

# Auditing Procedures Report

Issued under P.A. 2 of 1968, as amended and P.A. 71 of 1919, as amended.

Local Unit of Government Type <input type="checkbox"/> County <input type="checkbox"/> City <input type="checkbox"/> Twp <input type="checkbox"/> Village <input type="checkbox"/> Other		Local Unit Name	County
Fiscal Year End	Opinion Date	Date Audit Report Submitted to State	

We affirm that:

We are certified public accountants licensed to practice in Michigan.

We further affirm the following material, "no" responses have been disclosed in the financial statements, including the notes, or in the Management Letter (report of comments and recommendations).

**YES NO** Check each applicable box below. (See instructions for further detail.)

1.   All required component units/funds/agencies of the local unit are included in the financial statements and/or disclosed in the reporting entity notes to the financial statements as necessary.
2.   There are no accumulated deficits in one or more of this unit's unreserved fund balances/unrestricted net assets (P.A. 275 of 1980) or the local unit has not exceeded its budget for expenditures.
3.   The local unit is in compliance with the Uniform Chart of Accounts issued by the Department of Treasury.
4.   The local unit has adopted a budget for all required funds.
5.   A public hearing on the budget was held in accordance with State statute.
6.   The local unit has not violated the Municipal Finance Act, an order issued under the Emergency Municipal Loan Act, or other guidance as issued by the Local Audit and Finance Division.
7.   The local unit has not been delinquent in distributing tax revenues that were collected for another taxing unit.
8.   The local unit only holds deposits/investments that comply with statutory requirements.
9.   The local unit has no illegal or unauthorized expenditures that came to our attention as defined in the *Bulletin for Audits of Local Units of Government in Michigan*, as revised (see Appendix H of Bulletin).
10.   There are no indications of defalcation, fraud or embezzlement, which came to our attention during the course of our audit that have not been previously communicated to the Local Audit and Finance Division (LAFD). If there is such activity that has not been communicated, please submit a separate report under separate cover.
11.   The local unit is free of repeated comments from previous years.
12.   The audit opinion is UNQUALIFIED.
13.   The local unit has complied with GASB 34 or GASB 34 as modified by MCGAA Statement #7 and other generally accepted accounting principles (GAAP).
14.   The board or council approves all invoices prior to payment as required by charter or statute.
15.   To our knowledge, bank reconciliations that were reviewed were performed timely.

If a local unit of government (authorities and commissions included) is operating within the boundaries of the audited entity and is not included in this or any other audit report, nor do they obtain a stand-alone audit, please enclose the name(s), address(es), and a description(s) of the authority and/or commission.

I, the undersigned, certify that this statement is complete and accurate in all respects.

We have enclosed the following:	Enclosed	Not Required (enter a brief justification)
Financial Statements	<input type="checkbox"/>	
The letter of Comments and Recommendations	<input type="checkbox"/>	
Other (Describe)	<input type="checkbox"/>	
Certified Public Accountant (Firm Name)		Telephone Number
Street Address	City	State      Zip
Authorizing CPA Signature 	Printed Name	License Number

# **South Macomb Disposal Authority**

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**Financial Report**  
**June 30, 2007**

# **South Macomb Disposal Authority**

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## Independent Auditor's Report

To the Board of Directors  
South Macomb Disposal Authority

We have audited the accompanying basic financial statements of South Macomb Disposal Authority as of June 30, 2007 and for the year then ended, as listed in the table of contents. These financial statements are the responsibility of the Authority's management. Our responsibility is to express an opinion 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of South Macomb Disposal Authority at June 30, 2007 and the results of its operations and cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

The management's discussion and analysis (identified in the table of contents) is not a required part of the basic financial statements but is supplemental information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management, regarding the methods of measurement and presentation of the required supplemental information. However, we did not audit the information and express no opinion on it.

*Plante & Moran, PLLC*

December 12, 2007

# **South Macomb Disposal Authority**

## **Management's Discussion and Analysis**

### **Using this Annual Report**

South Macomb Disposal Authority (the "Authority") is a joint venture of five cities located in southern Macomb County: Center Line, Eastpointe, Roseville, St. Clair Shores, and Warren. The primary roles of the Authority are to manage the transfer of solid waste currently collected by all of the member cities (except Warren) and to provide for the postclosure care of landfill sites previously operated by the Authority. The Authority does not currently operate any landfill sites. This annual report consists of a series of financial statements. The statement of net assets and the statement of revenue, expenses, and changes in net assets provide information about the financial activities of the Authority. These are followed by the statement of cash flows, which presents detailed information about the changes in the Authority's cash position during the year.

