Otsego County Road Commission

BASIC FINANCIAL STATEMENTS

December 31, 2018

OTSEGO COUNTY ROAD COMMISSION

BOARD OF COUNTY ROAD COMMISSIONERS

William Holewinski
Chairman

Troy Huff Vice Chairman	Michael Dipzinski Member
James Camiller Member	Kathy Heinz Member
Jason Melancon Manager	Rebecca Jerry Board Secretary/ Finance Director

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ANDERSON, TACKMAN & COMPANY, PLC
CERTIFIED PUBLIC ACCOUNTANTS

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PHILLIP J. WOLF, CPA
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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, major fund and the aggregate remaining fund information of the Otsego County Road Commission (a component unit of Otsego County, Michigan) as of and for the year ended December 31, 2018, 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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Board of County Road Commissioners
Otsego County Road Commission

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, major fund and the aggregate remaining fund information of the Otsego County Road Commission, as of December 31, 2018, 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, employee retirement and benefit systems, budgetary comparison schedules on pages 4 through 8, pages 35 through 42 and pages 43 through 44 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 May 21, 2019, 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 that report is solely 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 effectiveness of the Otsego County Road Commission's 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's internal control over financial reporting and compliance.

Anderson Tackman & Co. PLC

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

May 21, 2019

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 45 and provide detailed information about the major fund. The Road Commission currently has only one major 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.

- Fiduciary fund – The Road Commission is trustee, or fiduciary, for its employees' health care plan. The Road Commission is responsible for ensuring that the assets reported in the fiduciary funds are used for their intended purposes. All of the Road Commission's fiduciary activities are reported in a separate statement of fiduciary net position and a statement of changes in fiduciary net position. We exclude these activities from the Road Commission's government-wide financial statements because the Road Commission cannot use these assets to finance its operations.

The Road Commission as a Whole

The Road Commission's Net Position increased 29.71% from $22,439,552 to $29,106,090 for the year ended December 31, 2018. The Net Position and Change in Net Position are summarized below.

Unrestricted Net Position increased $3,493,107. The primary reasons were related to OPEB liabilities and state funding.

Net Position as of the years ended December 31, 2018 and 2017 follows:

	Governmental Activities	
	2018	2017
Current Assets	$ 6,718,593	$ 6,470,149
Capital Assets	36,050,865	33,848,512
Total Assets	42,769,458	40,318,661
Deferred Outflows of Resources	789,530	591,103
Current Liabilities	843,111	1,425,496
Noncurrent Liabilities	12,522,042	15,534,810
Total Liabilities	13,365,153	16,960,306
Deferred Inflows of Resources	1,087,745	1,509,906
Net Position		
Net Investment in Capital Assets	35,035,854	31,862,423
Unrestricted (Deficit)	(5,929,764)	(9,422,871)
Total Net Position	$ 29,106,090	$ 22,439,552

A summary of Changes in Net Position for the years ended December 31, 2018 and 2017 follows:

	Governmental Activities	
	2018	2017
Program Revenues		
Charges for Services	$ 2,264,312	$ 2,229,510
Grants and Contributions	8,251,541	6,879,844
Interest and Rents	91,100	43,455
General Revenues		
Gain (Loss) on Equipment Disposal	77,539	16,800
Taxes and Other	1,056,096	985,400
Total Revenues	11,740,588	10,155,009
Program Expenses		
Primary Roads	1,606,552	1,436,478
Local Roads	2,050,406	1,766,502
State Trunkline	1,820,500	1,635,201
Equipment Expense	292,362	107,433
Administrative	744,349	624,683
Depreciation - Unallocated	1,665,151	1,607,452
Interest Expense and Other	(606,543)	836,160
Total Expenses	7,572,777	8,013,909
Change in Net Position	4,167,811	2,141,100
Net Position – Beginning, as Restated	24,938,279	20,298,452
Net Position – Ending	$ 29,106,090	$ 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, 2018, the fund balance of the general operations fund increased $324,600 as compared to an increase of $1,624,869 in the fund balance for the prior year. Total revenues were $11,902,644, an increase of $1,493,538 as compared to last year. This change in revenues resulted primarily from state sources.

Total expenditures were $11,578,044, an increase of $2,811,807. The increase is largely due to primary road expenditures and 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 2018 was $954,931 more than the actual receipts. This was due, in part, to the projection of federal grants. The Road Commission budgets for the receipt of funds for projects on primary and local roads as earned.

Road Commission expenditures were projected at $11,896,200 while actual expenditures were $11,578,044. This resulted in total expenditures being under budget by $318,156. There were several items that account for the variance in the projection of the budget.

Capital Assets

As of December 31, 2018 and 2017, the Road Commission had invested in capital assets as follows:

	2018	2017
Capital Assets Not Being Depreciated		
Land and Improvements	$ 11,647,119	$ 10,889,984
Other Capital Assets		
Buildings	3,936,130	3,936,130
Road Equipment	7,656,680	7,093,391
Other Equipment and Assets	164,088	174,307
Infrastructure	35,110,983	33,503,417
Total Capital Assets at Historic Cost	58,515,000	55,597,229
Total Accumulated Depreciation	(22,464,135)	(21,748,717)
Total Net Capital Assets	$ 36,050,865	$ 33,848,512

Major additions included the following:

	2018	2017
Land Improvements	$ 757,135	$ 994,034
Various Resurfacing Projects and Bridges	$ 2,881,339	$ 2,052,184
Trucks/Equipment/Other	$ 877,895	$ 379,059

Debt

The Road Commission currently has long-term debt in the amount of $12,589,860 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 2019 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.

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, 2018

ASSETS	
Cash and Equivalents	$ 3,448,756
Receivables:	
Taxes	1,087,745
Michigan Transportation Fund	747,234
State Trunkline Maintenance	181,849
State Transportation - Other	18,543
Due from State	333,424
Due on County Road Agreements	30,000
Sundry Accounts	7,375
Inventories:	
Road Materials	546,430
Equipment, Parts and Materials	317,237
Capital Assets (Not Depreciated)	11,647,119
Capital Assets (Net of Accumulated Depreciation)	24,403,746
Total Assets	42,769,458
DEFERRED OUTFLOWS OF RESOURCES	
Pension and OPEB Items	789,530
LIABILITIES	
Accounts Payable	157,578
Due to State	44,742
Accrued Liabilities	114,586
Advances	455,897
Interest Payable	2,490
Notes Payable - Due within one year	27,818
Notes Payable - Due in more than one year	332,193
Bonds Payable - Due within one year	40,000
Bonds Payable - Due in more than one year	615,000
Vested Employee Benefits - Due in more than one year	252,218
Other Post Employment Benefits - Due in more than one year	5,678,335
Net Pension Liability - Due in more than one year	5,644,296
Total Liabilities	13,365,153
DEFERRED INFLOWS OF RESOURCES	
Taxes Levied for Subsequent Period	1,087,745
NET POSITION	
Net Investment in Capital Assets	35,035,854
Unrestricted (Deficit)	(5,929,764)
Total Net Position	$ 29,106,090

