over financial reporting and compliance.

Anderson Tackman & Co. PLC

Anderson, Tackman & Company, PLC
Certified Public Accountants
Kincheloe, Michigan

April 20, 2018

Management's Discussion and Analysis

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 Road Commission as a whole and about its activities in a way that helps answer the question of 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, deferred outflows of resources, liabilities and deferred inflows of resources) 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 11. The fund financial statements begin on page 36 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 fund 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.

The Road Commission as a Whole

The Road Commission's Net Position increased 11% from $20,298,452 to $22,439,552 for the year ended December 31, 2017. The Net Position and Change in Net Position are summarized below.

Unrestricted Net Position increased $863,992. The primary reasons were related to pension liabilities and infrastructure.

Net Position as of the years ended December 31, 2016 and 2017 follows:

	Governmental Activities	
	2016	2017
Current Assets	$ 5,102,498	$ 6,470,149
Capital Assets	32,468,986	33,848,512
Total Assets	37,571,484	40,318,661
Deferred Outflows of Resources	614,471	591,103
Current Liabilities	1,534,103	1,425,496
Noncurrent Liabilities	15,275,023	15,534,810
Total Liabilities	16,809,126	16,960,306
Deferred Inflows of Resources	1,078,377	1,509,906
Net Position		
Net Investment in Capital Assets	30,585,315	31,862,423
Unrestricted (Deficit)	(10,286,863)	(9,422,871)
Total Net Position	$ 20,298,452	$ 22,439,552

A summary of Changes in Net Position for the years ended December 31, 2016 and 2017 follows:

	Governmental Activities	
	2016	2017
Program Revenues		
Charges for Services	$ 2,472,303	$ 2,229,510
Grants and Contributions	5,773,657	6,879,844
Interest Earnings	17,918	43,455
General Revenues		
Gain (Loss) on Equipment Disposal	54,652	16,800
Taxes and Other	956,742	985,400
Total Revenues	9,275,272	10,155,009
Program Expenses		
Primary Roads	1,151,211	1,436,478
Local Roads	1,728,123	1,766,502
State Trunkline	1,591,925	1,635,201
Equipment Expense	193,831	107,433
Administrative	656,889	624,683
Depreciation	1,661,329	1,607,452
Interest Expense and Other	582,200	836,160
Total Expenses	7,565,508	8,013,909
Change in Net Position	1,709,764	2,141,100
Net Position – Beginning	18,588,688	20,298,452
Net Position – Ending	$ 20,298,452	$ 22,439,552

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, 2017, the fund balance of the general operations fund increased $1,642,869 as compared to an increase of $564,215 in the fund balance for the prior year. Total revenues were $10,409,106, an increase of $297,562 as compared to last year. This change in revenues resulted primarily from state sources.

Total expenditures were $8,766,237, a decrease of $781,092. The decrease is largely due to capital outlay.

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 2017 was $21,406 less than the actual receipts. This was due, in part, to the projection of note proceeds. The Road Commission budgets for the receipt of funds for projects on primary and local roads as earned.

Road Commission expenditures were projected at $10,190,180 while actual expenditures were $8,766,237. This resulted in total expenditures being under budget by $1,423,943. There were several items that account for the variance in the projection of the budget.

Capital Assets

As of December 31, 2016 and 2017, the Road Commission had invested in capital assets as follows:

	2016	2017
Capital Assets Not Being Depreciated		
Land and Improvements	$ 9,895,950	$ 10,889,984
Other Capital Assets		
Buildings	3,934,836	3,936,130
Road Equipment	6,643,471	7,093,391
Other Equipment and Assets	175,075	174,307
Infrastructure	34,645,182	33,503,417
Total Capital Assets at Historic Cost	55,294,514	55,597,229
Total Accumulated Depreciation	(22,825,528)	(21,748,717)
Total Net Capital Assets	$ 32,468,986	$ 33,848,512

Major additions included the following:

	2016	2017
Land Improvements	$ 632,722	$ 994,034
Various Resurfacing Projects and Bridges	$ 2,869,315	$ 2,052,184
Trucks/Equipment/Other	$ 887,723	$ 379,059

Debt

The Road Commission currently has long-term debt in the amount of $16,078,620 which represents bond payments, bank loans, equipment financing, net pension liabilities, health benefit obligations, and vested employee benefits.

Economic Factors and Next Year's Budget

The Board of County Road Commissioner's considered many factors when setting the fiscal year 2018 budget. One of the factors is the economy. The Road Commission derives approximately 60% of its revenues from the fuel tax collected. The economic changes have resulted in stable consumption of fuel and consequently stable Michigan Transportation Funds to be distributed. As an increase in funding occurs, road projects will be increased. Additionally, management may consider reducing labor costs through attrition and adjusting health care benefits.

The board realized, and the reader should understand, that there are not sufficient funds available to repair and/or rebuild every road in Otsego County's transportation system. Therefore, the board attempts to spend the public's money wisely and equitably and in the best interest of the motoring public and the citizens of the County.

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.

Basic Financial Statements

Statement of Net Position
December 31, 2017

ASSETS	
Cash and Equivalents	$ 3,625,432
Receivables:	
Taxes	1,063,476
Michigan Transportation Fund	773,691
State Trunkline Maintenance	308,417
Due on County Road Agreements	35,635
Sundry Accounts	2,763
Inventories:	
Road Materials	394,568
Equipment, Parts and Materials	266,167
Capital Assets (Not Depreciated)	10,889,984
Capital Assets (Net of Accumulated Depreciation)	22,958,528
Total Assets	40,318,661
DEFERRED OUTFLOWS OF RESOURCES	
Pension Investment Experience and Assumptions	591,103
LIABILITIES	
Accounts Payable	213,933
Due to State	131,490
Accrued Liabilities	115,630
Advances	412,175
Interest Payable	8,458
Notes Payable - Due within one year	508,810
Notes Payable - Due in more than one year	787,279
Bonds Payable - Due within one year	35,000
Bonds Payable - Due in more than one year	655,000
Vested Employee Benefits - Due in more than one year	299,759
Other Post Employment Benefits - Due in more than one year	8,718,698
Net Pension Liability - Due in more than one year	5,074,074
Total Liabilities	16,960,306
DEFERRED INFLOWS OF RESOURCES	
Pension Projected and Actual Earnings	446,430
Taxes Levied for Subsequent Period	1,063,476
Total Deferred Inflows of Resources	1,509,906
NET POSITION	
Net Investment in Capital Assets	31,862,423
Unrestricted (Deficit)	(9,422,871)
Total Net Position	$ 22,439,552

See accompanying notes to financial statements.

