



SB & COMPANY, LLC
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Mr. Bud Otis
Council President
Frederick County, Maryland
Winchester Hall
12 E. Church Street
Frederick, MD 21701

Dear Mr. Otis,

We have audited the financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of Frederick County, Maryland (the County) as of and for the year ended June 30, 2016, and have issued our report thereon dated November 21, 2016. Professional standards require that we advise you of the following matters relating to our audit.

Our Responsibility in Relation to the Financial Statement Audit

As communicated in our engagement letter dated July 19, 2016, our responsibility, as described by professional standards, is to form and express an opinion about whether the financial statements that have been prepared by management with your oversight are presented fairly, in all material respects, in accordance with accounting principles generally accepted in the United States of America. Our audit of the financial statements does not relieve you or management of its respective responsibilities.

Our responsibility, as prescribed by professional standards, is to plan and perform our audit to obtain reasonable, rather than absolute, assurance about whether the financial statements are free of material misstatement. An audit of financial statements includes consideration of internal control over financial reporting as a basis for designing 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 over financial reporting. Accordingly, as part of our audit, we considered the internal control of the County solely for the purpose of determining our audit procedures and not to provide any assurance concerning such internal control.

We are also 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 for the purpose of identifying other matters to communicate to you.

Planned Scope and Timing of the Audit

We conducted our audit consistent with the planned scope and timing we previously communicated to you.

Compliance with All Ethics Requirements Regarding Independence

The engagement team, others in our firm, as appropriate, our firm, and our network firms have complied with all relevant ethical requirements regarding independence.



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Qualitative Aspects of the Entity's Significant Accounting Practices

Significant Accounting Policies

Management has the responsibility to select and use appropriate accounting policies. A summary of the significant accounting policies adopted by the County is included in Note 1 to the financial statements. There have been no initial selection of accounting policies and no changes in significant accounting policies or their application during 2016. No matters have come to our attention that would require us, under professional standards, to inform you about (1) the methods used to account for significant unusual transactions and (2) the effect of significant accounting policies in controversial or emerging areas for which there is a lack of authoritative guidance or consensus.

Significant Accounting Estimates

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's current judgments. Those judgments are normally based on 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 markedly from management's current judgments.

The most sensitive accounting estimates affecting the financial statements are:

- Useful lives of fixed assets
- Landfill closure and post closure liabilities
- Liabilities related to pension and OPEB

Financial Statement Disclosures

Certain financial statement disclosures involve significant judgment and are particularly sensitive because of their significance to financial statement users. The most sensitive disclosures affecting the County's financial statements relate to fair value estimates.

Identified or Suspected Fraud

We have not identified or have not obtained information that indicates that fraud may have occurred.

Significant Difficulties Encountered during the Audit

We encountered no significant difficulties in dealing with management relating to the performance of the audit.



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Disagreements with Management

For purposes of this letter, professional standards define a disagreement with management as a matter, whether or not resolved to our satisfaction, concerning a financial accounting, reporting, or auditing matter, which could be significant to the County's financial statements or the auditor's report. No such disagreements arose during the course of the audit.

Representations Requested from Management

We have requested certain written representations from management, which are included in the letter dated November 21, 2016.

Management's Consultations with Other Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters. Management informed us that, and to our knowledge, there were no consultations with other accountants regarding auditing and accounting matters.

Other Significant Matters, Findings or Issues

In the normal course of our professional association with the County, we generally discuss a variety of matters, including the application of accounting principles and auditing standards, operating conditions affecting the entity, and operating plans and strategies that may affect the risks of material misstatement. None of the matters discussed resulted in a condition to our retention as the County's auditors.

This report is intended solely for the information and use of the County Council and management of Frederick County, Maryland and is not intended to be and should not be used by anyone other than these specified parties.

Sincerely,

SB & Company, LLC

By: 
Christopher Lehman

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Presentation to the County Council
December 13, 2016





INTRODUCTIONS

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Engagement Team Leadership

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SB & Company, LLC

- ❖ **Chris Lehman, Engagement Partner**
- ❖ **Bill Seymour, Client Service Partner**





EXECUTIVE SUMMARY

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Scope of Services

- Audit of the June 30, 2016, financial statements
- Performance of the Uniform Guidance Single Audit
- Audit of Bell Court Apartments
- Audit of the Office for Children with Families
- Audit of 9-1-1 trust fund
- Examination of the Statement of Client Attendance Days and Client Fees (DHMH requirement)
- Examination of the Wage Survey Form (DHMH requirement)
- Review of Uniform Financial Report
- Preparation of Data Collection Form



Summary of the Results

- Issued an unmodified opinion on the financial statements
- Discovered no instances of fraud
- Discovered no material weakness in internal controls
- Received full cooperation from management
- Upcoming changes to OPEB accounting
- Audit journal entries
 - No material Audit journal entries noted
- No Single Audit findings



AUDIT PROCESS

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FORCAM Audit Approach

“Focus on Risk, Controls and Misstatement”