### **Financial Overview**

In analyzing the Authority's financial position, it is important to recognize the dual missions of the Authority. From a financial perspective, the Authority's core objective (and ongoing operation) is to manage the costs of solid waste transfer for Center Line, Eastpointe, Roseville, and St. Clair Shores. With respect to this core objective, the Authority acts as a conduit for the four participating members. The amounts to be charged to the participating members for these services will, therefore, approximate the Authority's costs of providing solid waste transfer services. The key financial statistics for the Authority, therefore, relate to measurements of the ability to reduce total costs to its members (as opposed to the ability to accumulate financial resources). To this end, the net assets of the Authority related to ongoing operations are approximately \$885,000, of which approximately \$442,000 is invested in capital assets.

The other objective of the Authority is to provide for the postclosure care of landfill sites previously operated by the Authority, including all of its original five member cities. In prior years, the Authority successfully sued its insurers and received a settlement for remediation of its previously owned sites. Under the terms of the settlement, the Authority's continuing insurance coverage is limited to costs of defense, past response costs, and the cost of remedial investigation on any owned sites for which the Authority has continuing maintenance and monitoring responsibilities. At June 30, 2007, the Authority has two remaining landfill sites. The Authority has recorded an estimated liability for a study on these two landfill sites to assess the level of contamination and to determine the level of potential remediation costs. The entire liability related to this study has been recorded as a current liability of \$280,000.

During the current year, the Authority paid out the \$950,000 that was previously accrued and recorded as a short-term liability at June 30, 2006. This payment was for the settlement with the last plaintiff in a series of lawsuits filed 23 years ago for contamination to the plaintiff's land caused from the adjacent landfills that the Authority previously owned.

# **South Macomb Disposal Authority**

## **Management's Discussion and Analysis (Continued)**

### **Financial Overview (Continued)**

In addition, the Authority had previously received a total of approximately \$5,700,000 in landfill grant funds from the State of Michigan to assist with the remediation of Sites 9 and 9a that are no longer owned by the Authority. The State demanded that these funds be returned since the Authority received reimbursement from its insurers. On May 4, 2005, the Macomb County Circuit Court upheld the State's demand, which the Authority appealed to the State of Michigan Court of Appeals. On October 17, 2006, the State of Michigan Court of Appeals affirmed the decision and mandated the Authority to pay back to the State of Michigan the grant monies previously received. However, the State of Michigan Court of Appeals indicated that the current ruling could be reduced by previous costs the Authority incurred in obtaining the insurance reimbursement for the sites. The State of Michigan Court of Appeals directed this decision to be made at the Macomb County Circuit Court level. On August 6, 2007, the Macomb County Circuit Court upheld the decision that the Authority would need to repay the full amount of landfill grant funds of approximately \$5,700,000 back to the State of Michigan. On August 27, 2007 (as amended on August 31, 2007), the Authority sought leave to appeal from this ruling of the Circuit Court. The Court of Appeals has not yet acted on the Authority's application for leave to appeal. If the Authority is ultimately required to pay all the grant monies back to the State, the attorneys that represented the Authority in its claim against the insurers will reimburse approximately \$400,000 of legal fees to the Authority. The payable and receivable are reflected in the Authority's balance sheet as of June 30, 2007.

### **Condensed Financial Information**

The following tables present condensed information about the Authority's financial position compared to the prior year.

In the first table, net assets increased by approximately \$99,500. This is due to the liabilities decreasing by an amount greater than the asset decrease in the current year. Overall, the liabilities decreased by approximately \$912,000 and assets decreased by approximately \$813,000. The decrease in assets was mainly due to a decrease in cash available to invest which was attributable to the payment during the current fiscal year of the \$950,000 lawsuit settlement that was accrued for in the prior fiscal year. This payment also reduced the current year liabilities due to the liability being paid in full in the current year. In addition to the decrease in cash which affected the overall asset balance, the capital asset balance decrease by approximately \$324,000 from prior year also affected the overall asset value. This decrease in capital assets was mainly due to a required adjustment to remove assets that were associated with Sites 9 and 9a. The assets were actually disposed with the sale of Sites 9 and 9a in a previous year.