Statement of Activities
For the Year Ended December 31, 2017

Program Expenses:	
Primary Road Maintenance	
and Preventive Maintenance	$ 1,436,478
Local Road Maintenance	
and Preventive Maintenance	1,766,502
State Trunkline	1,635,201
Net Equipment Expense	107,433
Net Administrative Expense	624,683
Depreciation - Unallocated	1,607,452
Interest Expense	53,073
Other	783,087
Total Program Expenses	8,013,909
Program Revenues:	
Charges for Services:	
Licenses and Permits	55,948
Charges for Services	2,173,562
Operating Grants and Contributions:	
State Grants	3,833,626
Interest Earnings	43,455
Capital Grants and Contributions:	
Federal Grants	390,835
State Grants	1,526,584
Contributions from Local Units	1,128,799
Total Program Revenues	9,152,809
Net Program Revenues (Expenses)	1,138,900
General Revenues:	
Taxes - Real Property	985,400
Gain (Loss) on Equipment Disposal	16,800
Total General Revenues	1,002,200
Change in Net Position	2,141,100
Net Position - Beginning Balance	20,298,452
Net Position - Ending Balance	$ 22,439,552

Balance Sheet
December 31, 2017

	Governmental Fund Type
	General Operating Fund
ASSETS	
Cash and Equivalents	$ 3,625,432
Receivables:	
Taxes	1,063,476
Michigan Transportation Fund	773,691
State Trunkline Maintenance	308,417
Due on County Road Agreements	35,635
Sundry Accounts	2,763
Inventories:	
Road Materials	394,568
Equipment, Parts and Materials	266,167
Total Assets	$ 6,470,149
LIABILITIES	
Accounts Payable	$ 213,933
Due to State	131,490
Accrued Liabilities	115,630
Advances	412,175
Total Liabilities	873,228
DEFERRED INFLOWS OF RESOURCES	
Taxes Levied for Subsequent Period	1,063,476
FUND BALANCE	
Nonspendable	660,735
Unassigned	3,872,710
Total Fund Balance	$ 4,533,445

Reconciliation of the Balance Sheet Fund Balance to the Statement of Net Position For the Year Ended December 31, 2017

Total Governmental Fund Balance	$ 4,533,445
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.	33,848,512
Net pension liability requirement.	(5,074,074)
Other post employment benefits liability.	(8,718,698)
Deferred outflows/inflows resulting from pension experience, investments and assumptions.	144,673
Other liabilities are not available to pay in the current period and therefore are not reported in the funds.	(2,294,306)
Net Position of Governmental Activities	$ 22,439,552

See accompanying notes to financial statements.

Statement of Revenues, Expenditures, and Changes in Fund Balance
For the Year Ended December 31, 2017

	Governmental Fund Type — General Operating Fund
Revenues	
Property Taxes	$ 985,400
Licenses and Permits	55,948
Federal Sources	390,835
State Sources	5,360,210
Contributions form Local Units	1,128,799
Charges for Services	1,869,003
Interest Earnings and Rent	43,455
Other Revenue	70,315
Other Financing Sources	505,141
Total Revenues	10,409,106
Expenditures	
Public Works	8,616,515
Capital Outlay	(310,284)
Debt Service	460,006
Total Expenditures	8,766,237
Excess of Revenues Over (Under) Expenditures	1,642,869
Fund Balance - Beginning of Year	2,890,576
Fund Balance - End of Year	$ 4,533,445

Reconciliation of the Statement of Revenues, Expenditures and Changes in Fund Balance of Governmental Fund to the Statement of Activities
For the Year Ended December 31, 2017

Net Change in Fund Balance - Total Governmental Funds	$ 1,642,869
Amounts reported for governmental activities in the statements are different because:	
Governmental funds report capital outlays and infrastructure costs 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 outlay exceeded depreciation in the current period.	1,128,482
Repayment of notes/bonds payable is an expenditure in governmental funds, but reduces the long-term liabilities in the statement of net position. Note proceeds provide current financial resources to governmental funds, but entering into loan agreements increases long-term liabilities in the statement of net position.	(102,418)
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 the governmental funds.	(527,833)
Net Change in Net Position of Governmental Activities	$ 2,141,100

See accompanying notes to financial statements.

Notes to Financial Statements

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies of the Otsego County Road Commission conform to accounting principles generally accepted in the United States of America (GAAP) as applicable to governmental units. The following is a summary of the significant accounting policies used by the Otsego County Road Commission.

A. Reporting Entity

The Otsego County Road Commission, which is established pursuant to the County Road Law (MCL 224.1), operates under an elected board of three (3) County Road Commissioners who establish policies and review operations of the Road Commission. An alternating Road Commissioner is elected biannually to serve a six-year term.

The criteria established by the Governmental Accounting Standards Board 61, "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.

The Road Commission Operating Fund is used to control the expenditures of Michigan Transportation Fund moneys distributed to the County, which are earmarked by law for street and highway purposes. The Board of County Road Commissioners is responsible for the administration of the Road Commission Operating Fund.

B. Government-Wide and Fund Financial Statements

The government-wide financial statements (i.e., the statement of net position and the statement of activities) report information on all of the activities of 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, deferred outflows of resources, liabilities and deferred inflows of resources with the difference being reported as either invested in capital assets or restricted net position.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment is 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.

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. Major individual governmental funds are reported as separate columns in the fund financial statements. The operating fund is the only major fund of the Commission.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

C. Measurement Focus, Basis of Accounting and Financial Statement Presentation

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. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

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 of 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 the 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. Under the terms of grant agreements, the Commission funds certain programs by a combination of specific cost-reimbursement grants, categorical block grants, and general revenues. Thus, when program expenses are incurred, there is both restricted and unrestricted net position available to finance the program. It is the Commission's policy to first apply cost-reimbursement grant resources to such programs, followed by categorical block grants, and then by general revenues.

D. Assets, Liabilities, Deferred Outflows/Inflows of Resources and Net Position/Fund Balance

Cash, Equivalents and Investments

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

Inventories

Inventories are priced at cost as determined on the average unit cost method. Inventory items are charged to road construction and maintenance, equipment repairs and operations as used.

Prepaid Items

Certain payments to vendors reflect costs applicable to future fiscal years and are recorded as prepaid items in both the government-wide and fund financial statements.

