

MEMO - COMMUNICATION WITH THOSE CHARGED WITH GOVERNANCE

To: Board of Finance, Town of Haddam, Connecticut
From: Vanessa E. Rossitto, CPA, Audit Partner
Blum Shapiro & Company, P.C.
Date: July 24, 2017
Re: Auditing Standard No. 114, "The Auditor's Communication with Those Charged with Governance" regarding audit of Town of Haddam, Connecticut

We are engaged to audit the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the Town of Haddam, Connecticut for the year ended June 30, 2017. Professional standards require that we provide you with the following information related to our audit. We would also appreciate the opportunity to meet with you to discuss this information further since a two-way dialogue can provide valuable information for the audit process.

Our responsibilities under Auditing Standards Generally Accepted in the United States of America, Government Auditing Standards and the Connecticut State Single Audit Act.

As stated in our engagement letter dated May 3, 2017, our responsibility, as described by professional standards, is to express opinions as to whether the financial statements, prepared by management with your oversight are fairly presented, in all material respects, in conformity with accounting principles generally accepted in the United States of America. Our audit of the financial statements does not relieve those charged with governance or management of their responsibilities.

In planning and performing our audit, we will consider the Town of Haddam, Connecticut's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and not to provide assurance on the internal control over financial reporting. We will also consider internal control over compliance with requirements that could have a direct and material effect on a major federal or state program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with the Uniform Guidance and the Connecticut State Single Audit Act.

As part of obtaining reasonable assurance about whether the Town of Haddam, Connecticut's financial statements are free of material misstatement, we will perform tests of its compliance with certain provisions of laws, regulations, contracts, and grants. However, providing an opinion on compliance with those provisions is not an objective of our audit. Also in accordance with the Uniform Guidance, we will examine, on a test basis, evidence about the Town of Haddam, Connecticut's compliance with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) Compliance Supplement applicable to each of its major federal programs for the purpose of expressing an opinion on the Town of Haddam, Connecticut's compliance with those requirements. While our audit will provide a reasonable basis for our opinion, it will not provide a legal determination on the Town of Haddam, Connecticut's compliance with those requirements.

Because of the inherent limitations of an audit, combined with the inherent limitations of internal control, and because we will not perform an examination of all transactions, there is a risk that material

misstatements or noncompliance may exist and not be detected by us, even though the audit is properly planned and performed in accordance with auditing standards generally accepted in the United States of America and *Government Auditing Standards*.

Planned Scope, Timing of the Audit and Other

An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements; therefore, our audit will involve judgment about the number of transactions to be examined and the areas to be tested.

Our audit will include obtaining an understanding of the entity and its environment, including internal control, sufficient to assess the risks of material misstatement of the financial statements and to design the nature, timing, and extent of further audit procedures. Material misstatements may result from (1) errors, (2) fraudulent financial reporting, (3) misappropriation of assets, or (4) violations of laws or governmental regulations that are attributable to the entity or to acts by management or employees acting on behalf of the entity. We will generally communicate our significant findings at the conclusion of our audit. However, some matters could be communicated sooner, particularly if significant difficulties are encountered during the audit where assistance is needed to overcome the difficulties or if the difficulties may lead to a modified opinion. We will also communicate any internal control related matters that are required to be communicated under professional standards.

Nonattest Services

In addition to above services, we will also assist in perform certain nonattest services. These services do not constitute an audit under Government Auditing Standards. The services are as follows:

- preparing a draft of the financial statements,
- preparing a draft of the schedule of expenditures of state financial assistance (SESFA),

Management agrees to oversee the nonattest services by designating an individual, preferably from senior management, with suitable skill, knowledge, or experience; evaluate the adequacy and results of those services; and accept responsibility for them.

Independence

There are no relationships between any of our representatives and the Town that in our professional judgment impair our independence.