Statement of Activities
For the Year Ended December 31, 2018

Program Expenses:	
Primary Road Maintenance	
and Preventive Maintenance	$ 1,606,552
Local Road Maintenance	
and Preventive Maintenance	2,050,406
State Trunkline	1,820,500
Net Equipment Expense	292,362
Net Administrative Expense	744,349
Depreciation - Unallocated	1,665,151
Interest Expense	57,268
Other	(663,811)
Total Program Expenses	7,572,777
Program Revenues:	
Charges for Services:	
Licenses and Permits	214,102
Charges for Services	2,050,210
Operating Grants and Contributions:	
State Grants	4,597,141
Contributions from Local Units	15,926
Interest & Rents	91,100
Capital Grants and Contributions:	
Federal Grants	654,441
State Grants	2,394,415
Contributions from Local Units	589,618
Total Program Revenues	10,606,953
Net Program Revenues (Expenses)	3,034,176
General Revenues:	
Taxes - Real Property	1,056,096
Gain (Loss) on Equipment Disposal	77,539
Total General Revenues	1,133,635
Change in Net Position	4,167,811
Net Position - Beginning Balance as Restated	24,938,279
Net Position - Ending Balance	$ 29,106,090

See accompanying notes to financial statements.

Balance Sheet
December 31, 2018

	Governmental Fund Type General Operating Fund
ASSETS	
Cash and Equivalents	$ 3,448,756
Receivables:	
Taxes	1,087,745
Michigan Transportation Fund	747,234
State Trunkline Maintenance	181,849
State Transportation - Other	18,543
Due from State	333,424
Due on County Road Agreements	30,000
Sundry Accounts	7,375
Inventories:	
Road Materials	546,430
Equipment, Parts and Materials	317,237
Total Assets	$ 6,718,593
LIABILITIES	
Accounts Payable	$ 157,578
Due to State	44,742
Accrued Liabilities	114,586
Advances	455,897
Total Liabilities	772,803
DEFERRED INFLOWS OF RESOURCES	
Taxes Levied for Subsequent Period	1,087,745
FUND BALANCE	
Nonspendable	863,667
Unassigned	3,994,378
Total Fund Balance	$ 4,858,045

See accompanying notes to financial statements.

Reconciliation of the Balance Sheet Fund Balance to the Statement of Net Position For the Year Ended December 31, 2018

Total Governmental Fund Balance	$ 4,858,045
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.	36,050,865
Net pension liability requirement.	(5,644,296)
Other post employment benefits net liability.	(5,678,335)
Deferred outflows resulting from pension and OPEB experience, investments and assumptions.	789,530
Other liabilities are not available to pay in the current period and therefore are not reported in the funds.	(1,269,719)
Net Position of Governmental Activities	$ 29,106,090

Statement of Revenues, Expenditures, and Changes in Fund Balance
For the Year Ended December 31, 2018

	Governmental Fund Type General Operating Fund
Revenues	
Property Taxes	$ 1,056,096
Licenses and Permits	214,102
Federal Sources	654,441
State Sources	6,991,556
Contributions from Local Units	605,544
Charges for Services	1,996,025
Interest Earnings and Rent	91,100
Other Revenue	131,724
Other Financing Sources	162,056
Total Revenues	11,902,644
Expenditures	
Public Works	10,152,643
Capital Outlay	229,031
Debt Service	1,196,370
Total Expenditures	11,578,044
Excess of Revenues Over (Under) Expenditures	324,600
Fund Balance - Beginning of Year	4,533,445
Fund Balance - End of Year	$ 4,858,045

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, 2018

Net Change in Fund Balance - Total Governmental Funds	$	324,600
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 and retirements in the current period.		2,202,353
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.		971,078
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.		669,780
Net Change in Net Position of Governmental Activities	$	4,167,811

See accompanying notes to financial statements.

Statement of Net Position
Fiduciary Fund
December 31, 2018

	OPEB Trust Fund
ASSETS	
Investments at Fair Market Value	$ 490,210
NET POSITION	
Restricted for Other Post Employment Benefits	$ 490,210

See accompanying notes to financial statements.

Statement of Changes in Net Position
Fiduciary Fund
For the Year Ended December 31, 2018

	OPEB Trust Fund
ADDITIONS	
Investment Earnings:	
Contributions - Employer	$ 520,000
Net Increase (Decrease) in Fair Value of Investments	(29,215)
Total Additions	490,785
DEDUCTIONS:	
Benefits payments, including refunds of member contributions	-
Administrative Fees	575
Total Deductions	575
Change in Net Position	490,210
Net Position Restricted for Other Post Employment Benefits	
Beginning of Year	-
End of Year	$ 490,210

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 five (5) 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 2018 taxable valuation of $1,258,730,002 for Road Millage amounted to $1,258,730 less $170,985 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 $1,087,745.

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 2018 ad valorem tax is levied and collectible December 1, 2018, 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 and OPEB 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 that qualify for reporting in this category.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Pension and Other Post Employment Benefits

For purposes of measuring the net pension and OPEB liability, deferred outflows of resources and deferred inflows of resources and fringe expense, information about the fiduciary net position of the Plans and additions to/deductions from the fiduciary net position have been determined on the same basis as they are reported by the actuary. 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 350 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 $90,698 and $161,520 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 44.

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	$ 700	
Bank Deposits (Checking and Savings Accounts)	1,256,193	$ 1,254,312
Investments at Fair Value	2,191,863	
Total Cash and Equivalents	$ 3,448,756	

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, $754,312 of the Road Commission's bank balance of $1,254,312 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	$ 1,691,863	$ -	$ 1,691,863	$ -	AA+	77%
Other	500,000	-	-	500,000	Unrated	23%
	$ 2,191,863	$ -	$ 1,691,863	$ 500,000		
OPEB Trust Pool	$ 490,210	$ -	$ 490,210	$ -	Unrated	100%