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 2017 taxable valuation of $1,231,607,518 for Road Millage amounted to $1,231,608 less $168,132 for cities and villages, (on which ad valorem taxes of 1.0000 mills were levied) for road maintenance purposes resulted in a net total of $1,063,476.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

In the government-wide financial statements, the tax is recorded as revenue when the tax is levied in the current year. Although the County's 2017 ad valorem tax is levied and collectible December 1, 2017, it is the Road Commission's policy to recognize revenues from the current tax levy in the subsequent year. When the proceeds of this levy are budgeted and made available for the financing of the Road Commission's operations in the governmental fund financial statements. The tax receivable is offset to deferred inflows.

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 the Otsego County Road Commission as assets with an initial individual cost of more than $1,000 and/or an estimated useful life in excess of two years. Such assets are recorded at historical cost or estimated historical cost of purchase or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation.

Depreciation

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

Buildings	30 to 50 years
Road Equipment	5 to 8 years
Shop Equipment	10 years
Engineers' Equipment	3 to 10 years
Office Equipment	4 to 10 years
Infrastructure – Roads	8 to 30 years
Infrastructure – Bridges	12 to 50 years

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 pension 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 and pension items that qualify for reporting in this category.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Pensions

For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about the fiduciary net position of the Pension Plan and additions to/deductions from the fiduciary net position have been determined on the same basis as they are reported by MERS. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

Long-Term Obligations

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

Vested Employee Benefits (Vacation and Sick Leave)

Substantially all employees of the Road Commission can accumulate vacation hours based on years of service from 40 hours to 200 hours of paid time off. Sick leave is paid up to 600 hours upon retirement or upon death. Sick leave is earned at 8 hours per month for union employees. Vacation leave and sick leave amounted to $88,371 and $211,388 respectively.

Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets, outflows, liabilities and inflows, and affect the disclosure of contingent assets and liabilities at the date of the financial statements. These estimates and assumptions also affect the reported amounts of revenue and expenditures during the reporting period. Actual results could differ from those estimates.

Fund Balance Classification

The governmental fund financial statements present fund balances based on classifications that comprise a hierarchy that is based primarily on the extent to which the 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:

- Nonspendable: This classification includes amounts that cannot be spent because they are either (a) not in spendable form or (b) are legally or contractually required to be maintained intact. The Road Commission has classified inventories as being Nonspendable as these items are not expected to be converted to cash within the next year.

- Restricted: This classification includes amounts for which constraints have been placed on the use of the resources either (a) externally imposed by creditors (such as through a debt covenant), grantors, contributors, or laws or regulations of other governments, or (b) imposed by law through constitutional provisions or enabling legislation.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

- Committed: This classification includes amounts that can be used only for specific purposes pursuant to constraints imposed by formal action of the Board. These amounts cannot be used for any other purpose unless the Board removes or changes the specified use by taking the same type of action that was employed when the funds were initially committed. This classification also includes contractual obligations to the extent that existing resources have been specifically committed for use in satisfying those contractual requirements.

- Assigned: This classification includes amounts that are constrained by the Board's intent to be used for a specific purpose but are neither restricted nor committed. This intent can be expressed by the Board through the budgetary process. This classification also includes the remaining positive fund balance for all governmental funds except for the General Fund.

- Unassigned: This classification includes the residual fund balance for the General Fund. The unassigned classification also includes negative residual fund balance of any other governmental fund that cannot be eliminated by offsetting of Assigned fund balance amounts.

The Board would typically use Restricted fund balances first, followed by Committed resources, and then Assigned resources, as appropriate opportunities arise, but reserves the right to selectively spend Unassigned resources first to defer the use of these other classified funds.

NOTE 2 - STEWARDSHIP, COMPLIANCE, AND ACCOUNTABILITY

Budgetary Procedures

Budgetary procedures are established pursuant to PA 2 of 1968, as amended, which requires the County Board of Road Commissioners to approve a budget for the County Road Fund. The Manager prepares a budget in accordance with the Act which is adopted by the Board at a public hearing each December. All budgets lapse at fiscal year end. Any violations of the Act are indicated on page 35.

NOTE 3 - CASH AND EQUIVALENTS

Michigan Compiled Laws, Section 129.91, authorizes the Road Commission to deposit and invest in the accounts of federally insured banks, credit unions, and 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; banker's acceptance of United States banks; commercial paper rated within the two highest classifications, which mature not more than 270 days after the date purchased; 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.

NOTE 3 - CASH AND EQUIVALENTS (Continued)

The Road Commission has adopted an investment policy, which is in accordance with the provisions of Public Act 196 of 1997.

	Carrying Amount	Financial Institution Balance
Petty Cash	$ 200	
Bank Deposits (Checking and Savings Accounts)	1,737,782	$ 1,139,949
Investments at Fair Value	1,887,450	
Total Cash and Equivalents	$ 3,625,432	

Interest rate risk. The Road Commission does have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

Credit risk. State law limits investments in commercial paper, corporate bonds, and mutual bond funds to the top two ratings issued by nationally recognized statistical rating organizations. The Road Commission has an investment policy that could further limit its investment choices.

Custodial deposit credit risk. Custodial deposit credit risk is the risk that in the event of a bank failure, the Road Commission's deposits may not be returned. State law does not require and the Road Commission does not have a policy for deposit custodial credit risk. As of year end, $765,038 of the Road Commission's bank balance of $1,139,949 was exposed to credit risk because it was uninsured and uncollateralized.

Custodial investment credit risk. Investment custodial credit risk is the risk that in the event of the failure of the counterparty, the Commission will not be able to recover the value of its investments or securities that are in the possession of an outside party. The Commission invests with the County of Otsego and would receive its proportional share of holdings.

Fair value measurement. The Commission categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The hierarchy is based on the valuation inputs used to measure the fair value of the asset. Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; Level 3 inputs are significant unobservable inputs. Investments that are measured at fair value using the net asset value per share (or equivalent) as a practical expedient are not classified.