Responsibilities under Auditing Standards Generally Accepted in the United States of America

Management's responsibilities include:

- The selection and application of accounting principles, the preparation and fair presentation of the financial statements, schedule of expenditures of federal awards, schedule of expenditures of state financial assistance, and all accompanying information
- Establishing and maintaining effective internal controls, including internal controls over compliance
- Making all financial records and related information available to us and for the accuracy and completeness of that information
- The design and implementation of programs and controls to prevent and detect fraud and for informing us about all known or suspected fraud affecting the government
- Identifying government award programs and understanding and complying with the compliance requirements

Auditor's responsibilities include:

- Express opinions on the financial statements based on our audit
- Plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement
- Performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements
- Consider 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
- 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

Audit Areas of Focus

- Cash
- Investments
- Receivables and revenues
- Capital Assets
- Payables, accruals, expenditures
- Payroll expenditures
- Debt
- Grants – State Single Audit

Engagement Timing

- Our initial planning for the year-end audit will be performed during July 2017. Our focus will be on documentation of the internal controls as required by auditing standards, fraud inquiry interviews with management and key personnel, preparation of certain confirmations some overall analytical procedures and audit fieldwork as applicable to the federal and state single audits and procedures performed relevant to the tax collector's and tax assessor's offices.

- Audit Timing:

Commencement of Fieldwork	10/2/17
End of Fieldwork	10/13/17
Issuance of Draft Financial Statements	11/6/17
Client Approval of Draft Statements	11/20/17
Issuance of Financial Statements	12/1/17
Issuance of Management Letter, if applicable	12/1/17
Post Audit Meeting with Management	TBD

Engagement Team

An engagement team consisting of the following individuals will be responsible for audit, and other services, including contact information to reach us:

- Vanessa Rossitto, Audit Partner
Direct Line: 860-561-6824
Email: vrossitto@blumshapiro.com
- Gerry Paradis, Concurring Audit Reviewer
Direct Line: 860-570-6371

Email: gparadis@blumshapiro.com

- Matt Coit, Audit Manager
Direct Line: 860-570-6416
Email: mcoit@blumshapiro.com

Other Communications

At the completion of our audit we will communicate in writing the following information related to our audit:

- Management judgments and significant sensitive accounting estimates
- Significant accounting policies
- The adoption of new accounting principles or changes in accounting principles
- Significant audit adjustments (recorded and unrecorded)
- Disagreements with management about auditing, accounting or disclosure matters
- Difficulties encountered in performing the audit
- Irregularities and illegal acts
- Consultation by management with other auditors
- Matters affecting independence of auditors
- Material weaknesses, significant deficiencies and control deficiencies

Knowledge of Fraud

- If management or those charged with governance has any knowledge of fraud or potential fraud, this information needs to be communicated to us. As part of the audit process, we will be meeting with management to discuss fraud risks and any further issues.

Fraud Risk Assessment

- It is estimated that a typical organization, including municipalities, lose up to 5% of annual revenue to fraud. Municipalities are especially vulnerable due to the large amounts of cash collected in the tax collector's office, in addition to decentralized cash collection points such as transfer stations, golf courses, recreation programs, etc.
- The objectives of a Fraud Risk Assessment are to gather perceptions of fraud risk and to promote fraud awareness and prevention across the entity. The Fraud Risk Assessment process starts with the gathering of information on the population of fraud risks that may apply to the entity. This includes consideration of various types of possible fraud schemes, scenarios and opportunities to commit fraud. This information is then used to assess the relative likelihood and potential significance of identified fraud risk based on historical information, known fraud schemes and interviews with staff and management. A report is prepared documenting fraud risk within the entity and setting forth suggested policies and procedures to help prevent and detect fraud.

Anonymous Fraud Tip Hotline

- According to the 2016 Report to the Nations on Occupational Fraud and Abuse by the Association of Certified Fraud Examiners, 39% of corruption cases are detected by tip. Organizations that had reporting hotlines were much more likely to detect fraud through tips than organizations without hotlines – 47.3% compared to 28.2%.

