

CITY OF STOUGHTON

REPORT ON INTERNAL CONTROL

**(Including Memorandum on Accounting Procedures,
Internal Controls, and Other Matters)**

December 31, 2010

CITY OF STOUGHTON

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To the City Council
City of Stoughton
Stoughton, Wisconsin

In planning and performing our audit of the financial statements of the City of Stoughton as of and for the year ended December 31, 2010, in accordance with auditing standards generally accepted in the United States of America, we considered its 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 its internal control. Accordingly, we do not express an opinion on the effectiveness of its internal control.

A separate Report on Internal Control was issued to the Utility Commission. The information contained in that report is not included with this report.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be significant deficiencies or material weaknesses and, therefore, there can be no assurance that all such deficiencies have been identified. However, as discussed below, we identified certain deficiencies in internal control that we consider to be material weaknesses.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the following deficiencies in the city's internal control to be material weaknesses:

- > Internal Control over Financial Reporting
- > Internal Accounting Controls

This communication is intended solely for the information and use of management, the city council and others within the organization and is not intended to be, and should not be, used by anyone other than the specified parties.

Baker Tilly Virchow Krause, LLP

Madison, Wisconsin
May 18, 2011

MATERIAL WEAKNESS – INTERNAL CONTROL OVER FINANCIAL REPORTING

In theory, a properly designed system of internal control staffed with enough people with sufficient training would provide your organization with the ability to not only process and record monthly transactions, but also to prepare a complete set of annual financial statements.

The definition of a material weakness in internal control includes consideration of the year end financial reporting process. To avoid the auditor reporting a material weakness in internal control, your system of controls would need to be able to accomplish the following:

1. Present the books and records to the auditor in such a condition that the auditor is not able to identify any material journal entries as a result of our audit procedures. This is very rare for most of our clients.
2. Be capable of preparing a complete set of year end financial statements for the auditor to test. This includes drafting the individual fund statements, making conversion entries, drafting the government-wide statements, and preparing footnote disclosures. Your staff would need to be capable of presenting the auditor with a set of complete financial statements in such a condition that the auditor is not able to identify any material changes as a result of the audit. Currently, most of our governmental clients have us prepare the financial statement document.

To accomplish such a high level of internal control over financial reporting is a difficult task for most governments. Many large organizations, such as SEC companies, have been required by law to prepare their own statements for years, and are staffed appropriately to do so. Most governments operate with only enough staff to process monthly transactions and reports, and so rely on us to prepare certain year end audit entries and handle the year end financial reporting. Under the new auditing standards, we must, therefore, inform you that these are material weaknesses in your internal control.

MATERIAL WEAKNESS – INTERNAL ACCOUNTING CONTROLS

As a result of our audit procedures, we are required to communicate to you information on specific controls that do not exist, or are not documented by the city. Below is a list of potential controls that should be in place to achieve a higher level of reliability that errors or irregularities in your processes would be discovered by your staff. Keep in mind that some of these controls may not be practical due to your staff size or other reasons. However, we are required to communicate these to you.

CONTROLS OVER ACCOUNTS PAYABLE/DISBURSEMENTS

1. There should be a formal approval of new vendors.
2. There should be controls in place surrounding the identification, recording, and review of retainages and encumbrances at year end.

CONTROLS OVER PROPERTY TAXES

1. Bank reconciliations should be performed by someone independent of the tax collection process.

CONTROLS OVER FINANCIAL REPORTING

1. Account reconciliations should be performed by someone independent of the processing of transactions in the account.
2. Adjusting journal entries and supporting documentation should be reviewed and approved by an appropriate person who is not the original preparer.

MATERIAL WEAKNESS – INTERNAL ACCOUNTING CONTROLS (cont.)

INFORMATION TECHNOLOGY CONTROLS

As part of our audit, we evaluated the information technology controls as they relate to financially significant applications. Our procedures primarily focused on documenting and evaluating general computer controls, including:

- > Logical access to data and applications
- > Change and incident management
- > Systems development and deployment
- > Data backup and recovery

The following points contain suggestions for strengthening internal controls in these areas.