In instances where inputs used to measure fair value fall into different levels in the above fair value hierarchy, fair value measurements in their entirety are categorized based on the lowest level input that is significant to the valuation. The Commission's assessment of the significance of particular inputs to these fair value measurements required judgment and considers factors specific to each asset or liability. The Road Commission had the following investments as part of the Otsego County pool or separately owned:

Investment Type	Fair Value	Level 1	Level 2	Level 3	Credit Rating	Concen-tration
Fixed Income Debt Securities:						
U.S. Government	$ 982,868	$ -	$ 982,868	$ -	AA+	52%
Pubic Money Market	502,710	-	502,710	-	Unrated	27%
Other	401,872	-	401,872	-	Unrated	21%
Total	$ 1,887,450	$ -	$ 1,887,450	$ -		

NOTE 4 - CAPITAL ASSETS

Capital asset activity of the Otsego County Road Commission for the current year was as follows:

	Beginning Balances 01/01/17	Additions	Adjustments/ Deductions	Ending Balances 12/31/17
Capital Assets Not Being Depreciated				
Land	$ 125,501	$ -	$ -	$ 125,501
Land Improvements – Infrastructure	9,770,449	994,034	-	10,764,483
Subtotal	9,895,950	994,034	-	10,889,984
Capital Assets Being Depreciated				
Buildings	3,934,836	8,995	7,701	3,936,130
Road Equipment	6,643,471	370,064	(79,856)	7,093,391
Shop Equipment	108,683	-	-	108,683
Office Equipment	51,030	-	768	50,262
Engineers' Equipment	13,562	-	-	13,562
Yard and Storage Equipment	1,800	-	-	1,800
Traffic Signals	49,557	-	-	49,557
Infrastructure – Bridges	1,112,301	-	-	1,112,301
Infrastructure – Roads	33,483,324	2,052,184	3,193,949	32,341,559
Subtotal	45,398,564	2,431,243	3,122,562	44,707,245
Less Accumulated Depreciation				
Buildings	1,811,734	86,903	7,570	1,891,067
Road Equipment	5,358,274	594,591	171,319	5,781,546
Shop Equipment	99,000	3,618	-	102,618
Office Equipment	43,197	3,922	768	46,351
Engineers' Equipment	13,253	309	-	13,562
Yard and Storage Equipment	1,800	-	-	1,800
Traffic Signals	43,695	1,701	-	45,396
Infrastructure – Bridges	276,270	28,839	-	305,109
Infrastructure – Roads	15,178,305	1,576,912	3,193,949	13,561,268
Subtotal	22,825,528	2,296,795	3,373,606	21,748,717
Net Capital Assets Being Depreciated	22,573,036	134,448	251,044	22,958,528
Capital Assets - Net	$ 32,468,986	$ 1,128,482	$ 251,044	$ 33,848,512

Depreciation expense was charged to programs of the Otsego County Road Commission as follows:

Infrastructure - unallocated	$ 1,607,452
Equipment Expense	594,591
Administrative	8,330
Other Allocated	86,422
Total Depreciation Expense	$ 2,296,795

NOTE 5 - EMPLOYEE RETIREMENT AND BENEFITS SYSTEMS

Description of Plan and Plan Assets

The Road Commission is in an agent multiple-employer defined benefit pension plan with the Municipal Employees' Retirement System (MERS). The system provides the following provisions: normal retirement, deferred retirement and service retirement to plan members and their beneficiaries. The service requirement is computed using credited service at the time of termination of membership multiplies by the sum of 2.50% times the final compensation (FAC). The most recent period of which actuarial data was available was for year ended December 31, 2016.

General Information about the Pension Plan

Plan Description. The employer's defined benefit pension plan provides certain retirement, disability and death benefits to plan members and beneficiaries. The employer participates in the Municipal Employees Retirement System (MERS) of Michigan. MERS is an agent multiple-employer, statewide public employee pension plan established by the Michigan Legislature under Public Act 135 of 1945 and administered by a nine-member Retirement Board. MERS issues a publicly available financial report that includes financial statements and required supplementary information. This report may be obtained accessing the MERS website at www.mersofmich.com.

01 – General: Closed Division	
	2016 Valuation
Benefit Multiplier:	2.50% Multiplier (80% max)
Normal Retirement Age:	60
Vesting:	10 Years
Early Retirement (Unreduced):	55/25
Early Retirement (Reduced):	50/25 55/15
Final Average Compensation:	5 years
Employee Contributions:	1.5%
Act 88:	Yes (Adopted 11/23/1970)

02 – General: Open Division	
	2016 Valuation
Benefit Multiplier:	2.00% Multiplier (no max)
Normal Retirement Age:	60
Vesting:	10 Years
Early Retirement (Unreduced):	-
Early Retirement (Reduced):	50/25 55/15
Final Average Compensation:	5 years
Employee Contributions:	1.50%
Act 88:	Yes (Adopted 11/23/1970)

NOTE 5 - EMPLOYEE RETIREMENT AND BENEFIT SYSTEMS (Continued)

NonUnion: Open Division	
	2016 Valuation
Benefit Multiplier:	2.50% Multiplier (no max)
Normal Retirement Age:	60
Vesting:	10 Years
Early Retirement (Unreduced):	55/25
Early Retirement (Reduced):	50/25
	55/15
Final Average Compensation:	5 years
Employee Contributions:	1.50%
Act 88:	Yes (Adopted 11/23/1970)

Employees Covered by Benefit Terms

At December 31, 2016, the following employees were covered by the benefit terms:

Inactive employees or beneficiaries currently receiving benefits	49
Inactive employees entitled to but not yet receiving benefits	5
Active employees	33
	87

Funding Policy

The obligation to contribute to and maintain the system for these employees was established by negotiation with the Road Commission's competitive bargaining unit and personnel policy, which require employees to contribute to the plan. The Road Commission is required to contribute at an actuarially determined blended rate for 2017 of 35.9% of nonunion payroll and 4.18% of general employees.

Net Pension Liability

The Road Commission's net pension liability was measured as of December 31, 2016, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date.

Actuarial Assumptions. The total pension liability in the December 31, 2016 actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

Inflation	2.50 %
Salary increases	3.75 %
Investment rate of return	7.75 %, net of interest and administrative expense including inflation

Mortality rates used were based on the RP-2014 Mortality Table of a 50% Male and 50% Female blend.

The actuarial assumptions used in valuation were based on the results of the most recent actuarial experience study of January 1, 2009, through December 31, 2013.