# South Macomb Disposal Authority

## Management's Discussion and Analysis (Continued)

In the second table, the most significant change is in the decrease in total nonoperating net income. This is mainly attributable to the \$950,000 settlement that was expensed in the prior year and higher realized interest earnings in the current year. During the current year, the Authority diversified its investments while staying fully in compliance with Public Act 20. The Authority's investment policy goals are to maximize its investment returns while ensuring safety and liquidity with its investment choices. In the current year, the Authority was able to increase its realized interest earnings by approximately \$79,000 or 14 percent from the prior year even with less cash reserves to invest. Operational net income also experienced a slight increase of approximately \$35,000 from the prior year. This was mainly due to less repair costs being required in the current year.

	June 30		Change	
	2007	2006	Amount	Percent
<b>Assets</b>				
Current assets	\$ 11,373,156	\$ 11,862,094	\$ (488,938)	(4)
Capital assets	<u>675,140</u>	<u>999,161</u>	<u>(324,021)</u>	(3)
Total assets	12,048,296	12,861,255	(812,959)	(6)
<b>Liabilities</b>				
Current liabilities	6,423,770	1,635,775	4,787,995	293
Long-term liabilities	<u>-</u>	<u>5,700,400</u>	<u>(5,700,400)</u>	100
Total liabilities	<u>6,423,770</u>	<u>7,336,175</u>	<u>(912,405)</u>	(12)
<b>Net Assets</b>				
Invested in capital assets	675,140	999,161	(324,021)	(32)
Unrestricted	<u>4,949,386</u>	<u>4,525,919</u>	<u>423,467</u>	9
Total net assets	<u>\$ 5,624,526</u>	<u>\$ 5,525,080</u>	<u>\$ 99,446</u>	2

# South Macomb Disposal Authority

## Management's Discussion and Analysis (Continued)

	Year Ended June 30		Change	
	2007	2006	Amount	Percent
<b>Operating Revenue</b>				
Disposal fees	\$ 1,379,610	\$ 1,448,116	\$ (68,506)	(5)
Administrative fees	<u>78,124</u>	<u>77,835</u>	<u>289</u>	-
Total operating revenue	1,457,734	1,525,951	(68,217)	(4)
<b>Operating Expenses</b>				
Operations and maintenance	84,119	151,288	(67,169)	(44)
General and administrative	67,624	61,327	6,297	10
Contracted disposal costs	<u>1,230,544</u>	<u>1,273,234</u>	<u>(42,690)</u>	(3)
Total operating expenses	1,382,287	1,485,849	(103,562)	(7)
<b>Nonoperating Revenue (Expenses)</b>				
Postclosure and remediation costs	(21,431)	(14,508)	(6,923)	48
Lawsuit settlement related to closed sites	-	(950,000)	950,000	-
Investment and other income	635,486	556,908	78,578	14
Unrealized loss in fair value	(90,212)	-	(90,212)	100
Other legal expenses related to closed sites	<u>(201,466)</u>	<u>(204,426)</u>	<u>2,960</u>	1
Total nonoperating revenue (expense)	<u>322,377</u>	<u>(612,026)</u>	<u>934,403</u>	(153)
<b>Net Income (Loss)</b>	<b><u>\$ 397,824</u></b>	<b><u>\$ (571,924)</u></b>	<b><u>\$ 969,748</u></b>	(170)

# **South Macomb Disposal Authority**

## **Management's Discussion and Analysis (Continued)**

At June 30, 2007, the Authority has only two landfill sites for which it is responsible for future postclosure care. Annually, the Authority expenses any postclosure care costs related to the two remaining sites of the Authority. As previously mentioned above, the Authority has recorded an additional estimated liability for a study on these two landfill sites to assess the level of contamination and to determine the level of potential remediation costs. The entire liability related to this study has been recorded as a current liability of \$280,000.

### **Net Asset Designations and Risk Management**

The Authority has potentially significant economic issues to resolve over the next several years related to the two remaining landfill sites. The potential liability will be assessed further in the contamination assessment projected to be completed by June 30, 2008. The accumulated net assets for postclosure care costs have been set aside by the Authority's governing body to serve as a reserve fund for potential remediation costs for which the Authority is now uninsured.

### **Economic Factors and Next Year's Budget**

For ongoing solid waste transfer operations, costs will be dependent on the volume of solid waste hauled. The Authority's budget for the year ending June 30, 2008 forecasts a moderate increase in solid waste and, therefore, costs.

The Authority has estimated and recorded the known postclosure care liabilities related to the assessment study and the estimated liability to the State of Michigan associated with previously received landfill grant money as of June 30, 2007. There are no other claims against the Authority that would result in funding by the Authority as of June 30, 2007. However, the Authority will amend its budget as necessary for additional costs assessed by the State of Michigan or other regulatory authorities.