- > The city should require new users to reset their passwords on the first login, force passwords to expire regularly, and create standard policies and procedures to authenticate users to systems and maintain password effectiveness. Best practices suggest that passwords should be changed every 45 days, require a minimum of six characters, and not allow reuse of recent passwords.
- > Access rights for the network and critical applications should be reviewed at least once a year by management to ensure users don't have access beyond their job responsibilities.
- > Currently, your server is located in its own area where most city employees have access. Ideally, physical access to the server should be restricted to only those people who must have access to it.
- > The city's present software system lacks certain security features that, if operated improperly, would not allow for the identification of changes made to financial data after the original entry of such data. This is a situation that exists in many database software packages, including Microsoft Office Access, which is the basis for your software. Many of the system users may not possess the technical knowledge to operate the system in a manner that would impair the system's control integrity. However, it is possible that some users may possess the knowledge to circumvent the system's controls. Therefore, it is our judgment that there is more than a remote possibility that an error could occur in amounts that are more than insignificant, and your controls would not detect them. Accordingly, we are required to communicate this fact to you.

A next step to resolve these issues might be to have a designated person in your organization review these potential controls and make a suggestion on your community's ability and cost (including time) to implement some or all of them. We can assist with that process.

PRIOR YEAR POINTS

COLLATERAL FOR BANK DEPOSITS (PER 12/31/08 LETTER)

Governmental Accounting Standards Board (GASB) Statement No. 40 requires disclosures about various risks associated with the city's deposits and investments. These disclosures can be found in Note IV.A of the financial statements.

One of the required disclosures is custodial credit risk. Custodial credit risk is the risk that in the event of a financial institution failure, the city's deposits may not be returned. To address this risk, the city has collateral agreements with its primary bank to cover deposits in excess of the FDIC limits. However, as of December 31, 2008, \$10,694,035 of the city's total deposits and investments of \$27,015,068 was exposed to custodial credit risk because the collateral was insufficient to cover all city deposits. In addition, the current collateral agreement in place with the city's primary bank allows for the collateral to be held in the trust department of this bank. GASB No. 40 states that this type of custodial arrangement exposes the city to greater risk than if the collateral was held by an independent third party custodian.

Recommendation

We recommend that the city evaluate its current collateral situation to determine if adjustments are desired.

Status (12/31/10)

A total of \$6,662,946 of deposits and investments were exposed to some level of custodial credit risk as of December 31, 2010.

INFORMATIONAL POINTS

DECENTRALIZED CASH COLLECTIONS

As part of our annual audit process, we focus our efforts on the primary accounting systems, internal controls, and procedures used by the city. This is in keeping with our goal to provide an audit opinion which states that the financial statements of the city are correct in all material respects.

In some cases, the primary system of accounting procedures and controls of the city are supported by smaller systems which are decentralized, and reside within a department or outside location. Specifically for the City of Stoughton, there are departments that collect cash and periodically remit those collections to city hall. Examples include the recreation department and senior center, among others.

Generally, the more centralized a function is, the easier it is to design and implement accounting controls that provide some level of checks and balances. That is because you are able to divide certain tasks over the people available to achieve some segregation of duties. For those tasks that are decentralized, it is usually very difficult to provide for proper segregation of duties. Therefore, with one person being involved in most or all aspects of a transaction, you lose the ability to rely on the controls to achieve the safeguarding of assets and reliability of financial records.

In addition to the decentralized collections in departments, there are also organizations outside the city that are collecting money and utilizing the city bank account for depositing and expending funds. Examples of these include the food pantry and holiday donations, among others. These receipts are collected by these organizations and turned over to city hall for deposit. Disbursements are authorized by the organizations and paid through the city disbursement process. In many instances, the individuals collecting funds and authorizing disbursement are not city employees. In addition, there is not a budget for these activities, and as a result city management and the city council have limited control over the operations.

INFORMATIONAL POINTS (cont.)

DECENTRALIZED CASH COLLECTIONS (cont.)

As auditors, we are required to communicate with you on a variety of topics. We believe it is appropriate to make sure that you are informed about the risks that can occur with decentralized cash collections, especially with the activities of the outside organizations utilizing the city bank account. In addition to segregation of duties concerns, the city should be aware of the fiduciary responsibility it maintains for all transactions and activities that run through the city accounting records and bank accounts. For that reason, it is important to regularly assess the decentralized cash collection activities to ensure funds for which the city maintains responsibility are appropriately safeguarded.