NOTE 4 - CAPITAL ASSETS

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

	Beginning Balances 01/01/18	Additions	Adjustments/ Deductions	Ending Balances 12/31/18
Capital Assets Not Being Depreciated				
Land	$ 125,501	$ -	$ -	$ 125,501
Land Improvements – Infrastructure	10,764,483	757,135	-	11,521,618
Subtotal	10,889,984	757,135	-	11,647,119
Capital Assets Being Depreciated				
Buildings	3,936,130	-	-	3,936,130
Road Equipment	7,093,391	877,895	314,606	7,656,680
Shop Equipment	108,683	-	2,004	106,679
Office Equipment	50,262	-	8,215	42,047
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	32,341,559	2,881,339	1,273,773	33,949,125
Subtotal	44,707,245	3,759,234	1,598,598	46,867,881
Less Accumulated Depreciation				
Buildings	1,891,067	87,241	-	1,978,308
Road Equipment	5,781,546	556,341	314,495	6,023,392
Shop Equipment	102,618	3,047	2,004	103,661
Office Equipment	46,351	2,125	8,215	40,261
Engineers' Equipment	13,562	-	-	13,562
Yard and Storage Equipment	1,800	-	-	1,800
Traffic Signals	45,396	320	-	45,716
Infrastructure – Bridges	305,109	28,840	-	333,949
Infrastructure – Roads	13,561,268	1,635,991	1,273,773	13,923,486
Subtotal	21,748,717	2,313,905	1,598,487	22,464,135
Net Capital Assets Being Depreciated	22,958,528	1,445,329	(111)	24,403,746
Capital Assets - Net	$ 33,848,512	$ 2,202,464	$ (111)	$ 36,050,865

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

Infrastructure - unallocated	$ 1,665,151
Equipment Expense	556,341
Administrative	12,974
Other Allocated	79,439
Total Depreciation Expense	$ 2,313,905

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 multiplied 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, 2017.

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	
	2017 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:	4.0%
Act 88:	Yes (Adopted 11/23/1970)

02 – General: Open Division	
	2017 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:	4.0%
Act 88:	Yes (Adopted 11/23/1970)

NOTE 5 - EMPLOYEE RETIREMENT AND BENEFIT SYSTEMS (Continued)

NonUnion: Open Division	
	2017 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:	4.0%
Act 88:	Yes (Adopted 11/23/1970)

Employees Covered by Benefit Terms

At December 31, 2017, 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	6
Active employees	32
	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 2018 of 32.90% of nonunion payroll and 25.61% of general employees.

Net Pension Liability

The Road Commission's net pension liability was measured as of December 31, 2017, 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, 2017 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	55.5%	3.41%
Global Fixed Income	18.5%	0.23%
Real Assets	13.5%	0.97%
Diversifying Strategies	12.5%	0.03%

Discount Rate. The discount rate used to measure the total pension liability is 8.00% for 2017. The projection of cash flows used to determine the discount rate assumes that employer and employee contributions will 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, 2017	$ 12,227,596	$ 7,153,522	$ 5,074,074
Service cost	185,530	-	185,530
Interest on total pension liability	953,214	-	953,214
Changes in benefits	(4,710)	-	(4,710)
Difference between expected and actual experience	255,051	-	255,051
Changes in assumptions	-	-	-
Employer contributions	-	1,065,147	(1,065,147)
Employee contributions	-	68,858	(68,858)
Net investment income	-	(299,600)	299,600
Benefit payments, including employee refunds	(810,376)	(810,376)	-
Administrative expense	-	(14,274)	14,274
Other changes	1,268	-	1,268
Net changes	579,977	9,755	570,222
Balances as of December 31, 2018	$ 12,807,573	$ 7,163,277	$ 5,644,296

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	$6,999,892	$5,644,296	$4,484,425

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, 2018, the Road Commission recognized pension expense of $1,028,431. At December 31, 2018, 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	$ 429,372	$ -
Changes in assumptions	-	-
Net difference between projected and actual earnings on pension plan investments	322,239	-
Total	$ 751,611	$ -

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:	
2019	$ 330,273
2020	211,230
2021	33,256
2022	176,852

NOTE 5 - EMPLOYEE RETIREMENT AND BENEFIT SYSTEMS (Continued)

Annual Pension Cost

During the year ended December 31, 2018, the Road Commission's contributions totaling $1,065,147 were made in accordance with contribution requirement determined by an actuarial valuation of the plan as of December 31, 2016. 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, 2018, the federal aid received and expended by the Road Commission was $654,441 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 01/01/18	Additions	Reductions	Balance 12/31/18	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.	$ 690,000	$ -	$ 35,000	$ 655,000	$ 40,000
Installment payable secured by equipment, payable in annual installments of $84,277 including interest of 1.59%, due 2018.	82,908	-	82,908	-	-
Installment payable secured by equipment, payable in monthly installments of $1,748 including interest of 2.19%, due 2020.	201,456	-	16,770	184,686	17,110

NOTE 8 - LONG-TERM DEBT (Continued)

	Balance 01/01/18	Additions	Reductions	Balance 12/31/18	Due Within One Year
Installment payable secured by equipment, payable in monthly installments of $14,430 including interest of 2.14%, due 2020.	489,177	-	489,177	-	-
Installment payable secured by equipment, payable in annual installments of $80,455 including interest of 1.59%, due 2018.	62,592	-	62,592	-	-
Installment payable secured by equipment, payable in monthly installments of $113 including interest of 2.69%, due 2020.	92,390	1,276	-	93,666	-
Installment payable secured by equipment, payable in annual installments of $116,358 including interest of 1.69%, due 2019.	226,947	-	226,947	-	-
Installment payable secured by equipment, payable in annual installments of $72,097 including interest of 1.69%, due 2019.	140,619	-	140,619	-	-
Installment payable secured by equipment, payable in annual installments of $14,122 including interest of 4.18%, due 2023.	-	160,780	79,121	81,659	10,708
Subtotal	1,986,089	162,056	1,133,134	1,015,011	$ 67,818
Vested Employee Benefits (1)	299,759	-	47,541	252,218	
TOTAL LONG-TERM DEBT	$ 2,285,848	$ 162,056	$ 1,180,675	$ 1,267,229	

(1) Net decrease.

	Bonds Payable		Installments Payable	
Year End December 31	Principal	Interest	Principal	Interest
2019	$ 40,000	$ 29,175	$ 27,818	$ 7,279
2020	40,000	27,775	272,398	4,160
2021	40,000	26,325	11,622	2,499
2022	45,000	24,562	12,108	2,014
2023	45,000	22,538	36,065	1,507
2024-2028	255,000	79,512	-	-
2029-2031	190,000	14,500	-	-
Total	$ 655,000	$ 224,387	$ 360,011	$ 17,459

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 74 and 75 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 - Contribution requirements also are negotiated between the Commission and employees. The Commission contributes 100% of the cost for eligible plan members. For fiscal year 2018, the Commission contributed $520,000 to the plan.