### **Contacting the Authority's Management**

This financial report is intended to provide our member cities with a general overview of the Authority's finances and to show the Authority's accountability for the money it receives from the member cities and other sources. If you have questions about this report or need additional information, we welcome you to contact the Authority's offices.

# South Macomb Disposal Authority

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## Statement of Net Assets June 30, 2007

### Assets

Cash and cash equivalents (Note 3)	\$ 347,874
Investments (Note 3)	10,239,664
Accounts receivable	377,322
Prepaid insurance	8,296
Receivables related to site remediation - Insurance and other (Note 7)	400,000
Land	254,963
Capital assets (Note 4)	<u>420,177</u>
Total assets	12,048,296

### Liabilities

Accounts payable	426,859
Accrued postclosure care and remediation liabilities (Note 7) - Due within one year	<u>5,996,911</u>
Total liabilities	<u>6,423,770</u>

### Net Assets

Invested in capital assets	675,140
Unrestricted (Note 5)	<u>4,949,386</u>
Total net assets	<u><u>\$ 5,624,526</u></u>

# South Macomb Disposal Authority

## Statement of Revenue, Expenses, and Changes in Net Assets Year Ended June 30, 2007

<b>Operating Revenue</b>	
Disposal fees	\$ 1,360,055
Closure cost billings	19,555
Administrative fees	<u>78,124</u>
Total operating revenue	1,457,734
<b>Operating Expenses</b>	
Operations and maintenance	84,119
General and administrative	67,624
Contracted disposal costs	<u>1,230,544</u>
Total operating expenses	<u>1,382,287</u>
<b>Operating Income</b>	75,447
<b>Nonoperating Revenue (Expenses)</b>	
Postclosure and remediation costs (Note 7)	(21,431)
Investment interest income	635,486
Unrealized loss in fair value	(90,212)
Other legal expenses related to closed sites (Note 7)	<u>(201,466)</u>
Total nonoperating expenses	<u>322,377</u>
<b>Net Income</b>	397,824
<b>Net Assets - Beginning of year, as adjusted (Note 9)</b>	<u>5,226,702</u>
<b>Net Assets - End of year</b>	<u><u>\$ 5,624,526</u></u>

# South Macomb Disposal Authority

## Statement of Cash Flows Year Ended June 30, 2007

### Cash Flows from Operating Activities

Cash received from customers	\$ 1,467,036
Cash payments to suppliers for goods and services	<u>(1,335,561)</u>
Net cash provided by operating activities	131,475

### Cash Flows from Capital and Noncapital Financing Activities

Net postclosure care, remediation costs, and legal attorney expenses	(194,099)
Lawsuit settlement	<u>(950,000)</u>
Net cash used in operating activities	(1,144,099)

### Cash Flows from Investing Activities

Net cash equivalents invested in investment vehicles	(9,898,888)
Interest received on investments	<u>705,742</u>
Net cash used in investing activities	<u>(9,193,146)</u>

**Net Decrease in Cash and Cash Equivalents** (10,205,770)

**Cash and Cash Equivalents - July 1, 2006** 10,553,644

**Cash and Cash Equivalents - June 30, 2007** \$ 347,874

### Cash Flows from Operating Activities

Operating income	\$ 75,447
Adjustments to reconcile operating income to net cash from operating activities:	
Depreciation	25,642
Changes in assets and liabilities:	
Decrease in accounts receivable	9,302
Increase in accounts payable	<u>21,084</u>
Net cash provided by operating activities	<u><u>\$ 131,475</u></u>

**Noncash Activities** - The Authority experienced an unrealized loss in the fair value of its investments during the year ended June 30, 2007.

# South Macomb Disposal Authority

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## Notes to Financial Statements June 30, 2007

### **Note 1 - Nature of Business and Significant Accounting Policies**

South Macomb Disposal Authority (the "Authority") consists of five member municipalities in Macomb County, Michigan. The Authority currently provides refuse disposal services primarily for the benefit of four of the five member municipalities. The governing body of the Authority consists of five members - one appointed by each of the five member communities.

The accounting policies of the Authority conform to accounting principles generally accepted in the United States of America as applicable to an Enterprise Fund of a governmental unit. Accordingly, the accrual basis of accounting is followed by the Authority. In accordance with accounting principles generally accepted in the United States of America, there are no component units to be included in these financial statements.

**Fixed Assets** - Fixed assets are recorded at cost and are shown net of accumulated depreciation. Depreciation is computed using the straight-line method.