TWO WAY COMMUNICATION REGARDING YOUR AUDIT

As part of our audit of your financial statements, we are providing communications to you throughout the audit process. Auditing requirements provide for two-way communication and are important in assisting the auditor and you with more information relevant to the audit.

As this past audit is concluded, we use what we have learned to begin the planning process for next year's audit. It is important that you understand the following points about the scope and timing of our next audit:

- a. We address the significant risks of material misstatement, whether due to fraud or error, through our detailed audit procedures.
- b. We will obtain an understanding of the five components of internal control sufficient to assess the risk of material misstatement of the financial statements whether due to error or fraud, and to design the nature, timing, and extent of further audit procedures. We will obtain a sufficient understanding by performing risk assessment procedures to evaluate the design of controls relevant to an audit of financial statements and to determine whether they have been implemented. We will use such knowledge to:
 - > Identify types of potential misstatements.
 - > Consider factors that affect the risks of material misstatement.
 - > Design tests of controls, when applicable, and substantive procedures.

We will not express an opinion on the effectiveness of internal control over financial reporting or compliance with laws, regulations, and provisions of contracts or grant programs. For audits done in accordance with Government Auditing Standards, our report will contain the following restriction: "This report is intended solely for the information and use of the client's management, others within the city federal and state awarding agencies and pass-through entities and is not intended to be, and should not be, used by anyone other than these specified parties."

- c. The concept of materiality recognizes that some matters, either individually or in the aggregate, are important for fair presentation of financial statements in conformity with generally accepted accounting principles while other matters are not important. In performing the audit, we are concerned with matters that, either individually or in the aggregate, could be material to the financial statements. Our responsibility is to plan and perform the audit to obtain reasonable assurance that material misstatements, whether caused by errors or fraud, are detected.

We are very interested in your views regarding certain matters. Those matters are listed here:

- a. We typically will communicate with your top level of management unless you tell us otherwise.
- b. We understand that the city council has the responsibility to oversee the strategic direction of your organization, as well as the overall accountability of the entity. Management has the responsibility for achieving the objectives of the entity.
- c. We need to know your views about your organization's objectives and strategies, and the related business risks that may result in material misstatements.

INFORMATIONAL POINTS (cont.)

TWO WAY COMMUNICATION REGARDING YOUR AUDIT (cont.)

- d. Which matters do you consider warrant particular attention during the audit, and are there any areas where you request additional procedures to be undertaken?
- e. Have you had any significant communications with regulators?
- f. Are there other matters that you believe are relevant to the audit of the financial statements?

Also, is there anything that we need to know about the attitudes, awareness, and actions of the city concerning:

- a. The city's internal control and its importance in the entity, including how those charged with governance oversee the effectiveness of internal control?
- b. The detection or the possibility of fraud?

We also need to know if you have taken actions in response to developments in financial reporting, laws, accounting standards, governance practices, or other related matters, or in response to previous communications with us.

With regard to the timing of our audit, here is some general information. If necessary, we may do preliminary audit work during the months of October-December, and sometimes early January. Our final fieldwork is scheduled during the spring to best coincide with your readiness and report deadlines. After fieldwork, we wrap up our audit procedures at our office and may issue drafts of our report for your review. Final copies of our report and other communications are issued after approval by your staff. This is typically 6-12 weeks after final fieldwork, but may vary depending on a number of factors.

Keep in mind that while this communication may assist us with planning the scope and timing of the audit, it does not change the auditor's sole responsibility to determine the overall audit strategy and the audit plan, including the nature, timing, and extent of procedures necessary to obtain sufficient appropriate audit evidence.

We realize that you may have questions on what this all means, or wish to provide other feedback. We welcome the opportunity to hear from you.

GASB STATEMENT NO. 54: FUND BALANCE REPORTING

Last year, we informed you that the Governmental Accounting Standards Board (GASB) had issued Statement No. 54, which changes governmental financial reporting. These changes will affect your financial statements for the year ended December 31, 2011, primarily the governmental fund's balance sheet presentation. No changes are necessary for proprietary fund types or government-wide statements. The major change is to the terminology used for fund balance reporting. The terms reserved, unreserved, designated, and undesignated are being replaced with the following categories: nonspendable, restricted, committed, assigned, and unassigned. The new categories are designed to promote more consistent financial reporting throughout the nation.