NOTE 5 - EMPLOYEE RETIREMENT AND BENEFIT SYSTEMS (Continued)

The long-term expected rate of return on pension plan investments was determined using a model method in which the best-estimate ranges of expected future real rates of return (expected returns, net of investment and administrative expenses and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. The target allocation and best estimates of arithmetic real rates of return for each major asset class are summarized in the following table:

Asset Class	Target Allocation	Long-Term Expected Real Rate of Return
Global Equity	57.5%	5.02%
Global Fixed Income	20.0%	2.18%
Real Assets	12.5%	4.23%
Diversifying Strategies	10.0%	6.56%

Discount Rate. The discount rate used to measure the total pension liability is 8.00% for 2016 and thereafter. The projection of cash flows used to determine the discount rate assumes that employer and employee contributions well be made at the rates agreed upon for employees and the actuarially determined rates for employers. Based on these assumptions, the pension plan's fiduciary net position was projected to be available to pay all projected future benefit payments of current active and inactive employees. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

Changes in the Net Pension Liability:

	Increases (Decreases)		
	Total Pension Liability	**Plan Fiduciary Net Position**	**Net Pension Liability**
Balances at December 31, 2016	$ 11,457,643	$ 6,332,620	$ 5,125,023
Service cost	171,132	-	171,132
Interest on total pension liability	891,675	-	891,675
Changes in benefits	(10,166)	-	(10,166)
Difference between expected and actual experience	518,676	-	518,676
Changes in assumptions	-	-	-
Employer contributions	-	667,663	(667,663)
Employee contributions	-	121,913	(121,913)
Net investment income	-	838,774	(838,774)
Benefit payments, including employee refunds	(794,192)	(794,192)	-
Administrative expense	-	(13,256)	13,256
Other changes	(7,172)	-	(7,172)
Net changes	769,953	820,902	(50,949)
Balances as of December 31, 2017	$ 12,227,596	$ 7,153,522	$ 5,074,074

NOTE 5 - EMPLOYEE RETIREMENT AND BENEFIT SYSTEMS (Continued)

Sensitivity of the net pension liability to changes in the discount rate. The following presents the net pension liability of the Road Commission, calculated using the discount rate of 8.00%, as well as what the Road Commission's net pension liability would be if it were calculated using a discount rate that is 1-percentage-point lower (7.00%) or 1-percentage-point higher (9.00%) than the current rate:

	1% Decrease (7.00%)	Current Discount Rate (8.00%)	1% Increase (9.00%)
Road Commission's net pension liability	$6,376,276	$5,074,074	$3,960,970

Pension plan fiduciary net position. Detailed information about the pension plan's fiduciary net position is available in the separately issued MERS financial report.

Pension Expense and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions

For the year ended December 31, 2017, the Road Commission recognized pension expense of $945,244. At December 31, 2017, the Road Commission reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Difference between expected and actual experience	$ 395,039	$ -
Changes in assumptions	196,064	-
Net difference between projected and actual earnings on pension plan investments	-	446,430
Total	$ 591,103	$ 446,430

Amounts reported as deferred outflows of resources and deferred inflows of resources related to pensions will be recorded in pension expense as follows:

Year Ended December 31:	
2018	270,501
2019	68,405
2020	(50,638)
2021	(143,595)

NOTE 5 - EMPLOYEE RETIREMENT AND BENEFIT SYSTEMS (Continued)

Annual Pension Cost

During the year ended December 31, 2017, the Road Commission's contributions totaling $437,460 were made in accordance with contribution requirement determined by an actuarial valuation of the plan as of December 31, 2015. The employer contribution rate has been determined based on the entry age normal funding method. Under the entry age normal cost funding method, the total employer contribution is comprised of the normal cost plus the level annual percentage of payroll payment required to normal cost is, for each employee, the level percentage of payroll contribution (from entry age to retirement) required to accumulate sufficient assets at the member's retirement to pay for his projected benefit. Significant actuarial assumptions used include a long-term investment yield rate of 8 percent and annual salary increases of 4.5 percent based on an age-related scale to reflect merit, longevity, and promotional salary increases. The unfunded actuarial liability is amortized as a level percent of payroll on a closed basis. The remaining amortization period is 23 years.

NOTE 6 - FEDERAL GRANTS

The Michigan Department of Transportation (MDOT) requires that all Road Commissions report all federal and state grants pertaining to their county. During the year ended December 31, 2017, the federal aid received and expended by the Road Commission was $390,835 for contracted projects. Contracted projects are defined as projects performed by private contractors paid for and administrated by MDOT (they are included in MDOT's single audit). Local administered projects are projects where the Road Commissions perform the work and would be subject to single audit requirements if they expended $750,000 or more. Local projects amounted to $0.

NOTE 7 - 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.

NOTE 8 - LONG-TERM DEBT

The long-term debt of the Road Commission is summarized as follows:

	Balance 01/01/17	Additions	Reductions	Balance 12/31/17	Due Within One Year
Otsego County Building Authority Bonds Payable – 2011 Series, payable general obligation, serial maturity, 3.25% to 5.00% interest, due June 2031.	$ 725,000	$ -	$ 35,000	$ 690,000	$ 35,000
Installment payable secured by equipment, payable in annual installments of $84,277 including interest of 1.59%, due 2018.	164,566	-	81,658	82,908	82,908
Installment payable secured by equipment, payable in monthly installments of $1,748 including interest of 2.19%, due 2020.	216,115	-	14,659	201,456	16,770

NOTE 8 - LONG-TERM DEBT (Continued)

	Balance 01/01/17	Additions	Reductions	Balance 12/31/17	Due Within One Year
Installment payable secured by equipment, payable in monthly installments of $14,450 including interest of 2.14%, due 2020.	-	502,710	13,533	489,177	164,297
Installment payable secured by equipment, payable in annual installments of $80,455 including interest of 1.59%, due 2018.	141,251	-	78,659	62,592	62,592
Installment payable secured by equipment, payable in monthly installments of $113 including interest of 2.69%, due 2020.	89,959	2,431	-	92,390	-
Installment payable secured by equipment, payable in annual installments of $116,358 including interest of 1.69%, due 2019.	337,599	-	110,652	226,947	112,523
Installment payable secured by equipment, payable in annual installments of $72,097 including interest of 1.69%, due 2019.	209,181	-	68,562	140,619	69,720
Subtotal	1,883,671	505,141	402,723	1,986,089	$ 543,810
Vested Employee Benefits (1)	223,889	75,870	-	299,759	
TOTAL LONG-TERM DEBT	$ 2,107,560	$ 581,011	$ 402,723	$ 2,285,848	

(1) Net increase.