**Cash Equivalents** - For the purpose of the statement of cash flows, the Authority considers all highly liquid investments with an original maturity of three months or less to be cash equivalents.

**Investments** - Investments are valued at fair value.

**Use of Estimates** - The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the period. Actual results could differ from those estimates.

Other accounting policies are disclosed in other notes to the financial statements.

### **Note 2 - Stewardship, Compliance, and Accountability**

**Noncompliance with Legal or Contractual Provisions** - The Authority has not currently adopted a formal policy to make and accept electronic fund transfers (ACH payments). A formal policy is required under Public Act 738.

# South Macomb Disposal Authority

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## Notes to Financial Statements June 30, 2007

### Note 3 - Deposits and Investments

Michigan Compiled Laws Section 129.91 (Public Act 20 of 1943, as amended) authorizes local governmental units to make deposits and invest in the accounts of federally insured banks, credit unions, and savings and loan associations that have offices in Michigan. The local unit is allowed to invest in bonds, securities, and other direct obligations of the United States or any agency or instrumentality of the United States; repurchase agreements; bankers' acceptances of United States banks; commercial paper rated within the two highest classifications, which matures not more than 270 days after the date of purchase; obligations of the State of Michigan or its political subdivisions, which are rated as investment grade; and mutual funds composed of investment vehicles that are legal for direct investment by local units of government in Michigan.

In addition to the Authority investing in accordance with Public Act 20 of 1943, the Authority also states in its investment policy that it will diversify its investments by security type and institution. With the exception of U.S. Treasury securities and authorized pools, no more than 60 percent of the Authority's investment portfolio will be invested in a single type or with a single financial institution.

The Authority has designated two banks for the deposit of its funds. The Authority's cash and investments are subject to several types of credit risk, which are examined in more detail below:

**Custodial Credit Risk of Bank Deposits** - Custodial credit risk is the risk that in the event of a bank failure, the Authority's deposits may not be returned to it. The Authority does not specifically address a deposit policy for custodial credit risk. At year end, the Authority had \$164,138 of bank deposits (certificates of deposit, checking, and savings accounts) that were uninsured and uncollateralized. The Authority believes that due to the dollar amounts of cash deposits and the limits of FDIC insurance, it is impractical to insure all deposits. As a result, the Authority evaluates each financial institution with which it deposits funds and assesses the level of risk of each institution; only those institutions with an acceptable estimated risk level are used as depositories.

**Custodial Credit Risk of Investments** - Custodial credit risk is the risk that, in the event of a bank failure of the counterparty, the Authority will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The Authority does not have a policy for custodial credit risk of investments.

# South Macomb Disposal Authority

## Notes to Financial Statements June 30, 2007

### Note 3 - Deposits and Investments (Continued)

At year end, the following investment securities were uninsured and unregistered, with securities held by the counterparty or by its trust department or agency but not in the Authority's name:

Type of Investment	Carrying Value	How Held
U.S. government and agency securities	\$ 10,239,664	Counterparty

**Interest Rate Risk** - Interest rate risk is the risk that the value of investments will decrease as a result of a rise in interest rates. The Authority's investment policy is in accordance with state law. At year end, the average weighted maturity for investments was as follows:

Investment	Fair Value	Weighted Average Maturity (in years)
U.S. government and agency securities:		
Federal Home Loan Mortgage Corp.	\$ 547,945	1.13
Federal Home Loan Bank	9,183,757	1.49
Federal National Mortgage Association	257,238	1.76
Federal Farm Credit Bank	250,725	0.62

**Credit Risk** - State law limits investments in commercial paper to the top two rating issued by nationally recognized statistical rating organizations. The Authority's investment policy is in accordance with the state law. At year end, the credit quality ratings are as follows:

Investment	Fair Value	Rating	Rating Organization
U.S. federal agencies	\$10,239,664	AAA	Moody's

**Concentration of Credit Risk** - The Authority states in its investment policy that it will diversify its investments by security type and institution. With the exception of U.S. Treasury securities and authorized pools, no more than 60 percent of the Authority's investment portfolio will be invested in a single type or with a single financial institution.