Employees Covered by Benefit Terms

As of December 31, 2018, the following employees were covered by the benefit terms:

Inactive employees or beneficiaries currently receiving benefit payments	37
Inactive employees entitled to but not yet receiving benefits	20
Active employees	16
Total participants covered by OPEB Plan	73

Total OPEB Liability and Trust Assets - The Road Commission's total OPEB liability of $6,168,545 was measured as of December 31, 2018, and was determined by an actuarial valuation as of that date.

As of December 31, 2018, there was $490,210 in assets in the Road Commission's OPEB trust.

Actuarial assumptions and other inputs - The total OPEB liability was determined by an actuarial valuation as of December 31, 2018 and the following actuarial assumptions, applies to all periods included in the measurement:

Inflation	Included in investment rate of return
Salary Increases	3.50%
Investment rate of return	7.00%
Uniform assumption for unfunded period	3.00%
Mortality	RP–2014 adjusted to 2006 Total Data Set, with MP–2018 mortality improvement.

The long-term expected rate of return on plan investments was determined using a building-block method in which best-estimate ranges of expected future rates of return (expected returns, net of retirement plan investment expense 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 rates of return by the target asset allocation percentage and by adding expected inflation. Best estimates of arithmetic rates of return for each major asset class included in the retirement plan's target asset allocation are summarized in the following table:

NOTE 9 - OTHER POST EMPLOYMENT BENEFITS (Continued)

Asset Class	Target Allocation	Long-Term Expected Rate of Return
Global Equity	63.2%	8.00%
Global Fixed Income	30.7%	5.50%
Real Assets	3.5%	6.20%
Diversifying Strategies	1.2%	2.75%
Cash	1.4%	0.50%

The sum of each target allocation times its long-term expected rate is 7.0%.

Discount Rate - The discount rate used to measure the total OPEB liability was 3.40%. The projection of cash flows used to determine the discount rate assumed that Employer contributions of $400,000 will be made in the next four years. Based on those assumptions, the retirement plan's fiduciary net position was not projected to be sufficient to make all projected future benefit payments of current plan members. For projected benefits that are covered by projected assets, the long-term expected rate was used to discount the projected benefits. From the year that benefit payments were not projected to be covered by the projected assets (the "depletion date"), projected benefits were discounted at a discount rate reflecting the Uniform Assumption for periods in which projected plan assets are not sufficient to make projected benefit payments. A single equivalent discount rate that yields the same present value of benefits is calculated. This discount rate is used to determine the Total OPEB Liability.

	Total OPEB Liability	Plan Fiduciary Net Position	Net OPEB Liability
Balances at December 31, 2017	$ 6,219,971	$ -	$ 6,219,971
Service cost	84,409	-	84,409
Interest	208,495	-	208,495
Contributions to OPEB Trust	-	520,000	(520,000)
Contributions paid from operations	-	344,330	(344,330)
Net investment income	-	(29,215)	29,215
Benefit payments	(344,330)	(344,330)	-
Administrative expense	-	(575)	575
Other changes	-	-	-
Net changes	(51,426)	490,210	(541,636)
Balances as December 31, 2018	$ 6,168,545	$ 490,210	$ 5,678,335

NOTE 9 - OTHER POST EMPLOYMENT BENEFITS (Continued)

Net OPEB Liability – Discount and Trend Rate Sensitivities – The following presents the net OPEB Liability (NOL) of the Road Commission, calculated using trend and discount rates 1% higher and lower than base assumptions:

Discount

	1% Decrease	Current Rate	1% Increase
Total OPEB Liability	$ 6,746,035	$ 6,168,545	$ 5,673,019
Plan Fiduciary Net Position	490,210	490,210	490,210
Net OPEB Liability	$ 6,255,825	$ 5,678,335	$ 5,182,809

Trend

	1% Decrease	Current Rate	1% Increase
Total OPEB Liability	$ 5,664,102	$ 6,168,545	$ 6,747,558
Plan Fiduciary Net Position	490,210	490,210	490,210
Net OPEB Liability	$ 5,173,892	$ 5,678,335	$ 6,257,348

OPEB Expense – Components of Road Commission's OPEB Expense for the fiscal year ending December 31, 2018 are as follows:

Service Cost	$ 84,409
Interest on Total OPEB Liability	208,495
Projected Earnings on OPEB Plan Investments	(18,184)
Investment Earnings (Gains)/Losses	9,480
Administrative Expenses	575
Other Changes in Fiduciary Net Position	-
Total OPEB Expense	$ 284,775

Deferred Outflows and Inflows of Resources Related to OPEB Plan

	Deferred Outflows of Resources	Deferred Inflows of Resources
Experience (Gains)/Losses	$ -	$ -
Changes of Assumptions	-	-
Investment Earnings (Gains)/Losses	37,919	-
Total	$ 37,919	$ -

NOTE 9 - OTHER POST EMPLOYMENT BENEFITS (Continued)

Amounts reported as deferred outflows of resources and deferred inflows of resources related to OPEB will be recognized in OPEB expense as follows:

Year Ended December 31:		
2019	$	9,480
2020		9,480
2021		9,480
2022		9,479

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.

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 $288,000. Additionally, the Road Commission remitted approximately $672,000 in payment of salt barn construction bonds.

NOTE 12- RESTATEMENT

	Governmental Activities
Beginning net position as previously stated at January 1, 2018	$ 22,439,552
Restatement of Net Position – for implementation of GASB 75 – OPEB cumulative effect	2,498,727
Beginning net position as restated at January 1, 2018	$ 24,938,279

Required Supplementary Information

Employee Retirement and Benefit Systems
Required Supplementary Information
Schedule of Changes in Pension Liability
For the Year Ended December 31, 2018

	2015	2016	2017	2018
Total pension liability				
Service cost	$ 137,944	$ 125,690	$ 171,132	$ 185,530
Interest	835,847	853,243	891,675	953,214
Changes in benefits	-	(5,403)	(10,166)	(4,710)
Difference between expected and actual experience	-	18,096	518,676	255,051
Changes in assumptions	-	588,192	-	-
Other changes	8,813	(5,518)	(7,172)	1,268
Benefit payments, including refund of member contributions	(738,956)	(792,294)	(794,192)	(810,376)
Net change in total pension liability	243,648	782,006	769,953	579,977
Total pension liability - beginning	10,431,989	10,675,637	11,457,643	12,227,596
Total pension liability - ending	$ 10,675,637	$ 11,457,643	$ 12,227,596	$ 12,807,573
Plan fiduciary net position				
Contributions - employer	$ 498,792	$ 508,482	$ 667,663	$ 1,065,147
Contributions - employee	77,134	39,017	121,913	68,858
Net investment income	(91,306)	662,026	838,774	(299,600)
Benefit payments, including refunds of member contributions	(738,956)	(792,294)	(794,192)	(810,376)
Administrative expense	(13,449)	(13,077)	(13,256)	(14,274)
Net change in plan fiduciary net position	(267,785)	404,154	820,902	9,755
Plan fiduciary net position - beginning	6,196,251	5,928,466	6,332,620	7,153,522
Plan fiduciary net position - ending	$ 5,928,466	$ 6,332,620	$ 7,153,522	$ 7,163,277
Net pension liability - ending	$ 4,747,171	$ 5,125,023	$ 5,074,074	$ 5,644,296
Plan fiduciary net position as a percentage of the total pension liability	56%	55%	59%	56%
Covered - employee payroll	$ 1,409,673	$ 1,256,307	$ 1,576,491	$ 1,668,776
Net pension liability as a percentage of covered-employee payroll	337%	408%	322%	338%

