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August 9, 2016

To the Board of Trustees
Township of Scio

We have audited the financial statements of the Township of Scio (the “Township”) as of and for the year ended March 31, 2016 and have issued our report thereon dated August 9, 2016. Professional standards require that we provide you with the following information related to our audit, which is divided into the following sections:

Section I - Internal Control Related Matters Identified in an Audit

Section II - Required Communications with Those Charged with Governance

Section III - Legislative and Informational Items

Section I includes any deficiencies we observed in the Township’s accounting principles or internal control that we believe are significant. Current auditing standards require us to formally communicate annually matters we note about the Township’s accounting policies and internal control.

Section II includes information that current auditing standards require independent auditors to communicate to those individuals charged with governance. We will report this information annually to the board of trustees of the Township.

Section III contains updated legislative and informational items that we believe will be of interest to you.

We would like to take this opportunity to thank the Township’s staff for the cooperation and courtesy extended to us during our audit. Their assistance and professionalism were invaluable.

This report is intended solely for the use of the board of trustees and management of the Township and is not intended to be and should not be used by anyone other than these specified parties.

We welcome any questions you may have regarding the following communications and we would be willing to discuss any of these or other questions that you might have at your convenience.

Very truly yours,

Plante & Moran, PLLC

Michael J. Swartz

Section I - Internal Control Related Matters Identified in an Audit

In planning and performing our audit of the financial statements of the Township as of and for the year ended March 31, 2016, in accordance with auditing standards generally accepted in the United States of America, we considered the Township's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Township's internal control. Accordingly, we do not express an opinion on the effectiveness of the Township's internal control.

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

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.

We consider the following deficiency in the Township's internal control to be a material weakness:

- **Review of Project Agreements** - During our audit procedures, we found that the Township entered into an agreement regarding the Liberty Road Pump Station, noting the City of Ann Arbor holds 15 percent ownership of the asset. This agreement between the Township and the City of Ann Arbor was not initially identified by the Township and so they recorded the entire asset, resulting in an overstatement of approximately $141,000 in sewer fund capital assets. This error had no effect on net position. This lack of thorough review of project agreements could lead to a material misstatement of the financial statements. This is a similar finding from the prior year.

Section II - Required Communications with Those Charged with Governance

<u>Our Responsibility Under U.S. Generally Accepted Auditing Standards</u>

As stated in our engagement letter dated May 24, 2016, our responsibility, as described by professional standards, is to express an opinion 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. Our responsibility is to plan and perform the audit to obtain reasonable, but not absolute, assurance that the financial statements are free of material misstatement.

As part of our audit, we considered the internal control of the Township. Such considerations were solely for the purpose of determining our audit procedures and not to provide any assurance concerning such internal control.

We are responsible for communicating significant matters related to the audit that are, in our professional judgment, relevant to your responsibilities in overseeing the financial reporting process. However, we are not required to design procedures specifically to identify such matters.

<u>Planned Scope and Timing of the Audit</u>

We performed the audit according to the planned scope and timing previously communicated to you in our meeting about planning matters on June 2, 2016.

<u>Significant Audit Findings</u>

Qualitative Aspects of Accounting Practices

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 Township are described in Note 1 to the financial statements. As described in Note 12, the Township changed accounting policies related to *Accounting and Financial Reporting for Pensions*, GASB Statement No. 68. Accordingly, the accounting change has been retrospectively applied to prior periods presented as if the policy had always been used.

We noted no transactions entered into by the Township 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.

Section II - Required Communications with Those Charged with Governance (Continued)

The most sensitive estimates affecting the basic financial statements were unbilled water and sewer receivables, the calculation of the net other postemployment benefits liability (i.e., retiree health care), and the calculation of the net pension liability. The unbilled water and sewer receivable estimate is based on prior performance. Management's estimate of the net other pension liability is based on assumptions used in the actuarial valuation. The net other postemployment benefits liability is based on the alternative measurement method prepared by the Township and permitted by GASB Statement No. 45. Certain assumptions are used to calculate the estimated long-term cost of retiree healthcare benefits and it is management's responsibility to assess whether the assumptions made are reasonable. We evaluated the key factors and assumptions used to develop these estimates to determine that they are reasonable in relation to the basic financial statements taken as a whole.

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

Difficulties Encountered in Performing the Audit

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

Disagreements with Management

For the purpose of this letter, professional standards define a disagreement with management as 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.

Corrected and Uncorrected Misstatements

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management. We identified an immaterial misstatement related to the recording of long-term assets and current assets for the City Ann Arbor's portion of the Liberty Road Pump Station. Management has corrected this misstatement.

Significant Findings or Issues

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, business conditions affecting the Township, and business plans and strategies that may affect the risks of material misstatement with management each year prior to our retention as the Township's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition of our retention.

Management Representations

We have requested certain representations from management that are included in the management representation letter dated August 9, 2016.

Section II - Required Communications with Those Charged with Governance (Continued)

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 Township'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 to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Other Information in Documents Containing Audited Financial Statements

Our responsibility for other information in documents containing the Township's financial statements and report does not extend beyond the financial statements. We do not have an obligation to determine whether or not such other information is properly stated. However, we read the management's discussion and analysis and nothing came to our attention that caused us to believe that such information, or its manner of presentation, is materially inconsistent with the information or manner of its presentation appearing in the financial statements.