# South Macomb Disposal Authority

## Notes to Financial Statements June 30, 2007

### Note 3 - Deposits and Investments (Continued)

At year end, the Authority had the following investment concentrations:

U.S. government agencies:	
Federal Home Loan Mortgage Corp.	5.35%
Federal Home Loan Bank	89.69%
Federal National Mortgage Association	2.51%
Federal Farm Credit Bank	2.45%

### Note 4 - Capital Assets

Capital asset activity for the year ended June 30, 2007 was as follows:

	2006	Additions	Restatement of Fixed Assets (Note 9)	2007	Depreciable Life - Years
Capital assets not being depreciated -					
Land	\$ 254,963	\$ -	\$ -	\$ 254,963	-
Capital assets being depreciated:					
Site improvements	585,145	-	(539,086)	46,059	40
Equipment	346,848	-	(210,973)	135,875	7-15
Waste transfer station	1,201,645	-	-	1,201,645	40
Transfer station equipment	36,807	-	(36,807)	-	10-15
Subtotal	2,170,445	-	(786,866)	1,383,579	
Less accumulated depreciation for:					
Site improvements	(256,683)	(1,252)	239,894	(18,041)	
Equipment	(347,661)	-	211,786	(135,875)	
Waste transfer station	(785,096)	(24,390)	-	(809,486)	
Transfer station equipment	(36,807)	-	36,807	-	
Subtotal	(1,426,247)	(25,642)	488,487	(963,402)	
Net capital assets being depreciated	744,198	(25,642)	(298,379)	420,177	
Net capital assets	\$ 999,161	\$ (25,642)	\$ (298,379)	\$ 675,140	

# South Macomb Disposal Authority

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## Notes to Financial Statements June 30, 2007

### **Note 5 - Net Assets**

The Authority has designated certain net assets related to postclosure care and potential remediation activities. The designated net assets include proceeds from several litigation settlements with the Authority's insurers for remediation of the Authority's landfill sites. As part of these settlements, the insurers may be held to pay future defense costs but not remediation costs for the remaining two sites operated by the Authority. The amount of net assets designated totals approximately \$4,756,000, which includes approximately \$233,000 of the capital assets of the Authority. The Authority has designated these funds in a postclosure care/insurance reserve fund to pay for the potential remediation of the remaining two landfill sites (see Note 7).

### **Note 6 - Risk Management**

The Authority is exposed to various risks of loss related to property loss, torts, errors and omissions, and employee injuries (workers' compensation), as well as medical benefits provided to employees. The Authority has purchased commercial insurance for medical and life insurance claims and participates in the Michigan Municipal League risk pool for claims relating to property loss, torts, errors and omissions, and employee injuries (workers' compensation). Settled claims relating to the commercial insurance have not exceeded the amount of insurance coverage in any of the past three fiscal years.

The Michigan Municipal League risk pool program operates as a common risk-sharing management program for local units of government in Michigan; member premiums are used to purchase commercial excess insurance coverage and to pay member claims in excess of deductible amounts.

### **Note 7 - Postclosure Care, Remediation Costs, Commitments, and Contingent Liabilities**

Current state and federal laws and regulations require final covers on active landfill sites and the performance of certain maintenance and monitoring functions at the site for 30 years after closure. As of June 30, 2007, the Authority has two landfill sites for which it has continuing postclosure maintenance and monitoring responsibilities. The Authority reports annual closure and postclosure care costs as an operating expense in each fiscal year.

The Authority has also recorded an estimated liability for a study on these two landfill sites to assess the level of contamination and to determine the level of potential remediation costs. The entire liability related to this study has been recorded as a current liability of \$280,000.

# South Macomb Disposal Authority

## Notes to Financial Statements June 30, 2007

### **Note 7 - Postclosure Care, Remediation Costs, Commitments, and Contingent Liabilities (Continued)**

During the current year, the Authority paid \$950,000 for the settlement of a previously accrued lawsuit liability. This settlement was the last plaintiff in a series of lawsuits filed 23 years ago for contamination to the plaintiff's land caused from adjacent landfills that the Authority previously owned. The entire liability was recorded in prior year.

The Authority had previously received a total of approximately \$5,700,000 in landfill grant funds from the State of Michigan to assist with the remediation of Sites 9 and 9a that are no longer owned by the Authority. The State demanded that these funds be returned since the Authority received reimbursement from its insurers. On May 4, 2005, the Macomb County Circuit Court upheld the State's demand, which the Authority appealed to the State of Michigan Court of Appeals. On October 17, 2006, the State of Michigan Court of Appeals affirmed the decision and mandated the Authority to pay back to the State of Michigan the grant monies previously received. However, the State of Michigan Court of Appeals indicated that the current ruling could be reduced by previous costs the Authority incurred in obtaining the insurance reimbursement for the sites. The State of Michigan Court of Appeals directed this decision to be made at the Macomb County Circuit Court level. On August 6, 2007, the Macomb County Circuit Court upheld the decision that the Authority would need to repay the full amount of landfill grant funds of approximately \$5,700,000 back to the State of Michigan. On August 27, 2007 (as amended on August 31, 2007), the Authority sought leave to appeal from this ruling of the Circuit Court. The Court of Appeals has not yet acted on the Authority's application for leave to appeal. If the Authority is ultimately required to pay all the grant monies back to the State, the attorneys that represented the Authority in its claim against the insurers will reimburse approximately \$400,000 of legal fees to the Authority. The payable and receivable are reflected in the Authority's balance sheet as of June 30, 2007.