Employee Retirement and Benefit Systems
Required Supplementary Information
Schedule of Employer Contributions
For the Year Ended December 31, 2018

	2015	2016	2017	2018
Actuarially determined contribution	$ 376,152	$ 366,192	$ 437,460	$ 470,448
Contributions in relation to the actuarially determined contribution	(498,792)	(508,482)	(667,663)	(1,065,147)
Contribution deficiency (excess)	$ (122,640)	$ (142,290)	$ (230,203)	$ (594,699)
Covered - employee payroll	$ 1,399,784	$ 1,409,673	$ 1,256,307	$ 1,576,491
Contributions as a percentage of covered-employee payroll	36%	36%	53%	68%

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 administrative expense including inflation
Retirement age	In the 2017 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

Employee Retirement and Benefit Systems
Required Supplementary Information
Schedule of Changes in the OPEB Liability and Related Ratios
For the Year Ended December 31, 2018

	2018
Total OPEB Liability - Beginning of Year	$ 6,219,971
Service cost	84,409
Interest	208,495
Benefit payments	(344,330)
Total OPEB Liability - End of Year	6,168,545
Plan fiduciary net position	
Contributions to OPEB trust	520,000
Contributions paid from operations	344,330
Net investment income	(29,215)
Benefits payments, including refunds of member contributions	(344,330)
Administrative expense	(575)
Net change in plan fiduciary net position	490,210
Plan fiduciary net position - Beginning of Year	-
Plan fiduciary net position - End of Year	490,210
Net OPEB liability - End of Year	$ 5,678,335
Plan fiduciary net position as a percentage of the total OPEB liability	7.9%
Covered Payroll	Not available
Net OPEB liability as a percentage of covered payroll	Not available
Schedule of Employer Contributions:	
Normal Cost	$ 84,409
Interest Cost	41,127
Amortization of unfunded liability	1,125,202
Actuarially determined employer contribution	1,250,738
Employer contribution	(864,330)
Contribution deficiency/(excess)	$ 386,408
Covered Payroll	Not available
Contribution as percentage of covered payroll	Not available

Notes to Schedule:

Actuarially determined contribution rates are calculated as of December 31, 2018.

Methods and assumptions used to determine contribution rates:

Actuarial cost method	Entry age normal
Asset valuation method	5-years smoothed market
Discount rate	3.40%
Salary increases	3.50%
Investment rate of return	7.00%
PA 202 discount rate	3.40%
Mortality rate	RPH -2014 adjusted to 2006 total data set with MP-2018 mortality improvement scale

Employee Retirement and Benefit Systems
Required Supplementary Information
State of Michigan Public Acts 530 and 202 Information
For the Year Ended December 31, 2018

Financial Information	
Assets (Fiduciary Net Position)	$ 490,210
Liabilities (Total OPEB Liability)	6,168,545
Funded ratio for the plan year	7.90%
Actuarially recommended contribution (ARC)	1,250,738
Is ARC calculated in compliance with No. Letter 2018-3?	Yes

Membership	
Active members	16
Retirees and beneficiaries	37
Premiums paid on behalf of the retirants	344,330

Actuarial Assumptions	
Actuarially assumed rate of investment return	7.00%
Discount rate	3.40%
Amortization method used for funding unfunded liability	Level dollar
Amortization period used for funding unfunded liability	6
Is each division closed to new employees	Yes
Healthcare trend assumption	PA 202 uniform trend

Uniform Assumptions	
Actuarial value of assets using uniform assumptions	$ 490,210
Actuarial accrued liability using uniform assumptions	6,168,545
Funded ratio using uniform assumptions	7.90%
Actuarially determined contribution (ADC) using uniform assumptions	1,250,738

Information for Summary Report (minimum required contribution)	
Retiree insurance premiums for the year	344,330
Normal cost as a percent of covered payroll	84,409
Covered payroll for employees hired after June 30, 2018	Not available
Normal cost for employees hired after June 30, 2018	Not available
Minimum required contribution under PA 202	344,330

Employee Retirement and Benefit Systems
Required Supplementary Information
Assumptions and Methods for Calculation of Actuarially Determined Contributions
For the Year Ended December 31, 2018

Valuation Date	December 31, 2018
Actuarial Methods	
Cost method	Entry Age Normal (level percentage of compensation)
Amortization method	Level dollar
Asset valuation method	Equal to market value of assets

Actuarial Assumptions

Discount rate - 3.40% for December 31, 2018 liability and 2019 contribution
Rationale - Consistent with Uniform Assumptions under Public Act 202 for unfunded plans

Salary scale - 3.50%
Rationale - Consistent with Uniform Assumptions under Public Act 202

Return on plan assets - 7.00%
Rationale - Consistent with plan investment experience

Mortality rates - RPH-2014 adjusted to 2006 Total Data Set with MP-2018 mortality improvement
Rationale - Contemporary table consistent with Uniform Assumptions under Public Act 202

Turnover rates - None
Rationale - Small group

Retirement rates - 100% at first eligibility
Rationale - Consistent with experience

Utilization - 100% of eligible employees will elect coverage at retirement
Rationale - Benefits are provided at no cost or low cost to retirees

Marital status - not applicable
Rationale -Future retirees are not eligible for employer paid spouse coverage

Pre-65 medical claims cost - See monthly rates below
Rationale - Actual age-graded premiums in effect as of January 1, 2019

Blue Care Network HRA		
Age	Per Person	
55	$	680.64
56		712.08
57		743.82
58		777.70
59		794.49
60		828.37
61		857.67
62		876.89
63		901.01
64		915.65

Pre-65 medical claims cost - See monthly rates below
Rationale - Actual premiums in effect as of January 1, 2019

Coverage	Per Person	
Blue Care Network	$	395.82
Humana		337.00

HRA load - $4,500 per person pre-65
Rationale - Maximum deductible reimbursement for pre-65 retirees and spouses