	Bonds Payable		Installments Payable	
Year End December 31	Principal	Interest	Principal	Interest
2018	$ 35,000	$ 30,488	$ 508,810	$ 24,361
2019	40,000	29,175	368,851	14,799
2020	40,000	27,775	418,428	3,534
2021	40,000	26,325	-	-
2022	45,000	24,562	-	-
2023-2027	245,000	91,175	-	-
2028-2031	245,000	25,375	-	-
Total	$ 690,000	$ 254,875	$ 1,296,089	$ 42,694

NOTE 9 - OTHER POST EMPLOYMENT BENEFITS

The 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.

Annual OPEB Cost and Net OPEB Obligation. 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 cost 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 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.

Funding Progress. For the year ended December 31, 2017, the Road Commission has determined an estimated cost of providing post employment benefits through an actuarial measurement method of calculation as of December 31, 2015. 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. For fiscal year 2017, the Road Commission contributed $353,506 to the plan, including member contributions of $2,961.

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

Annual required contribution/Annual OPEB cost (ARC)	$ 307,622
Interest on net OPEB obligation	337,213
Annual OPEB cost (expense)	644,835
Contributions made	(356,467)
Increase in net OPEB obligation	288,368
Net OPEB obligation – beginning of year	8,430,330
Net OPEB obligation – end of year	$ 8,718,698

NOTE 9 - OTHER POST EMPLOYMENT BENEFITS (Continued)

The Road Commission's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation for fiscal years 2015, 2016 and 2017 are as follows:

Fiscal Year End	Annual OPEB Cost		Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation	
2015	$	319,151	97.02%	$	8,148,256
2016	$	633,552	55.40%	$	8,430,330
2017	$	644,835	55.28%	$	8,718,698

Funded Status and Funding Progress: As of December 31, 2015, the actuarial accrued liability for benefits was $6,088,899, all of which was unfunded. The covered payroll (annual payroll of active employees covered by the plan) was $1,103,398, and the ratio of the unfunded actuarial accrued liability to the covered payroll was 552%.

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 the 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 member 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.

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 2007 Version – United States Life Tables. 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 2015 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 2005 – 2020 version of the National Health Expenditures projection.

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 4.0%. 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.

NOTE 10 - COMMITMENTS AND CONTINGENCIES

Grants – The Road Commission has received significant financial assistance from state and federal agencies in the form of various grants. The disbursement of funds received under these programs generally requires compliance with terms and conditions specified in the grant agreement and are subject to audit by the grantor agency. Any disallowed claims resulting from such audits could become a liability of the applicable fund of the Commission.

NOTE 10 - COMMITMENTS AND CONTINGENCIES (Continued)

Risk Management – The Road Commission is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The Road Commission was unable to obtain general liability insurance at a cost it considered to be economically justifiable. The Road Commission joined together with other Road Commissions and created a public entity risk pool currently operating as a common risk management and insurance program. The Road Commission pays an annual premium to the pool for its general insurance coverage. The agreement provides that the pool will be self-sustaining through member premiums and will reinsure through commercial companies for claims in excess of $1,000 ($2,000 for errors and omissions) for each insured event. The maximum limit of liability for each occurrence is $10,500,000.

The pooling agreement allows for the pool to make additional assessments to make the pool self-sustaining. The Road Commission is unable to provide an estimate of the amounts of additional assessments.

The Road Commission from time to time is named as a defendant in accident claims and lawsuits requesting damages of various amounts, the majority of which do not state a specific maximum. Insurance coverage related to these claims and lawsuits, if any, is categorized under the general liability insurance program. It is the opinion of management and legal counsel that reasonable estimates of the Road Commission's current liability for these matters, if any, have been recorded.

There are nonaccident liability and condemnation lawsuits sometimes are pending against the Road Commission claiming amounts for damages and relief without stated limitations. It is the opinion of management and legal counsel that reasonable estimates of the Road Commission's current liability for these matters, if any, have been recorded.

NOTE 11 - SUBSEQUENT EVENTS

After fiscal year end, the Road Commission executed equipment purchases amounting to approximately $68,000. Additionally, the Road Commission established a Public Act 115 Health Care Trust in January 2018 with a $100,000 contribution.

Required Supplementary Information

Employee Retirement and Benefit Systems
Schedule of Funding Progress
For the Year Ended December 31, 2017

	2015	2016	2017
Total pension liability			
Service cost	$ 137,944	$ 125,690	$ 171,132
Interest	835,847	853,243	891,675
Changes in benefits	-	(5,403)	(10,166)
Difference between expected and actual experience	-	18,096	518,676
Changes in assumptions	-	588,192	-
Other changes	8,813	(5,518)	(7,172)
Benefit payments, including refund of member contributions	(738,956)	(792,294)	(794,192)
Net change in total pension liability	243,648	782,006	769,953
Total pension liability - beginning	10,431,989	10,675,637	11,457,643
Total pension liability - ending	$ 10,675,637	$ 11,457,643	$ 12,227,596
Plan fiduciary net position			
Contributions - employer	$ 498,792	$ 508,482	$ 667,663
Contributions - employee	77,134	39,017	121,913
Net investment income	(91,306)	662,026	838,774
Benefit payments, including refunds of member contributions	(738,956)	(792,294)	(794,192)
Administrative expense	(13,449)	(13,077)	(13,256)
Net change in plan fiduciary net position	(267,785)	404,154	820,902
Plan fiduciary net position - beginning	6,196,251	5,928,466	6,332,620
Plan fiduciary net position - ending	$ 5,928,466	$ 6,332,620	$ 7,153,522
Net pension liability - ending	$ 4,747,171	$ 5,125,023	$ 5,074,074
Plan fiduciary net position as a percentage of the total pension liability	56%	55%	59%
Covered - employee payroll	$ 1,409,673	$ 1,256,307	$ 1,576,491
Net pension liability as a percentage of covered-employee payroll	337%	408%	322%

Employee Retirement and Benefit Systems
Schedule of Funding Progress
For the Year Ended December 31, 2017

	2015	2016	2017
Actuarially determined contribution	$ 376,152	$ 366,192	$ 437,460
Contributions in relation to the actuarially determined contribution	(498,792)	(508,482)	(667,663)
Contribution deficiency (excess)	$ (122,640)	$ (142,290)	$ (230,203)
Covered - employee payroll	$ 1,399,784	$ 1,409,673	$ 1,256,307
Contributions as a percentage of covered-employee payroll	36%	36%	53%

Notes to Schedule:

Actuarially determined contribution rates are calculated as of December 31st, two years prior to the end of the fiscal year in which contributions are reported.