### **Note 8 - Postemployment Benefits**

The Authority provides healthcare benefits to all full-time employees upon retirement. Currently, three retirees are receiving benefits. The Authority includes retirees and their dependents in its insured healthcare plan, with no contribution required by the participants.

Expenditures for postemployment healthcare benefits are recognized as insurance premiums become due; during the year, this amount was approximately \$5,400.

# South Macomb Disposal Authority

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## Notes to Financial Statements June 30, 2007

### **Note 8 - Postemployment Benefits (Continued)**

**Upcoming Reporting Change** - The Governmental Accounting Standards Board has recently released Statement Number 45, *Accounting and Reporting by Employers for Postemployment Benefits Other Than Pensions*. The new pronouncement provides guidance for local units of government in recognizing the cost of retiree health care, as well as any "other" postemployment benefits (other than pensions).

The new rules will cause the government-wide financial statements to recognize the cost of providing retiree healthcare coverage over the working life of the employee, rather than at the time the healthcare premiums are paid. The new pronouncement is effective for the year ending June 30, 2010.

### **Note 9 - Prior Period Adjustments**

During the current year, an adjustment was required that related to the Authority's fixed asset value. The required restatement resulted in a prior period adjustment. As a result of the adjustment, the net book value of capital assets has been restated from \$999,161 to \$700,782 as of July 1, 2006.

This restatement occurred due to the Authority continuing to maintain capital assets on its financial statements that were previously disposed with the sale of Sites 9 and 9a.



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December 12, 2007

To the Board of Directors  
South Macomb Disposal Authority  
St. Clair Shores, MI 48080

Dear Board Members:

Beginning with this year's audit, national auditing standards now call for auditors to communicate matters to the governing body that may be useful to you in your oversight of the financial statements of South Macomb Disposal Authority (the "Authority"). Specifically, they require us to report internal control issues to you that may be relatively minor, in order to allow you to evaluate their significance, and make any changes you may deem appropriate. The purpose of these new standards is to allow you an opportunity to discuss issues when they are relatively minor, rather than waiting until they become more serious problems. We hope this new report on internal control will be helpful to you, and we look forward to being able to discuss any questions you may have concerning these issues.

In planning and performing our audit of the financial statements of the Authority as of and for the year ended June 30, 2007, in accordance with auditing standards generally accepted in the United States of America, we considered the Authority's internal control over financial reporting (internal control) as a basis for designing our auditing procedures 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 Authority's internal control. Accordingly, we do not express an opinion on the effectiveness of the Authority's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control that we consider to be significant deficiencies.

A control deficiency 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 misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the following deficiencies to be significant deficiencies in internal controls:

### **Segregation of Duties**

Strong internal controls attempt to segregate the three duties associated with custody, authorization, and recordkeeping for any transaction. Incompatible functions place a person in the position to both perpetrate and conceal errors or fraud in the normal course of his or her duties. Due to its limited staff size, the Authority does not have an adequate segregation of accounting duties due to one individual performing the three duties noted above. The Authority's board has worked to mitigate the risk noted above by reviewing all disbursements before being remitted, initiating wire transfers, and reviewing the overall cash balances and bank statements monthly. However, in order to further strengthen the controls, we suggest that a timely secondary review of the bank reconciliations be done monthly, including evidence through a signoff and date of this procedure by another member of the Authority's management or board. We would also suggest that journal entries posted monthly be reviewed by another member of the Authority's management or board. These enhanced procedures could help to identify errors in a timely manner and improve the overall controls at the Authority.