Implicit Subsidy - Not applicable
Rationale - Pre-65 premiums are age-graded so there is no implicit subsidy

Medical trend
Pre-65 - 8.5% graded down to 4.5% by 0.25% per year
Post-65 - 7.5% graded down to 4.5% by 0.25% per year
Rationale - Consistent with Uniform Assumptions under Pubic Act 202

40% excise tax on "high cost" group health plan - Premiums when aggregated are projected to exceed the 2022 thresholds; The thresholds were indexed by CPI plus 1.0% in 2023 and CPI only beginning in 2024; The CPI is assumed to be 3.0% in 2023 and following

Data Collection
Date and form of data - All personnel and asset data was prepared by the plan sponsor or a representative and was generally relied upon as being correct and complete without audit by Watkins Ross

Assumption changes since prior valuation
- First valuation prepared by Watkins Ross

Employee Retirement and Benefit Systems
Required Supplementary Information
Schedule of Amortization of Deferred Outflows/Inflows of Resources
For the Year Ended December 31, 2018

Schedule of Difference between Actual and Expected Experience

Year	Difference between actual and expected experience	Recognition period (Years)	Amount Recognized in Year Ended December 31, 2019	2020	2021	2022	2023+	Deferred Outflows of Resources	Deferred Inflows of Resources
2018	-	1.45	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Net recognized in OPEB expense			$ -	$ -	$ -	$ -	$ -	$ -	$ -

Schedule of Changes in Assumptions

Year	Changes in assumptions	Recognition period (Years)	Amount Recognized in Year Ended December 31, 2019	2020	2021	2022	2023+	Deferred Outflows of Resources	Deferred Inflows of Resources
2018	-	1.45	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Net recognized in OPEB expense			$ -	$ -	$ -	$ -	$ -	$ -	$ -

Schedule of Differences between Projected and Actual Earnings on OPEB Assets

Year	Difference between projected and actual earnings on OPEB assets	Recognition period (Years)	Amount Recognized in Year Ended December 31, 2019	2020	2021	2022	2023+	Deferred Outflows of Resources	Deferred Inflows of Resources
2018	37,918	5	$ 9,480	$ 9,480	$ 9,480	$ 9,479	$ -	$ 37,919	$ -
Net recognized in OPEB expense			$ 9,480	$ 9,480	$ 9,480	$ 9,479	$ -	$ 37,919	$ -

Total Deferred Outflow/(Inflow) of Resources

	Amount Recognized in Year Ended December 31, 2019	2020	2021	2022	2023+
Total Deferred Outflow/(Inflow) of Resources	$ 9,480	$ 9,480	$ 9,480	$ 9,479	$ -

Employee Retirement and Benefit Systems
Required Supplementary Information
Summary of Plan Provisions
For the Year Ended December 31, 2018

Plan name	Otsego County Road Commission Retiree Health Plan
Eligibility requirements	Hired prior to December 31, 2008 and retire with at least 20 years of employment and age 55 years
Benefits	
Retirement prior to 2011	Lifetime health coverage for the retiree and spouse
Retirement from 2011 through 2015	
Pre-65	Coverage for the retiree and spouse and annual reimbursement of deductible up to $4,500 per person
Post-65	Employer paid supplemental coverage for the retiree and spouse capped at $350 per month per person
Retirement after 1/1/2016	
Pre-65	Coverage for the retiree and annual reimbursement of deductible up to $4,500
Post-65	None
Retiree contribution	Balance of premium not paid by the employer
Changes since prior valuation	First valuation prepared by Watkins Ross

Required Supplementary Information
Budgetary Comparison Schedule
Statement of Revenues - Budget and Actual
For the Year Ended December 31, 2018

	Original Budget	Final Amended Budget	Actual	Variance Favorable (Unfavorable)
Taxes	$ 1,000,000	$ 1,100,000	$ 1,056,096	$ (43,904)
Licenses and Permits	71,000	71,000	214,102	143,102
Federal Sources				
Surface Transportation Program	800,000	1,000,000	654,441	(345,559)
State Sources				
Michigan Transportation Fund				
Engineering	10,000	10,000	10,000	-
Allocation	4,600,000	5,140,000	4,769,244	(370,756)
Snow Removal	260,000	320,000	315,152	(4,848)
Urban Road	499,000	560,000	527,847	(32,153)
Forest Road	86,000	86,000	85,107	(893)
Other	350,000	1,100,000	1,284,206	184,206
Contributions from Local Units				
City and Village	-	25,000	15,926	(9,074)
Townships	800,000	800,000	589,618	(210,382)
Charges for Services				
Trunkline Maintenance	1,400,000	1,420,000	1,325,778	(94,222)
Trunkline Nonmaintenance	520,000	600,000	494,722	(105,278)
Salvage Sales	7,500	7,500	5,901	(1,599)
Other	-	175,000	169,624	(5,376)
Interest Earnings and Rent	45,000	95,000	91,100	(3,900)
Other Revenue				
Gain (Loss) on Disposal	15,000	78,000	77,539	(461)
Private Contributions and Other	65,075	70,075	54,185	(15,890)
Other Financing Sources	510,000	200,000	162,056	(37,944)
Total Revenues	$ 11,038,575	$ 12,857,575	$ 11,902,644	$ (954,931)

Required Supplementary Information
Budgetary Comparison Schedule
Statement of Expenditures - Budget and Actual
For the Year Ended December 31, 2018

	Original Budget	Final Amended Budget	Actual	Variance Favorable (Unfavorable)
Primary Road				
Preservation - Structural Improvements	$ 2,702,000	$ 3,300,000	$ 3,361,583	$ (61,583)
Maintenance	1,487,100	1,587,100	1,606,552	(19,452)
Local Road				
Preservation - Structural Improvements	1,000,000	500,000	276,891	223,109
Maintenance	2,018,100	1,869,100	2,050,406	(181,306)
Trunkline Maintenance	1,400,000	1,400,000	1,325,778	74,222
Trunkline Nonmaintenance	350,000	570,000	494,722	75,278
Administrative Expense - Net	625,000	800,000	744,349	55,651
Equipment Expense - Net	505,000	290,000	292,362	(2,362)
Capital Outlay - Net	250,000	210,000	229,031	(19,031)
Debt Service				
Principal	500,000	1,300,000	1,133,134	166,866
Interest	70,000	70,000	63,236	6,764
Total Expenditures	10,907,200	11,896,200	$ 11,578,044	$ 318,156
Fund Balance - January 1, 2018	4,533,445	4,533,445		
Total Budget	$ 15,440,645	$ 16,429,645		