Methods and assumptions used to determine contribution rates:

Actuarial cost method	Entry age
Amortization method	Level percentage of payroll, closed
Remaining amortization period	22 years
Asset valuation method	10-years smoothed market
Inflation	2.50%
Salary increases	3.75%
Investment rate of return	7.75%, net of interest and aministrative expense including inflation
Retirement age	In the 2016 actuarial valuation, expected retirement ages of general employees were adjusted to more closely reflect actual experience
Mortality	Assumptions were based on the RP2014 Mortality Table - Blended 50% Male / 50% Female

Required Supplementary Information
Employee Retirement and Benefit Systems
Schedule of Funding Progress
December 31, 2017

Health Benefits:

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) - Entry Age (b)	Unfunded AAL (UAAL) (b – a)	Funded Ratio (a / b)	Covered Payroll (c)	UAAL as a Percent of Covered Payroll ((b – a) / c)
2011	$ -	$ 13,009,780	$ 13,009,780	0.0%	$ 1,397,173	931%
2014	$ -	$ 9,281,304	$ 9,281,304	0.0%	$ 1,526,387	608%
2015	$ -	$ 6,088,899	$ 6,088,899	0.0%	$ 1,103,398	552%

Required Supplementary Information
Budgetary Comparison Schedule
Statement of Revenues - Budget and Actual
For the Year Ended December 31, 2017

	Original Budget	Final Amended Budget	Actual	Variance Favorable (Unfavorable)
Taxes	$ 980,000	$ 999,000	$ 985,400	$ (13,600)
Licenses and Permits	71,000	71,000	55,948	(15,052)
Federal Sources				
Surface Transportation Program	524,000	524,000	390,835	(133,165)
State Sources				
Michigan Transportation Fund				
Engineering	10,000	10,000	10,000	-
Allocation	4,072,000	4,600,000	4,446,296	(153,704)
Snow Removal	260,000	260,000	241,594	(18,406)
Urban Road	422,000	499,000	492,105	(6,895)
Forest Road	172,000	172,000	170,215	(1,785)
Contributions from Local Units				
Townships	1,200,000	1,200,000	1,128,799	(71,201)
Charges for Services				
Trunkline Maintenance	1,200,000	1,400,000	1,363,253	(36,747)
Trunkline Nonmaintenance	350,000	350,000	271,948	(78,052)
Salvage Sales	7,500	7,500	4,103	(3,397)
Other	-	170,000	229,699	59,699
Interest Earnings and Rent	20,000	45,000	43,455	(1,545)
Other Revenue				
Gain (Loss) on Disposal	50,000	15,000	16,800	1,800
Private Contributions and Other	35,200	65,200	53,515	(11,685)
Other Financing Sources	-	-	505,141	505,141
Total Revenues	$ 9,373,700	$ 10,387,700	$ 10,409,106	$ 21,406

Required Supplementary Information
Budgetary Comparison Schedule
Statement of Expenditures - Budget and Actual
For the Year Ended December 31, 2017

	Original Budget	Final Amended Budget	Actual	Variance Favorable (Unfavorable)
Primary Road				
Preservation - Structural Improvements	$ 2,580,000	$ 2,580,000	$ 2,084,587	$ 495,413
Maintenance	1,487,100	1,487,100	1,436,478	50,622
Local Road				
Preservation - Structural Improvements	936,000	936,000	961,631	(25,631)
Maintenance	1,988,480	2,016,080	1,766,502	249,578
Trunkline Maintenance	1,200,000	1,400,000	1,363,253	36,747
Trunkline Nonmaintenance	350,000	350,000	271,948	78,052
Administrative Expense - Net	624,000	624,000	624,683	(683)
Equipment Expense - Net	104,000	455,000	107,433	347,567
Capital Outlay - Net	(356,000)	(118,000)	(310,284)	192,284
Debt Service				
Principal	400,000	400,000	402,723	(2,723)
Interest	60,000	60,000	57,283	2,717
Total Expenditures	9,373,580	10,190,180	$ 8,766,237	$ 1,423,943
Fund Balance - January 1, 2017	2,890,576	2,890,576		
Total Budget	$ 12,264,156	$ 13,080,756		

Other Information

Analysis of Changes in Fund Balance
For the Year Ended December 31, 2017

	Primary Road Fund	Local Road Fund	County Road Commission	Total
Total Revenues	$ 4,354,317	$ 2,598,296	$ 3,456,493	$ 10,409,106
Total Expenditures	3,935,445	3,041,475	1,789,317	8,766,237
Excess of Revenues Over (Under) Expenditures	418,872	(443,179)	1,667,176	1,642,869
Optional Transfers and Adjustments	(418,872)	443,179	(24,307)	-
Fund Balance - January 1, 2017	-	-	2,890,576	2,890,576
Fund Balance - December 31, 2017	$ -	$ -	$ 4,533,445	$ 4,533,445

Analysis of Revenues
For the Year Ended December 31, 2017

	Primary Road Fund	Local Road Fund	County Road Commission	Total
Taxes	$ -	$ -	$ 985,400	$ 985,400
Licenses and Permits	-	-	55,948	55,948
Federal Sources				
Surface Transportation Program	390,835	-	-	390,835
State Sources				
Michigan Transportation Fund				
Engineering	6,197	3,803	-	10,000
Allocation	2,755,398	1,690,898	-	4,446,296
Snow Removal	-	241,594	-	241,594
Urban Road	337,114	154,991	-	492,105
Forest Road	170,215	-	-	170,215
Contributions from Local Units				
Townships	621,789	507,010	-	1,128,799
Charges for Services				
Trunkline Maintenance	-	-	1,363,253	1,363,253
Trunkline Nonmaintenance	-	-	271,948	271,948
Salvage Sales	-	-	4,103	4,103
Other	72,769	-	156,930	229,699
Interest and Rents				
Interest Earnings	-	-	32,355	32,355
Property Rentals	-	-	11,100	11,100
Other Revenue				
Gain on Equipment Disposals	-	-	16,800	16,800
Other	-	-	53,515	53,515
Other Financing Sources				
Installment Purchases	-	-	505,141	505,141
Total Revenues	$ 4,354,317	$ 2,598,296	$ 3,456,493	$ 10,409,106