The GASB made these changes to fund balance reporting to make it easier for the reader of financial statements to determine the various levels of restrictions that exist for the future use of fund balance. In addition to the new method for displaying fund balances, the Statement also clarifies the definitions of the various governmental fund types. You have clarified your financial policies and have identified which fund types are applicable to each of your funds. All that remains is to show the new presentation in your 2011 financial statements next year. We will assist you with that as needed when that time comes.

INFORMATIONAL POINTS (cont.)

CHARITABLE CONTRIBUTIONS – SUBSTANTIATION AND DISCLOSURE

Organizations that receive tax-deductible charitable contributions, such as the city should be aware of two general rules to meet IRS substantiation and disclosure requirements (as noted in IRS Publication 1771) for federal income tax return reporting purposes:

1. A charitable organization is required to provide a **written disclosure** to a donor who receives goods or services in exchange for a single payment in excess of \$75, such as the value of a round of golf or gift certificates.
2. A donor is responsible for obtaining a **contemporaneous written acknowledgment** from a charity for any single contribution of \$250 or more before the donor can claim a charitable contribution on his/her federal income tax return.

The written disclosure statement in 1. above must:

- > inform a donor that the amount of the contribution that is deductible for federal income tax purposes is limited to the excess of money (and the fair market value of property other than money) contributed by the donor over the value of goods or services provided by the organization
- > provide a donor with a good faith estimate of the fair market value of the goods and services
- > be made in a manner that is likely to come to the attention of the donor.

A penalty is imposed on organizations that do not meet the written disclosure requirement. The penalty is \$10 per contribution, not to exceed \$5,000 per fund raising event or mailing.

To assist a donor, an organization can provide a timely, written statement containing the following information:

- > Name of organization
- > Amount of cash contribution
- > Description (but not the value) of non-cash contribution
- > Statement that no goods or services were provided by the organization in return for the contribution, if that was the case
- > Description and good faith estimate of the value of goods or services, if any, that an organization provided in return for the contribution
- > Statement that goods or services, if any, that an organization provided in return for the contribution consisted entirely of intangible religious benefits, if that was the case.

A separate acknowledgment may be provided for each single contribution of \$250 or more, or one acknowledgment, such as an annual summary, may be used to substantiate several single contributions of \$250 or more. Recipient organizations typically send written acknowledgments to donors no later than January 31 of the year following the donation.

We recommend the city review their policies on charitable contributions to ensure they are in compliance with the above requirements.

INFORMATIONAL POINTS (cont.)

ECONOMIC CONDITIONS AND YOUR COMMUNITY

Economic conditions for the nation as a whole have declined in recent years. There has been widespread impact on federal, state, and local governments. To position your community for fiscal stability, you should continue to regularly evaluate many of the topics we've outlined in our letters from prior years, including:

- > Collateralized bank balances
- > Long term borrowing and refinancing plans in a tightening credit market
- > Cash flow impacts of an increase in delinquencies
- > Equalized value changes
- > Tax base impacts of slowed development
- > State budget issues

Suggested steps in proactively planning for these challenges include:

- > Preparing annual budgets that are realistic and accurate
- > Monitoring compliance with the annual budget based on financial records that are accurate and understandable
- > Making amendments to the budget when necessary and determining sources of revenues to cover additional appropriations
- > Developing a fund balance policy to ensure that your community has enough reserves on hand for emergency appropriations
- > Forecasting cash flows as a result of changing economic conditions and developing a plan to address significant issues
- > Forecasting capital needs and anticipated financing available
- > Monitoring your community's debt capacity compared to the limit established by the state
- > Exploring ways to confine costs, such as consolidation of services with other local governments or outsourcing
- > Developing investment policies that address collateralization of deposits and investments

Your community's long-term success is important. As a governing body, your involvement and understanding of your community's financial activities will help you make informed decisions regarding the future of your community. Please feel free to contact us if you have questions – we are happy to discuss these topics in further detail.