### **Accrual Adjustments**

The board of directors of the Authority and their staff maintain the books on a cash-type basis during the course of the year. The Authority has continued to assume increasing responsibilities for the calculation and posting of year-end accrual entries by providing the Authority staff with quarterly accounting assistance from an outside source. The Authority has historically and continues to enlist Plante & Moran auditors' assistance in determining the remaining accrual adjustments to the accounting records at the end of the year that are related to the legal liabilities that are required to be disclosed within the financial statements. The board has determined that the processes implemented by the Authority result in the most cost-effective and value-added method of complying with the requirements for full accrual statements. We are pleased to assist in this process as our staff has a high degree of expertise in these types of accrual adjustments.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control. We believe that the significant deficiency noted below is a material weakness:

### **Capital Assets**

During the testing of capital assets during the current year audit, it was discovered that the Authority has capital assets on its books that are no longer in existence. While the Authority has chosen for Plante & Moran to depreciate the Authority's fixed assets on a Plante & Moran depreciation program, Plante & Moran relies on management at the Authority to keep us informed of capital asset additions and deletions so that fixed asset detail is kept up to date. Every year during the audit we are required and do inquire of the Authority if there are any assets that were added, disposed, or impaired. The Authority may want to consider a formal communication between departments when a fixed asset status has changed. During the current year, a material amount of capital assets being maintained on the financial statements was found to no longer exist at the Authority. This situation resulted in a required prior period adjustment to be reflected within the financial statements.

### **New Auditing Standards**

As noted with this year's required changes in auditing procedures, there are even more major and comprehensive changes to the auditing rules that will impact the Authority's audits beginning next year. These new auditing standards require significant changes in how audits are done and how the results of the auditor's work are communicated to clients, bringing governmental auditing rules into closer alignment with the standards imposed on audits of public companies under Sarbanes-Oxley.

These new rules, which are known collectively as the Risk Assessment Standards, require auditors to:

- More thoroughly examine and evaluate clients' accounting processes and controls, including the overall control environment, key controls over significant transactions, and the quality of internal oversight of the financial reporting process
- More thoroughly assess and document conditions in clients' systems and processes that create risks of material misstatement in their financial statements, and perform additional testing in response to these risks
- Design and perform more analytical tests of accounting and financial data
- Apply more stringent standards in identifying, assessing, and communicating internal control deficiencies
- Communicate more information about the results of the auditor's work to individuals involved in overseeing strategic direction and accountability for operations

As a practical effect of these new rules, auditors will need to make more detailed and specific requests for information from clients, particularly about processes and controls, and clients will need to do more work to be well prepared for their audits. The new rules will also require increased audit testing and more thorough auditing procedures, and will increase the amount of related documentation that auditors must prepare and maintain.

Plante & Moran began analyzing these new standards and incorporating the necessary changes into our audit process and tools more than a year ago. It is clear that the new rules will require us to perform more audit procedures than we have done in the past. Our firm has invested heavily to implement our new audit methodology and train our staff on these changes and will continue to do so over the next several months. Our goal is to have our staff trained and working with our clients to prepare for the transition to these new rules well in advance of the required implementation date.

As we move forward, we will be communicating more specifically about how these matters will affect the Authority's next financial statement audit. In addition, we plan to begin work with the Authority's staff during the upcoming year in a number of areas, including review and documentation of internal accounting procedures and controls, to ensure a smooth transition to the new standards.

The primary objective of these new rules is to strengthen and enhance the independent audit of financial statements, including more thorough evaluation and information about the Authority's internal accounting and financial reporting processes and controls. We believe that these new rules and the additional communications the board will receive from us about the results of our audit work will enhance the value received from the financial statement audit.

### **Retiree Healthcare Benefits**

Please keep in mind that beginning on July 1, 2009, new accounting rules will require an actuarial valuation to determine the annual contribution that would be necessary to fund retiree healthcare costs over a 30-year period. While the accounting rules do not (cannot) require you to make any annual contributions to pre-fund this obligation, the liability size will cause the board to have to debate the merits of funding some or all of the recommended contribution.

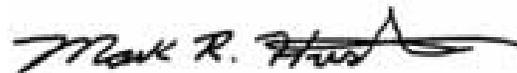
### **Annual Reminder - Reporting Requirements**

As a reminder, the Authority will need to complete a municipal finance qualifying statement online with the State of Michigan by December 31, 2007. The Authority should have been given a password to use in this process. Please call us if you would like assistance in filling it out.

We would like to thank you and your staff for the courtesy and cooperation extended to us during the audit. We appreciate the opportunity to serve you as your auditors. If there are any questions about your financial report or the above comments and recommendations, we would be happy to discuss them at your convenience.

Very truly yours,

**Plante & Moran, PLLC**



Mark R. Hurst



Kathryn J. Kercorian