Analysis of Expenditures
For the Year Ended December 31, 2017

	Primary Road Fund	Local Road Fund	County Road Commission	Total
Primary Road				
Preservation - Structural Improvements	$ 2,084,587	$ -	$ -	$ 2,084,587
Maintenance	1,436,478	-	-	1,436,478
Local Road				
Preservation - Structural Improvements	-	961,631	-	961,631
Maintenance	-	1,766,502	-	1,766,502
Trunkline Maintenance	-	-	1,363,253	1,363,253
Trunkline Nonmaintenance	-	-	271,948	271,948
Administrative Expense - Net	351,973	272,710	-	624,683
Equipment Expense - Net	62,407	40,632	4,394	107,433
Capital Outlay - Net	-	-	(310,284)	(310,284)
Debt Service				
Debt Principal Payments	-	-	402,723	402,723
Interest Expense	-	-	57,283	57,283
Total Expenditures	$ 3,935,445	$ 3,041,475	$ 1,789,317	$ 8,766,237

Report on Compliance

ANDERSON, TACKMAN & COMPANY, PLC
CERTIFIED PUBLIC ACCOUNTANTS

KINROSS OFFICE
SUE A. BOWLBY, CPA, PRINCIPAL
KENNETH A. TALSMA, CPA, PRINCIPAL
AMBER N. MACK, CPA, PRINCIPAL

PHILLIP J. WOLF, CPA

MEMBER AICPA
DIVISION FOR CPA FIRMS
MEMBER MACPA
OFFICES IN
MICHIGAN & WISCONSIN

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*

Board of County Road Commissioners
Otsego County Road Commission
669 West McCoy Road
Gaylord, Michigan 49734

We 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 component unit of Otsego County, Michigan), as of and for the year ended December 31, 2017, and the related notes to the financial statements, which collectively comprise the Otsego County Road Commission's basic financial statements and have issued our report thereon dated April 20, 2018.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we 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 our 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, we 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.

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Our 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 our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. We did identify certain deficiencies in internal control, described in the accompanying schedule of findings and responses that we consider to be significant deficiencies listed as 2017-001 and 2017-002.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Otsego County Road Commission's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed one instance of noncompliance or other matters that is required to be reported under *Government Auditing Standards,* and which is described in the accompanying schedule of findings and responses as items 2017-003.

Otsego County Road Commission's Response to Findings

The Otsego County Road Commission's responses to the findings identified in our audit are described in the accompanying schedule of findings and responses. The Otsego County Road Commission's responses were not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on them.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the result 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.

Anderson Tackman & Co. PLC

Anderson, Tackman & Company, PLC
Certified Public Accountants
Kincheloe, Michigan

April 20, 2018

Schedule of Findings and Responses
For the Year Ended December 31, 2017

Significant Deficiency - Internal Control

Preparation of the Financial Statements in Accordance with Generally Accepted Accounting Principles — ***Finding 2017-001***

Specific Requirement: Establishment and maintenance of internal control over the financial reporting process as defined by Statement on Auditing Standards Number 115 requires management to prepare annual audit statements in accordance with GASB Statement Number 34. (Audit report format)

Criteria: Internal controls should be in place to provide reasonable assurance to the Commission that management reports financial statements (with GASB Statement number 34 formats) necessary to monitor and report annual financial activity without auditor intervention.

Condition: Auditor modifies financial statements and footnotes to comply with governmental generally accepted accounting principles.

Effect: The effect of this condition places a reliance on the independent auditor as part of the Commission's internal controls over financial reporting.

Cause: Change in application of auditing standard.

Recommendation: The Commission should consider subcontracting financial statement preparation activities to monitor and report annual financial activity in accordance with GASB Statement Number 34 or train staff to accomplish this element.

Planned Corrective Action: In the past, the Board has relied on the auditors for this type of reporting for cost effectiveness. Due to limited resources, management does not wish to allocate additional funds to change this process. Management reviews adjustments for accuracy upon completion and reconciles discrepancies and other disclosures.

- Contact Person(s) Responsible for Correction:
  Jason Melancon, Manager

Significant Deficiency - Internal Control

Segregation of Duties **_Finding 2017-002_**

Condition/Criteria: The Road Commission Finance Director performs several functions of receipting/disbursing (when other personnel are not available), and posting to the general ledger. To provide a system of checks and balances, these functions are generally assigned to separate positions to minimize the potential for unauthorized transactions.

Effect: Lack of segregation of duties provides opportunities for inaccurate or unauthorized disbursements or transfers from road funds and increases the potential for inaccurate reporting of account activity.

Cause: Sufficient resources and staff are not available to adequately segregate these functions. Additionally, the benefit of separating these duties does not appear to exceed the costs associated with the added personnel.

Recommendation: The Board should be aware of the potential weakness in the system and provide appropriate oversight or assistance to personnel when cost beneficial.

Planned Corrective Action: The Board has implemented compensating controls to reduce the risks discussed above such as dual signature checks and account reviews.

- Contact Person(s) Responsible for Correction:
  Jason Melancon, Manager

Significant Deficiencies – Noncompliance with State Statutes

Expenditures in Excess of Appropriations—Budgetary Funds ***Finding 2017-003***

Criteria: The expenditures of funds in excess of appropriations are contrary to the provisions of Section 16 of Public Act 2 of 1968, as amended.

Condition: Our examination of procedures used by the Road Commission to adopt and maintain operating budgets for the Road Commission's budgetary fund revealed the following instances of noncompliance with the provisions of Public Act 2 of 1968, as amended, the Uniform Budgeting and Accounting Act.

The Road Commission's 2017 General Appropriations Act (budget) provided for expenditures of the General Fund to be controlled to the activity level. As detailed, actual 2017 expenditures exceeded the board's approved budget allocations for some general fund activities.

During the fiscal year ended December 31, 2017, expenditures were incurred in excess of amounts appropriated in the amended budgets for the General Fund as listed on page 35 of the financial statements.

Effect: Condition's may violate State Law.

Cause: Unknown.

Recommendation: We recommend that the Road Commission's chief administrative officer and personnel responsible for administering the activities of the various funds of the Road Commission, develop budgetary control procedures for the General Fund which will assure that expenditures do not exceed amounts authorized in the General Appropriations Act, or amendments thereof.

Planned Corrective Action: Amounts will be maintained in the future. Most of the expenditure variance was related to a project initiated by the City of Gaylord and reported to the Road Commission subsequent to year end. We do not anticipate this circumstance in the future.

- Contact Person(s) Responsible for Correction:
  Jason Melancon, Manager