

Memorandum

To: Board of Water Commissioners Finance Committee, City of Detroit Water and Sewerage Department

From: Beth Bialy and Tim St. Andrew

Subject: Summary of audit observations and comments

Date: December 14, 2019

CC: Gary Brown and Thomas Naughton

We recently completed our audit of the financial statements for the City of Detroit, Michigan (the "City"), which included the Water Fund and Sewage Disposal Fund as enterprise funds of the City. As part of that audit, we have communicated relevant matters to those charged with governance of the City. With the issuance of the separate Water Fund and Sewage Disposal Fund financial statements, we felt it appropriate to summarize the information contained in those communications that is relevant to the City of Detroit Water and Sewerage Department (the "DSWD" or the "Department").

Below is a summarized discussion of the observations and comments that are contained in our formal communications to the City of Detroit, Michigan (note that the finding numbers refer to the more comprehensive discussion to be found in the City's report on internal control and compliance). For a more complete understanding, we refer you to those original documents. However, the two of us are available to discuss these concepts with the Board of Water Commissioners at its convenience.

It is important to understand that, due to the financial environment in place, the DWSD is reliant on certain accounting procedures and controls of the City and the Great Lakes Water Authority (GLWA). We include all such matters here because we feel that, in your oversight role, it is important to focus on all internal control issues that impact the DWSD.

Internal Control Matters

Finding No. 2019-007

Finding Type Significant deficiency

Finding The Detroit Water and Sewerage Department (the "DWSD") should have a process in place to ensure proper recording of all journal entries in accordance with generally accepted accounting principles (GAAP) prior to the commencement of the audit. During the audit for the Detroit Water and Sewer Department, we noted certain invoices from the Great Lakes Water Authority were improperly included in accounts payable at year end. The balances on these particular invoices were settled in the prior year as part of the bifurcation and final negotiations with the Great Lakes Water Authority. The payables were flagged in the system during fiscal year 2020 as closed, and, therefore, no payment would have been made on them. The general ledger and accounts payable detail were not updated to reflect the adjustment in fiscal year 2019.

Other Internal Control Matters

During our audit, we noted areas where we believe there are opportunities for the Department to further strengthen internal controls over financial reporting. While these items do not rise to the level of a material weakness or significant deficiency, we believe these items are important enough to merit your attention as the Department continues to evaluate and improve the internal control environment.

- The Department's process to ensure that all customer accounts are updated and billed at the appropriate rates for water and sewerage consumption did not properly update all customer accounts to the appropriate water and sewage billing rate. We noted an instance where the water charge was billed at the suburban rate, but the sewage charge was improperly billed at the city rate (versus the suburban rate).
- During the audit, we noted that debt issuance costs were capitalized by the Department rather than expensed. Going forward, the Department should expense debt issuance costs in accordance with Governmental Accounting Standards Board Statement No. 65.
- During the audit, we noted that the accrued interest balance on cash and investments was not updated from the prior year. We recommend that the Department adjust the accrued interest balance based on the actual amounts at least annually.
- The Department has a process in place to record an allowance on accounts receivable for estimated uncollectible amounts based on past collection history and current collection trends. The process is not applied to unbilled accounts receivable balances at year end. Going forward, we recommend that the Department apply an estimated uncollectible percentage to unbilled accounts receivable as well.

- During the audit, we noted that accrued salaries and wages at year end were not properly allocated between the Water Fund and Sewage Disposal Fund. Going forward, we recommend that the Department allocate the accrued salaries and wages in order for the liabilities and expense to be properly recognized in the funds.

Audit Observations

Qualitative Aspects of Accounting Practices

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.

Estimate	Basis for Estimate
Accrued claims and judgments	The estimated probable loss that will result from ongoing litigation involving general and automobile claims
Accrued workers' compensation	An actuarial report prepared by an independent third party. The report was based on certain assumptions pertaining to actual loss development patterns that are augmented with industry benchmark loss development patterns.
Allowance for doubtful accounts	Management's analysis of accounts receivable for water and sewer billings that are unlikely to be collected by the DWSD based on past collection history and current collection trends
Net pension liability, deferred inflows and outflows, and pension expense	Independent third-party actuary services. These valuations are based on certain assumptions pertaining to mortality, expected returns on plan assets, and future contributions from the City or the DWSD.

We evaluated the key factors and assumptions used to develop the estimates above in determining that they are reasonable in relation to the financial statements taken as a whole.

Certain financial statement disclosures are particularly sensitive because of their significance to financial statement users. The most sensitive disclosures affecting the financial statements were the long-term obligation disclosures included in Note 6, the risk management disclosures in Note 8, and the pension disclosures in Note 9.

To the Board of Water Commissioners
Finance Committee
City of Detroit Water and
Sewerage Department

December 14, 2019

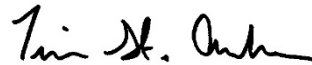
We would like to take this opportunity to thank the DWSD's staff for the cooperation and courtesy extended to us during our audit. Their assistance and professionalism are invaluable. We welcome any questions you may have regarding the following communications, and we would be willing to discuss any of these or other questions that you might have at your convenience.

Very truly yours,

Plante & Moran, PLLC

A handwritten signature in black ink, appearing to read "Beth Bialy".

Beth Bialy
Partner

A handwritten signature in black ink, appearing to read "Tim St. Andrew".

Tim St. Andrew
Senior Manager