REQUIRED COMMUNICATIONS WITH AUDIT COMMITTEE OR ITS EQUIVALENT

OUR RESPONSIBILITY UNDER AUDITING STANDARDS GENERALLY ACCEPTED IN THE UNITED STATES OF AMERICA, GOVERNMENT AUDITING STANDARDS, OMB CIRCULAR A-133 AND THE STATE SINGLE AUDIT GUIDELINES

The objective of a financial statement audit is the expression of an opinion on the financial statements. We conducted the audit in accordance with auditing standards generally accepted in the United States of America, Government Auditing Standards, OMB Circular A-133, and the State Single Audit Guidelines. These standards require that we plan and perform our audit to obtain reasonable, rather than absolute, assurance about whether the financial statements prepared by management with your oversight are free of material misstatement, whether caused by error or fraud. Our audit included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit does not relieve management or the City Council of their responsibilities.

REQUIRED COMMUNICATIONS WITH AUDIT COMMITTEE OR ITS EQUIVALENT (cont.)

OUR RESPONSIBILITY UNDER AUDITING STANDARDS GENERALLY ACCEPTED IN THE UNITED STATES OF AMERICA, GOVERNMENT AUDITING STANDARDS, OMB CIRCULAR A-133 AND THE STATE SINGLE AUDIT GUIDELINES (cont.)

We will also consider the internal control over compliance with requirements that could have a direct and material effect on a major federal or major 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 OMB Circular A-133 and the State Single Audit Guidelines.

As part of obtaining reasonable assurance about whether City of Stoughton's financial statements are free of material misstatement, we will perform tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions is not an objective of our audit. Also, in accordance with OMB Circular A-133 and the State Single Audit Guidelines, we will examine, on a test basis, evidence about City of Stoughton's compliance with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement and the State Single Audit Guidelines applicable to each of its major federal and state programs for the purpose of expressing an opinion on City of Stoughton's compliance with those requirements. While our audit provides a reasonable basis for our opinion, it does not provide a legal determination on City of Stoughton's compliance with those requirements.

We will issue a separate document which contains the results of our audit procedures to comply with OMB Circular A-133 and the State Single Audit Guidelines.

OTHER INFORMATION IN DOCUMENTS CONTAINING AUDITED FINANCIAL STATEMENTS

Our responsibility does not extend beyond the audited financial statements identified in this report. We do not have any obligation to and have not performed any procedures to corroborate other information contained in client prepared documents, such as official statements related to debt issues.

PLANNED SCOPE AND TIMING OF THE AUDIT

We performed the audit according to the planned scope and timing previously communicated to you in our management letter about planning matters dated April 9, 2010, and our meeting with the finance committee and council on April 27, 2010.

QUALITATIVE ASPECTS OF THE ENTITY'S SIGNIFICANT ACCOUNTING PRACTICES

Accounting Policies

Management is responsible 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 the City of Stoughton are described in Note I to the financial statements. No new accounting policies were adopted and the application of existing policies was not changed during 2010. We noted no transactions entered into by the City of Stoughton during the year that were both significant and unusual, and of which, under professional standards, we are required to inform you, or transactions for which there is a lack of authoritative guidance or consensus.

REQUIRED COMMUNICATIONS WITH AUDIT COMMITTEE OR ITS EQUIVALENT (cont.)

QUALITATIVE ASPECTS OF THE ENTITY'S SIGNIFICANT ACCOUNTING PRACTICES (cont.)***Accounting Estimates***

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. The most sensitive estimates affecting the financial statements was the allowance related to uncollectible EMS receivables.

Management's estimate of the allowance for uncollectible EMS receivables is based on historical collections. We evaluated the key factors and assumptions used to develop the allowance of uncollectible EMS receivables in determining that it is reasonable in relation to the financial statements taken as a whole.

Financial Statement Disclosures

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

DIFFICULTIES ENCOUNTERED IN PERFORMING THE AUDIT

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

AUDIT ADJUSTMENTS

Professional standards require us to accumulate all known and likely misstatement identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management.

Management has corrected all such misstatements. The following is a summary of material financial statement misstatements (audit adjustments):

	<u>Amount</u>
Adjustments to long-term debt	\$ 1,015,000
Adjustments to accounts receivable	174,918
Adjustment to transfers	69,286

In addition, we prepare GASB No. 34 conversion entries which are summarized in the "Reconciliation of the Balance Sheet of Governmental Funds to the Statement of Net Assets" and the "Reconciliation of the Statement of Revenues, Expenditures, and Changes in Fund Balances of Governmental Funds to the Statement of Activities" in the financial statements.