Other Information

Analysis of Changes in Fund Balance
For the Year Ended December 31, 2018

	Primary Road Fund	Local Road Fund	County Road Commission	Total
Total Revenues	$ 6,029,942	$ 2,435,701	$ 3,437,001	$ 11,902,644
Total Expenditures	5,557,664	2,676,087	3,344,293	11,578,044
Excess of Revenues Over (Under) Expenditures	472,278	(240,386)	92,708	324,600
Optional Transfers and Adjustments	(240,386)	240,386	-	-
Fund Balance - January 1, 2018	-	-	4,533,445	4,533,445
Fund Balance - December 31, 2018	$ 231,892	$ -	$ 4,626,153	$ 4,858,045

Analysis of Revenues
For the Year Ended December 31, 2018

	Primary Road Fund	Local Road Fund	County Road Commission	Total
Taxes	$ -	$ -	$ 1,056,096	$ 1,056,096
Licenses and Permits	214,102	-	-	214,102
Federal Sources				
Surface Transportation Program	654,441	-	-	654,441
State Sources				
Michigan Transportation Fund				
Engineering	6,207	3,793	-	10,000
Allocation	2,960,496	1,808,748	-	4,769,244
Snow Removal	-	315,152	-	315,152
Urban Road	362,883	164,964	-	527,847
Forest Road	85,107	-	-	85,107
Other	1,284,206	-	-	1,284,206
Contributions from Local Units				
City and Village	-	15,926	-	15,926
Townships	462,500	127,118	-	589,618
Charges for Services				
Trunkline Maintenance	-	-	1,325,778	1,325,778
Trunkline Nonmaintenance	-	-	494,722	494,722
Salvage Sales	-	-	5,901	5,901
Other	-	-	169,624	169,624
Interest and Rents				
Interest Earnings	-	-	65,044	65,044
Property Rentals	-	-	26,056	26,056
Other Revenue				
Gain on Equipment Disposals	-	-	77,539	77,539
Other	-	-	54,185	54,185
Other Financing Sources				
Installment Purchases	-	-	162,056	162,056
Total Revenues	$ 6,029,942	$ 2,435,701	$ 3,437,001	$ 11,902,644

Analysis of Expenditures
For the Year Ended December 31, 2018

	Primary Road Fund	Local Road Fund	County Road Commission	Total
Primary Road				
Preservation - Structural Improvements	$ 3,361,583	$ -	$ -	$ 3,361,583
Maintenance	1,606,552	-	-	1,606,552
Local Road				
Preservation - Structural Improvements	-	276,891	-	276,891
Maintenance	-	2,050,406	-	2,050,406
Trunkline Maintenance	-	-	1,325,778	1,325,778
Trunkline Nonmaintenance	-	-	494,722	494,722
Administrative Expense - Net	506,896	237,453	-	744,349
Equipment Expense - Net	82,633	111,337	98,392	292,362
Capital Outlay - Net	-	-	229,031	229,031
Debt Service				
Debt Principal Payments	-	-	1,133,134	1,133,134
Interest Expense	-	-	63,236	63,236
Total Expenditures	$ 5,557,664	$ 2,676,087	$ 3,344,293	$ 11,578,044

Report on Compliance

ANDERSON, TACKMAN & COMPANY, PLC
CERTIFIED PUBLIC ACCOUNTANTS

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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*

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, major fund and the aggregate remaining fund information of the Otsego County Road Commission (a component unit of Otsego County, Michigan), as of and for the year ended December 31, 2018, 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 May 21, 2019.

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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Board of County Road Commissioners
Otsego County Road Commission

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 2018-001 and 2018-002.

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 2018-003.

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

May 21, 2019

Significant Deficiency - Internal Control

<u>Preparation of the Financial Statements in Accordance with Generally Accepted Accounting Principles</u> ***Finding 2018-001***

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

<u>Segregation of Duties</u> ***Finding 2018-002***

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

<u>Expenditures in Excess of Appropriations—Budgetary Funds</u> ***Finding 2018-003***

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 2018 General Appropriations Act (budget) provided for expenditures of the General Fund to be controlled to the activity level. As detailed, actual 2018 expenditures exceeded the board's approved budget allocations for some general fund activities.

During the fiscal year ended December 31, 2018, expenditures were incurred in excess of amounts appropriated in the amended budgets for the General Fund as listed on page 44 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 projects 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

ANDERSON, TACKMAN & COMPANY, PLC
CERTIFIED PUBLIC ACCOUNTANTS

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MICHIGAN & WISCONSIN

COMMUNICATION WITH THOSE CHARGED WITH GOVERNANCE

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

We have audited the financial statements of the governmental activities, major fund and the aggregate remaining fund information of the Otsego County Road Commission (a component unit of Otsego County, Michigan) for the year ended December 31, 2018, and have issued our reports thereon dated May 21, 2019. Professional standards require that we provide you with information about our responsibilities under generally accepted auditing standards and *Government Auditing Standards* as well as certain information related to the planned scope and timing of our audit. Professional standards also require that we communicate to you the following information related to our audit.

Our Responsibility under U.S. Generally Accepted Auditing Standards and *Government Auditing Standards*

As stated in our engagement letter dated March 15, 2019, our responsibility, as described by professional standards, is to express opinions about whether the financial statements prepared by management with your oversight are fairly presented, in all material respects, in conformity with U.S. generally accepted accounting principles. Our audit of the financial statements does not relieve you or management of your responsibilities.

As part of our audit, we considered the internal control of the Otsego County Road Commission. Such considerations were solely for the purpose of determining our 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, we performed tests of the Otsego County Road Commission's compliance with certain provisions of laws, regulations, contracts, and grants. However, the objective of our tests was not to provide an opinion on compliance with such provisions.

Generally accepted accounting principles provide for certain required supplementary information (RSI) to supplement the basic financial statements. Our responsibility with respect to the management's discussion and analysis, schedule of funding progress, and budgetary comparison schedules, which supplement the basic financial statements, is to apply certain limited procedures in accordance with generally accepted auditing standards. However, the RSI will not be audited and, because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance, we will not express an opinion or provide any assurance on the RSI.

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We have been engaged to report on other schedules which accompany the financial statements but are not RSI. Our responsibility for this other information, as described by professional standards, is to evaluate the presentation of the other information in relation to the financial statements as a whole and to report on whether the other information is fairly stated, in all material respects, in relation to the financial statements as a whole.

Planned Scope and Timing of the Audit

We performed the audit according to the planned scope and timing previously communicated to you in your March 2019 Board Packet.