Cybersecurity Threats

The frequency, scale and cost of cybersecurity incidents has increased exponentially. Here are some recent trends, facts and stats that illustrate the current cybersecurity climate:

- Cybersecurity incidents have surged 38% since 2014
- 77% of organizations reported an increase in cybersecurity attacks in 2015
- 50% of organizations feel they lack the talent to combat today's cybersecurity threats
- Nearly every state has a data protection law, most include fines for data breaches
- Global cybersecurity spending came in at \$77 billion for 2015
- Ransomware and targeted attacks are on the rise
- Attackers have found ways to monetize many types of personal data, and aren't just targeting SSNs and credit cards
- 80% of board members say that cyber security is discussed at most or all board meetings
- Commonly affected industries include: government, financial services, healthcare, retail and manufacturing

BlumShapiro offers a range of services to assess your company's cybersecurity strategy and develop a plan to mitigate risk. It can start with a short educational session for employees. We also offer a portfolio of Implementation services to help mitigate overall risks.

Industry Developments - Current Year (June 30, 2017) Accounting Standards

- **GASB Statement 73 - Pensions Not Within the Scope of Statement 68 and Amendments to Statements 67 and 68** This Statement establishes requirements for defined benefit pensions that are not within the scope of Statement No. 68, *Accounting and Financial Reporting for Pensions*, as well as for the assets accumulated for purposes of providing those pensions. In addition, it establishes requirements for defined contribution pensions that are not within the scope of Statement 68. It also amends certain provisions of Statement No. 67, *Financial Reporting for Pension Plans*, and Statement 68 for pension plans and pensions that are within their respective scopes.
- **GASB Statement 74 - Financial Reporting by OPEB Plans (disclosure)** The objective of this Statement is to improve the usefulness of information about postemployment benefits other than pensions (other postemployment benefits or OPEB) included in the general purpose external financial reports of state and local governmental OPEB plans for making decisions and assessing accountability.

This Statement requires the net OPEB liability to be measured as the total OPEB liability, less the amount of the OPEB plan's fiduciary net position. The total OPEB liability generally is required to be determined through an actuarial valuation. Actuarial valuations, or calculations using the specified alternative measurement method, of the total OPEB liability are required to be performed at least every two years, with more frequent valuations or calculations encouraged. Unless otherwise specified by this Statement, all assumptions underlying the determination of the total OPEB liability are required to be made in conformity with the guidance in Actuarial Standards of Practice issued by the Actuarial Standards Board.

- **GASB Statement 77 - Tax Abatement Disclosures** Financial statement users need information about certain limitations on a government's ability to raise resources. This includes limitations on revenue-raising capacity resulting from government programs that use tax abatements to induce behavior by individuals and entities that is beneficial to the government or its citizens. For financial reporting purposes, this Statement defines a tax abatement as resulting from an agreement between a government and an individual or entity in which the government promises to forgo tax revenues and the individual or entity promises to subsequently take a specific action that contributes to economic development or otherwise benefits the government or its citizens.

This Statement requires governments that enter into tax abatement agreements to disclose the following information about the agreements:

- Brief descriptive information, such as the tax being abated, the authority under which tax abatements are provided, eligibility criteria, the mechanism by which taxes are abated, provisions for recapturing abated taxes, and the types of commitments made by tax abatement recipients
 - The gross dollar amount of taxes abated during the period
 - Commitments made by a government, other than to abate taxes, as part of a tax abatement agreement.
- **GASB Statement 78 - Pensions Provided Through Certain Multiple-Employer DB Pension Plans** This Statement amends the scope and applicability of Statement 68 to exclude pensions provided to employees of state or local governmental employers through a cost-sharing multiple-employer defined benefit pension plan that 1) is not a state or local governmental pension plan, 2) is used to provide defined benefit pensions both to employees of state or local governmental employers and to employees of employers that are not state or local governmental employers, and 3) has no predominant state or local governmental employer (either individually or collectively with other state or local governmental employers that provide pensions through the pension plan). This Statement establishes requirements for recognition and measurement of pension expense, expenditures, and liabilities; note disclosures; and required supplementary information for pensions that have the characteristics described above.
 - **GASB Statement 80 - Blending Requirements for Certain Component Units - an Amendment of GASB Statement No. 14** This Statement amends the blending requirements for the financial statement presentation of component units of all state and local governments. The additional criterion requires blending of a component unit incorporated as a not-for-profit corporation in which the primary government is the sole corporate member. The additional criterion does not apply to component units included in the financial reporting entity pursuant to the provisions of Statement No. 39, *Determining Whether Certain Organizations Are Component Units*.
 - **GASB Statement 82 – Pension Issues, an Amendment of GASB Statements 67, 68 and 73.** Specifically, this Statement addresses issues regarding (1) the presentation of payroll-related measures in required supplementary information, (2) the selection of assumptions and the treatment of deviations from the guidance in an Actuarial Standard of Practice for financial reporting purposes, and (3) the classification of payments made by employers to satisfy employee (plan member) contribution requirements.

Industry Developments - Future Accounting Standards - June 30, 2018

- **GASB Statement 75 - OPEB Accounting for Employers and Non-Employer Contributing Entities** The scope of this Statement addresses accounting and financial reporting for OPEB that is provided to the employees of state and local governmental employers. This Statement establishes standards for recognizing and measuring liabilities, deferred outflows of resources, deferred inflows of resources, and expense/expenditures. For defined benefit OPEB, this Statement identifies the methods and assumptions that are required to be used to project benefit payments, discount projected benefit payments to their actuarial present value, and attribute that present value to periods of employee service. Note disclosure and required supplementary information requirements about defined benefit OPEB also are addressed.
- **GASB Statement 81 – Irrevocable Split-Interest Agreements** The objective of this Statement is to improve accounting and financial reporting for irrevocable split-interest agreements by providing recognition and measurement guidance for situations in which a government is a beneficiary of the agreement. Split-interest agreements are a type of giving agreement used by donors to provide resources to two or more beneficiaries, including governments. This Statement requires that a government that receives resources pursuant to an irrevocable split-interest

agreement recognize assets, liabilities, and deferred inflows of resources at the inception of the agreement.

- **GASB Statement 85 – Omnibus** The objective of this Statement is to address practice issues that have been identified during implementation and application of certain GASB Statements.
 - Blending a component unit in circumstances in which the primary government is a business-type activity that reports in a single column for financial statement presentation
 - Reporting amounts previously reported as goodwill and “negative” goodwill
 - Measuring certain money market investments and participating interest-earning investment contracts at amortized cost
 - Timing of the measurement of pension or OPEB liabilities and expenditures recognized in financial statements prepared using the current financial resources measurement focus
 - Recognizing on-behalf payments for pensions or OPEB in employer financial statements
 - Presenting payroll-related measures in required supplementary information for purposes of reporting by OPEB plans and employers that provide OPEB
 - Classifying employer-paid member contributions for OPEB
 - Simplifying certain aspects of the alternative measurement method for OPEB
 - Accounting and financial reporting for OPEB provided through certain multiple-employer defined benefit OPEB plans.

Industry Developments - Future Accounting Standards - June 30, 2019

- **GASB Statement 83 – Certain Asset Retirement Obligations** This Statement addresses accounting and financial reporting for certain asset retirement obligations (AROs). An ARO is a legally enforceable liability associated with the retirement of a tangible capital asset. A government that has legal obligations to perform future asset retirement activities related to its tangible capital assets should recognize a liability based on the guidance in this Statement.

Industry Developments - Future Accounting Standards - June 30, 2020

- **GASB Statement 84 – Fiduciary Activities** The objective of this statement is to improve guidance regarding the identification of fiduciary activities for accounting and financial reporting purposes and how those activities should be reported.

Areas of Concerns

- If you have any concerns that you would like to discuss with Blum Shapiro, we will make ourselves available either by phone or in person to discuss such concerns.