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 that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

REQUIRED COMMUNICATIONS WITH AUDIT COMMITTEE OR ITS EQUIVALENT (cont.)

CONSULTATIONS WITH OTHER INDEPENDENT ACCOUNTANTS

In some cases, management may decide to consult with other accountants about auditing and accounting matters. If a consultation involves application of an accounting principle to the governmental unit's financial statements or a determination of the type of auditors' opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

MANAGEMENT REPRESENTATIONS

We have requested certain representations from management that are included in the management representation letter. This letter is attached.

INDEPENDENCE

We are not aware of any relationships between Baker Tilly Virchow Krause, LLP and the city that, in our professional judgment, may reasonably be thought to bear on our independence.

Relating to our audit of the financial statements of for the year ended December 31, 2010, Baker Tilly Virchow Krause, LLP hereby confirms in accordance with the Code of Professional Conduct issued by the American Institute of Certified Public Accountants, that we are, in our professional judgment, independent with respect to the City of Stoughton and provided no services to the City of Stoughton other than audit services provided in connection with the audit of the current year's financial statements and nonaudit services which in our judgment do not impair our independence including:

- > Civic Systems Software
- > Financial Statement Preparation
- > Adjusting Journal Entries
- > Compiled TIF Financial Statements
- > Compiled Regulatory Reports

OTHER AUDIT FINDINGS OR ISSUES

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the City of Stoughton's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

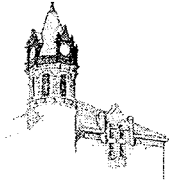
CLOSING

In closing, we would like to thank you for allowing us to serve you. We are very interested in the long-term success of the City of Stoughton and our comments are intended to draw your attention to issues which need to be addressed for the city to meet its goals and responsibilities.

This letter, by its nature, focuses on improvements and does not comment on the many strong areas of the city's systems and procedures. The comments and suggestions in this report are not intended to reflect in any way on the integrity or ability of the personnel of the city. They are made solely in the interest of establishing sound internal control structure practices and improving the city's financial operations. The city's staff seemed genuinely concerned about maintaining the city's financial reporting system so that informed decisions can be made. They were receptive to our ideas, comments and suggestions.

CLOSING (cont.)

We will review the status of these comments during our next audit engagement. We have already discussed the previous comments and suggestions with various city personnel and we would be pleased to discuss them with you in further detail.



CITY OF STOUGHTON

May 18, 2011

Baker Tilly Virchow Krause, LLP
Ten Terrace Court
P.O. Box 7398
Madison, WI 53707-7398

Dear Auditors or Baker Tilly Virchow Krause, LLP:

We are providing this letter in connection with your audit of the financial statements of the City of Stoughton as of December 31, 2010 and for the year then ended for the purpose of expressing an opinion as to whether the financial statements present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of the City of Stoughton and the respective changes in financial position and cash flows, where applicable, in conformity with accounting principles generally accepted in the United States of America. We confirm that we are responsible for the fair presentation of the previously mentioned financial statements in conformity with accounting principles generally accepted in the United States of America. We are also responsible for adopting sound accounting policies, establishing and maintaining internal control, and preventing and detecting fraud.

We confirm, to the best of our knowledge and belief, the following representations made to you during your audit.

1. The financial statements referred to above are fairly presented in conformity with accounting principles generally accepted in the United States of America. We have engaged you to advise us in fulfilling that responsibility. The financial statements include all properly classified funds of the oversight unit and all component units required by accounting principles generally accepted in the United States of America to be included in the financial reporting entity.
2. We have made available to you all –
 - a. Financial records and related data and all audit or relevant monitoring reports, if any, received from funding sources.
 - b. Minutes of the meetings of the city council or summaries of actions of recent meetings for which minutes have not yet been prepared.