Section III - Legislative and Informational Items

New Other Postemployment Benefits Standards (Retiree Healthcare Obligations)

In June 2015, the Governmental Accounting Standards Board (GASB) issued a new standard addressing accounting and financial reporting by state and local governments for postemployment benefits other than pensions (OPEB, which refers to retiree health care). GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, addresses accounting and reporting by employer governments that provide OPEB benefits to their employees.

The Township will, after adoption of GASB Statement No. 75, recognize on the face of the financial statements its net OPEB liability. The Township is currently evaluating the impact these standards will have on the financial statements when adopted. GASB Statement No. 75 is effective for fiscal years beginning after June 15, 2017 (the Township's fiscal year 2019).

A pro forma of how this is expected to impact the Township's government-wide net position is shown below:

	As Currently Reported	With Unfunded Health Care
Net position:		
Net investment in capital assets	$ 36,042,184	$ 36,042,184
Restricted	30,024,376	30,024,376
Unrestricted	7,260,394	6,315,707
Total net position	$ 73,326,954	$ 72,382,267

This pro forma indicates that Township will likely still have a positive unrestricted net position. The fact that the unrestricted portion is still positive indicates that legacy costs earned to date have already been fully funded.

Section III - Legislative and Informational Items
(Continued)

Revenue Sharing

The FY 2017 governor's budget recommendation includes $1.3 billion for revenue sharing broken down as follows:

Description	FY 2016 Budget	FY 2016 Forecasted Actual	Governor's 2017 Recommended Budget
Constitutionally required payments	$783.8 M	$752.1 M	$781.5 M
CVTRS	243.0 M	243.0 M	243.0 M
CVTRS - One-time payments	5.8 M	5.8 M	0 M
County revenue sharing	171.8 M	171.8 M	172.2 M
County incentive program	42.9 M	42.9 M	43.0 M
Fiscally distressed community grants	5.0 M	5.0 M	5.0 M
Competitive grants			11.0 M
Total	$1,252.3 M	$1,220.6 M	$1,255.7

It should be noted that the governor's budget notes a 3.9 percent increase in constitutional revenue sharing, but as you can see above, the 2016 budget included $783.8 million, which never materialized and was adjusted downward as sales tax revenue failed to come in as projected. As a result, the 3.9 percent increase is comparing the lower estimate of $752.1 million to the 2017 budget of $781.5 million. If you compared the 2017 budget to the 2016 budget, there is actually a decrease in this line item. The FY 2017 budget also includes the "City, Village, and Township Revenue Sharing" (CVTRS), which was established in FY 2015, and that number remains flat at $243 million. Each community's overall increase will vary as each has a different mix of constitutional and CVTRS.

In order to receive the CVTRS payments in FY 2017, qualified local units will once again need to comply with the same best practices as they did last year:

- A citizen's guide to local finances with disclosure of unfunded liabilities
- Performance dashboard
- Debt service report
- Two-year budget projection

The "one-time" additional CVTRS payments that existed in the 2015 and 2016 budgets are not in the governor's 2017 budget. If the payments are not reinstated in the final 2017 budget, approximately 100 townships will no longer benefit from these CVTRS payments, leaving only 34 of the State's 1,240 townships in the CVTRS allocation.

Personal Property Tax

In August 2014, Michigan voters put the last piece of personal property tax reform in place. As a result, personal property taxes will be reduced in two respects:

1. Small Taxpayer Exemption Loss (STEL) - Small taxpayers with total personal property within a taxing unit valued at less than $80,000 are able to sign an affidavit exempting this personal property from taxation. This exemption began with the 2014 tax billings.

2. Beginning with 2016 tax filings, an affidavit can be filed to exempt eligible property used in a manufacturing process that is purchased either prior to 2006 or after December 31, 2012.

For 2014 and 2015, all communities were qualified to be reimbursed for losses related to debt millages and lost TIF capture arising from the STEL. Only cities were reimbursed for the balance of the Small Taxpayer Exemption Loss. However, for 2016, the legislation is generally intended to fully reimburse all local units of government for revenue losses that result from all exempt personal property.

The changes include creation of a new Local Community Stabilization Authority (LCSA) that will receive money from two sources:

- <u>Use Tax</u>: The legislation includes specific amounts of the use tax that will be diverted from the State's General Fund to the new LCSA; and

- <u>Essential Services Assessment</u>: Manufacturers will pay a "local community essential services assessment" to the LCSA based on the value of their exempt manufacturing property. The rate is set at 2.4 mills for a property's first five years; then 1.25 mills for the next five; then 0.9 mills thereafter.

Please keep in mind that if these two sources do not generate sufficient revenue for 100 percent of the losses, there could be a potential for something less than full reimbursement.

Local Community Stabilization Authority Revenue - As noted above, eligible communities began receiving reimbursements for certain lost personal property taxes. The state agency making those reimbursements is the Local Community Stabilization Authority (LCSA). These reimbursements should not be reported on the financial statements with property taxes; instead, they should be included with other intergovernmental revenue from the State (state-shared revenue, grants, and other). The State has created a new account number for the revenue, 573, and titled it "Local Community Stabilization Share Appropriation." As always, communities should follow the State's guidance related to the uniform chart of accounts.

The State Department of Treasury will compute the reimbursements and is scheduled to make the payments by October 20 of each year. The State will compare the total current year taxable value of commercial and industrial personal property to the value as of 2013 (the year before PPT reform).