FORCAM Audit Approach

Focus on Risk, Controls, and Account Misstatement

Agree on Expectations and Deliverables

Planning - Understand the Business & Risk

Client Acceptance • Client Environment • Tone at the Top
Materiality • Initial Risk Assessment • Audit Plan • Client Expectations

Assess & Test Design & Operations of Controls

What Can Go Wrong? • Test Key Controls • Walkthrough
Map Accounts & Transactions • Identify Key Controls

Financial Close & Reporting Misstatement Analysis

Analyze Balances • Financial Close Process
Principles Applied • Management's Verification

Substantive Testing

Negative Account Analysis • Negative Financial Close
Firm & GAAS Required • Significant Estimates
Negative Operating Controls • Unusual Transactions

GAAS Compliance & Reporting

GAAS Checklist • Review Reports • Wrap Up
Draft Board/Management Presentation
Did We Meet Your Expectations?

Goals:

Detect Financial Statement Misstatement Risk
Detect Error

- Accounting Principle
- Estimate
- Information Processing
- Account Balances

Fraud

Business Failure

Business Improvement Opportunities

Client Expectations

Communicate Value Delivered and Measure Satisfaction





Assessment of Control Environment

Area	Points to Consider	Our Assessment
Control Environment	<ul style="list-style-type: none">▪ Key executive integrity, ethical, and behavior▪ Control consciousness and operating style▪ Commitment to competence▪ Exercise oversee responsibility▪ Organizational structure, responsibility, and authority▪ Enforce accountability▪ HR policies and procedures	
Risk Assessment	<ul style="list-style-type: none">▪ Define objectives and risk tolerances▪ Identify, analyze, and respond to risk▪ Assess fraud risk▪ Identify, analyze, and respond to change▪ Mechanisms to anticipate, identify, and react to significant events▪ Processes and procedures to identify changes in GAAP, business practices, and internal control	
Control Activities	<ul style="list-style-type: none">▪ Design control activities▪ Design activities for the information system▪ Implement control activities▪ Existence of necessary policies and procedures▪ Clear financial objectives with active monitoring▪ Logical segregation of duties▪ Periodic comparisons of book-to-actual and physical count-to-books▪ Adequate safeguards of documents, records, and assets▪ Assess controls in place	

Legend:

- Not effective (Red)
- Suggested improvements (Yellow)
- Effective (Green)



Assessment of Control Environment

Area	Points to Consider	Our Assessment
Information and Communication	<ul style="list-style-type: none"> ▪ Use quality information ▪ Communicate internally ▪ Communicate externally ▪ Adequate performance reports produced from information systems ▪ Information systems are connected with business strategy ▪ Commitment of HR and finance to develop, test, and monitor IT systems and programs ▪ Business continuity and disaster plan for IT ▪ Established communication channels for employees to fulfill responsibilities ▪ Adequate communication across organization 	
Monitoring	<ul style="list-style-type: none"> ▪ Perform monitoring activities ▪ Remediate deficiencies ▪ Periodic evaluations of internal controls ▪ Implementation of improvement recommendations 	





Evaluation of Key Processes

Process	Function	A	B	C	D	Design	Operation
Treasury	<ul style="list-style-type: none">▪ Cash Management▪ Investment Accounting▪ Investment Monitoring▪ Investment Valuation▪ Investment Policy▪ Reconciliation	✓	✓	✓	✓		
Estimation	<ul style="list-style-type: none">▪ Methodology▪ Information▪ Calculation	✓	✓	✓			
Financial Reporting	<ul style="list-style-type: none">▪ Accounting Principles and Disclosure▪ Closing the Books▪ Report Preparation▪ General Ledger and Journal Entry Processing▪ Verification and Review of Results	✓	✓	✓			
Expenditures	<ul style="list-style-type: none">▪ Purchasing▪ Accounts Payable and Cash Disbursement▪ Purchase Card Transactions	✓	✓	✓	✓		

A	Understand the Process
B	Walk-Through

C	What Can Go Wrong
D	Test of Controls



Not effective

Suggested improvements

Effective



Evaluation of Key Processes

Process	Function	A	B	C	D	Design	Operation
Payroll	<ul style="list-style-type: none">Attendance ReportingPayroll Accounting and ProcessingPayroll Disbursements	✓	✓	✓	✓		
Revenue	<ul style="list-style-type: none">BillingCash ReceiptsRevenue RecognitionCutoff	✓	✓	✓	✓		
Fixed Assets	<ul style="list-style-type: none">Physical CustodyAsset AccountingDepreciation	✓	✓	✓			
Compliance	<ul style="list-style-type: none">Assess Internal and External RiskRegulatory ComplianceMonitor ComplianceCompliance	✓	✓	✓	✓		

A	Understand the Process
B	Walk-Through

C	What Can Go Wrong
D	Test of Controls



Not effective

Suggested improvements

Effective



Evaluation of Key Processes

Process	Function	A	B	C	D	Design	Operation
Information Technology	<ul style="list-style-type: none"> Computer Operations Segregation of Duties and Management Oversight Information Security and Transaction Authorization Program Integrity and Change Management 	✓	✓	✓			
Grant Compliance	<ul style="list-style-type: none"> Acceptance Grant oversight Compliance Reporting Monitoring Accounting Billing and collection 	✓	✓	✓	✓		