Significant Audit Findings

Management is responsible for the selection and use of appropriate accounting policies. In accordance with the terms of our engagement letter, we will advise management about the appropriateness of accounting policies and their application. The significant accounting policies used by the Otsego County Road Commission are described in Note 1 to the financial statements. One new accounting policy was adopted regarding GASB Statement Number 75 and the application of existing policies was not changed during the fiscal year. We noted no transactions entered into by the Road Commission during the year for which there is a lack of authoritative guidance or consensus. There are no significant transactions that have been recognized in the financial statements in a different period than when the transaction occurred.

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

- Management's estimate of the depreciation expense is based on estimated lives. We evaluated the key factors and assumptions used to develop the estimate to determining that it is reasonable in relation to the financial statements taken as a whole.

- Management's estimate of the vested employee benefits is based on current hourly rates and policies.

- Management's estimate of the amounts for OPEB liabilities and Pension liabilities and investments were based on various assumptions regarding life expectancies, inflation, premium increases, and investment rates.

The financial statement disclosures are neutral, consistent and clear.

Difficulties Encountered in Performing the Audit

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

Corrected and Uncorrected Misstatements

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are clearly trivial, and communicate them to the appropriate level of management. In addition, there were no misstatements detected as a result of audit procedures and corrected by management that were material, either individually or in the aggregate, to the financial statements taken as a whole. A copy of any adjustments are available from management.

Disagreement with Management

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

Management Representations

We have requested certain representations from management that are included in the management representation letter dated May 21, 2019.

Management 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 auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us as to determine the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Other Audit findings or Issues

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

Comments and Recommendations

Excess Expenditures Over Appropriations (Prior)

Public Act 621 of 1978, Section 18(1), as amended, provides that a local unit of government shall not incur expenditures in excess of the amount appropriated. In the body of the financial statements, the Road Commission's actual expenditures were in excess of amounts appropriated for certain line items as indicated on the Statement of Expenditures – Budget and Actual.

Status: Some items were over due to unanticipated billings after year end.

Parts Management (Prior)

HMS software utilized by the Road Commission has a parts management module which would assist in the purchasing, inventory, and usage reporting of parts and other nonstock inventory items. Implementation of this software would increase internal control over parts management and eliminate redundant inventory procedures currently in practice. We strongly recommend the implementation of inventory software.

We reviewed parts and other material for obsolete items. Our procedures indicated that approximately 80 percent of items have not changed over a two year period which may indicate items should be scrapped or charge out processes are incomplete or pricing errors. The Road Commission should conduct a review of parts and handling costs and reduce theft risk.

Status: Unchanged.

Other Postemployment Benefits (Prior)

In June 2015, the Governmental Accounting Standards Board issued Statement Number 75 – "Financial Reporting for Postemployment Benefits Other Than Pensions." The standard addresses how to measure long-term liabilities and annual costs of Other Postemployment Benefits (OPEB) for the purposes of reporting them in the financial statements. The standard does not apply to how a governmental unit should fund future OPEB payments, however. The standard makes significant changes which will increase the liability and may adjust annual OPEB expense as well. A net OPEB liability will be reported in the employer's statement of net position which could amount to a significant increase than past amounts reported. The OPEB expense will also be significantly more volatile, since there will likely be two sets of calculations for expense and funding. Additionally, changes in methods and assumptions used in the actuarial calculations, more extensive footnote disclosures and required supplementary information will be needed.

The standard is effective for fiscal years beginning after June 15, 2017. We encourage the Board and management to review the provisions of this new standard and anticipate its effect on the financial reporting process.

Status: Corrected.

Single Approach for Reporting Leases (Prior Year)

The Governmental Accounting Standards Board (GASB) issued guidance that establishes a single approach to accounting for and reporting leases by state and local governments. The single approach is based on the principle that leases are financing of the right to use an underlying asset.

GASB Statement No. 87, *Leases*, provides guidance for lease contracts for nonfinancial assets – including vehicles heavy equipment, and buildings – but excludes nonexchange transactions, including donated assets, and leases of intangible assets.

Under the new Statement a lessee government is required to recognize (1) a lease liability and (2) an intangible asset representing the lessee's right to use the leased asset. A lessor government is required to recognize (1) a lease receivable and (2) a deferred inflow of resources. A lessor will continue to report the leased asset in its financial statements.

A lease also will report the following in its financial statements:

- Amortization expense for using the lease asset (similar to depreciation) over the shorter of the term of the lease or the useful life of the underlying asset.
- Interest expense on the lease liability
- Note disclosures about the lease, including a general description of the leasing arrangement, the amount of the lease assets recognized, and a schedule of future lease payments to be made.

Limited exceptions to the single-approach guidance are provided for:

- Short-term leases, defined as lasting a maximum of 12 months at inception, including any options to extend.
- Financial purchases
- Certain regulated leases, such as between municipal airports and air carriers.

The full text of Statement 87 is available on the GASB website, www.gasb.org.

Status: To be implemented by 2020.

Prepaid Items

Although the ledger contains twelve months of financial activity, the Board should enact accounting procedures to identify prepaid expense items such as health insurance and liability coverage. Amortization of these costs should be posted to proper periods of coverage in accordance with accounting principles.

Employee Withholding Forms

Due to the significant changes recently enacted with the 2018 Tax Cuts and Jobs Act, the Board should consider having employees update their Form W4 – Employee's Withholding Allowance Certificate. Tax rate, credit and deduction changes have impacted federal income tax withheld from gross pay.

Public Act 202 of 2017

Public Act 202 of 2017 required local units of government with employee retiree healthcare plans to provide adequate funding. The Road Commission established a retiree healthcare program which is not adequately funded at 40% of the actuarially determined total liability. The Road Commission is not in compliance with the statute and must receive an approved waiver from the Michigan Department of Treasury or adequately fund this plan.

GASB 83 – Certain Asset Retirement Obligations
Effective 06/15/19 (your FY 2019)

This statement addresses accounting and financial reporting for certain asset retirement obligations—legally enforceable liabilities associated with the retirement of a tangible capital assets.

GASB 84 – Fiduciary Activities
Effective 12/15/2019 (your FY 2019)

This standard establishes new criteria for determining how to report fiduciary activities in governmental financial statements. The focus is on whether the government is controlling the assets, and who the beneficiaries are. Under this revised standard, certain activities previously reported in agency funds may be reclassified in future periods. Due to the number of specific factors to consider, management should assess the degree to which this standard may impact the Road Commission.

Other Matters

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

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

Conclusion

We would like to express our appreciation, as well as that of our staff for the excellent cooperation we received while performing the audit. If we can be of assistance, please contact us.

This information is intended solely for the use of the Otsego County Road Commission, the cognizant audit agencies and other federal and state agencies, and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Anderson Tackman & Co. PLC

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

May 21, 2019