A	Understand the Process
B	Walk-Through

C	What Can Go Wrong
D	Test of Controls



Not effective

Suggested improvements

Effective



Changes in OPEB Accounting

- GASB Statement No. 74, Financial Reporting for Postemployment Benefit Plans other than Pension Plans, required to be implemented for fiscal year 2017
- GASB Statement No. 75, Accounting and Financial Reporting for Postemployment Benefits other than Pensions, required to be implemented for fiscal year 2018. This can be early implemented.
- The accounting and disclosures are similar to the pension standards (GASB 67 and 68)
- Net OPEB liability recorded on the Entity-wide Statement of Net Position
- As of June 30, 2016, the County had an unfunded actuarial accrued liability of approximately \$67 million (with a funded ratio of 62%)



Single Audit Results

Major Programs	Expenditures
Highway Planning and Construction- Bridge Projects	\$ 5,263,623
Assistance to Firefighters Grant	1,842,794
Disaster Grants-Public Assistance	854,566
Total Major Programs	\$ 7,960,983
Total Federal Expenditures	\$ 23,430,218
Percentage of Coverage	34%
No Single Audit findings	



REQUIRED COMMUNICATIONS

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Required Communications

1. Auditor's Responsibilities Under Generally Accepted Auditing Standards (GAAS)

The financial statements are the responsibility of management. Our audit was designed in accordance with auditing standards generally accepted in the United States of America, and provide for reasonable, rather than absolute, assurance that the financial statements are free of material misstatement.

2. Significant Accounting Policies

Management has the responsibility for 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 management are described in the notes to the financial statements.

3. Auditor's Judgments About the Quality of Accounting Principles

We discuss our judgments about the quality, not just the acceptability, of accounting principles selected by management, the consistency of their application, and the clarity and completeness of the financial statements, which include related disclosures.

We have reviewed the significant accounting policies adopted by Frederick County Government. (the County) and have provided recommendations related to the policies as noted above.



Required Communications

(continued)

4. Audit Adjustments

We are required to inform the County's oversight body about adjustments arising from the audit (whether recorded or not) that could in our judgment either individually or in the aggregate have a significant effect on the entity's financial reporting process. We also are required to inform the County's oversight body about unadjusted audit differences that were determined by management to be individually and in the aggregate, immaterial.

There were no material audit adjustments identified during the audit process.

5. Fraud and Illegal Acts

We are required to report to the County's oversight body any fraud and illegal acts involving senior management and fraud and illegal acts (whether caused by senior management or other employees) that cause a material misstatement of the financial statements.

Our procedures identified no instances of fraud or illegal acts.

6. Material Weaknesses in Internal Control

We are required to communicate all significant deficiencies in the County's systems of internal controls, whether or not they are also material weaknesses.

There were no material weaknesses noted during the audit.



Required Communications

(continued)

7. Other Information in Documents Containing Audited Financial Statements

None.

8. Disagreements with Management on Financial Accounting and Reporting Matters

None.

9. Serious Difficulties Encountered in Performing the Audit

None.

10. Major Issues Discussed with Management Prior to Acceptance

None.

11. Management Representations

We have received certain written representations from management as part of the completion of the audit.

12. Consultation with Other Accountants

To our knowledge, there were no consultations with other accountants since our appointment as the County's independent public accountants.

13. Independence

*As part of our client acceptance process, we go through a process to ensure we are independent of the County.
We are independent of the County.*



Required Communications

(continued)

14. Our Responsibility Related to Fraud

- Plan and perform the audit to obtain reasonable assurance that there is no material misstatement caused by error or fraud;
- Comply with AU-C Section 240: Consideration of Fraud in a Financial Statement Audit;
- Approach all audits with an understanding that fraud could occur in any entity, at any time, by anyone; and
- Perform mandatory procedures required by GAAS and our firm policies.

Examples of Procedures Performed

- Discuss thoughts and ideas on where the financial statements might be susceptible to material misstatement due to fraud;
- Understand pressures on the financial statement results;
- Understand the tone and culture of the organization;
- Look for unusual or unexpected transactions, relationships, or procedures;
- Discussions with individuals outside of finance;
- Evaluate key processes and controls; and
- Consider information gathered throughout the audit.



Responsibility for Mitigating Fraud



External Auditor

- Evaluate management programs and controls to deter and detect fraud for identified risks
- Reasonable assurance that financial statements are free of material misstatement due to fraudulent financial reporting or misappropriation of assets
- Compliance with fraud standard (SAS 99)
 - Conversations with finance and operations personnel
 - Disaggregated analytics
 - Surprise audit procedures
 - Journal entry testing

Audit Committee:

- CFO/Controller: controls to deter and detect fraud
- General Counsel/Compliance: monitoring

Audit Committee:

- Evaluate management identification of fraud risk
- Evaluate implementation of fraud controls
- Reinforce “tone at the top”
- Conduct special investigations



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