3. There have been no communications from regulatory agencies concerning noncompliance with, or deficiencies in, financial reporting practices.
4. There are no material transactions that have not been properly recorded in the accounting records underlying the financial statements or the schedule of expenditures of federal and state awards.
5. All known audit and bookkeeping adjustments have been included in our financial statements, and we are in agreement with those adjustments.
6. We acknowledge our responsibility for the design and implementation of programs and controls to prevent and detect fraud.
7. We have no knowledge of any fraud or suspected fraud affecting the entity involving:
 - a. Management,
 - b. Employees who have significant roles in internal control, or
 - c. Others where the fraud could have a material effect on the financial statements.
8. We have no knowledge of any allegations of fraud or suspected fraud affecting the entity received in communications from employees, former employees, analysts, regulators, or others.
9. We have a process to track the status of audit findings and recommendations.
10. We have identified to you any previous financial audits, attestation engagements, and other studies related to the audit objectives and whether related recommendations have been implemented.
11. We have provided our views on reported findings, conclusions, and recommendations, as well as our planned corrective actions, for our report.
12. The City of Stoughton has no plans or intentions that may materially affect the carrying value or classification of assets, liabilities, or fund equity.

13. The following, if any, have been properly recorded or disclosed in the financial statements:

- a. Related party transactions, including revenues, expenditures/expenses, loans, transfers, leasing arrangements, and guarantees, and amounts receivable from or payable to related parties.
- b. Guarantees, whether written or oral, under which the municipality is contingently liable.
- c. All accounting estimates that could be material to the financial statements including the key factors and significant assumptions underlying those estimates and measurements. We believe the estimates and measurements are reasonable in the circumstances, consistently applied, and adequately disclosed.

14. We are responsible for compliance with the laws, regulations, and provisions of contracts and grant agreements applicable to us, including tax or debt limits and debt contracts; and we have identified and disclosed to you all laws, regulations and provisions of contracts and grant agreements that we believe have a direct and material effect on the determination of financial statement amounts or other financial data significant to the audit objectives, including legal and contractual provisions for reporting specific activities in separate funds.

15. There are no –

- a. Violations or possible violations of budget ordinances, provisions of contracts and grant agreements, laws or regulations including those pertaining to adopting and amending budgets, tax or debt limits, and any related debt covenants whose effects should be considered for disclosure in the financial statements or as a basis for recording a loss contingency, or for reporting on noncompliance.
- b. Unasserted claims or assessments that our lawyer has advised us are probable of assertion and must be disclosed in accordance with Financial Accounting Standards Board (FASB) Statement No. 5, *Accounting for Contingencies*.
- c. Other liabilities or gain or loss contingencies that are required to be accrued or disclosed by FASB Statement No. 5.
- d. Reservations or designation of fund equity that were not properly authorized and approved.
- e. Rates being charged to customers other than the rates as authorized by the applicable authoritative body.
- f. Violations of restrictions placed on revenues as a result of bond resolution covenants such as revenue distribution or debt service funding.

16. The City of Stoughton has satisfactory title to all owned assets, and there are no liens or encumbrances on such assets nor has any asset been pledged as collateral.
17. The city has complied with all aspects of contractual agreements that would have a material effect on the financial statement in the event of noncompliance.
18. We have followed all applicable laws and regulations in adopting, approving, and amending budgets.
19. The financial statements include all component units. There are no joint ventures with an equity interest or other related organizations that should be reported.
20. The financial statements properly classify all funds and activities.
21. All funds that meet the quantitative criteria in GASB Statement No. 34 and No. 37 for presentation as major are identified and presented as such and all other funds that are presented as major are particularly important to financial statement users.
22. Net asset components (invested in capital assets, net of related debt; restricted; and unrestricted) and fund balance reserves and designations are properly classified and, if applicable, approved.
23. Provisions for uncollectible receivables have been properly identified and recorded.
24. Expenses have been appropriately classified in or allocated to functions and programs in the statement of activities, and allocations have been made on a reasonable basis.
25. Revenues are appropriately classified in the statement of activities within program revenues and general revenues.
26. Interfund, internal, and intra-entity activity and balances have been appropriately classified and reported.
27. Deposits and investment securities are properly classified as to risk, and investments are properly valued.
28. The city has no derivative financial instruments such as contracts that could be assigned to someone else or net settled, interest rate swaps, collars or caps.
29. Capital assets, including infrastructure assets, are properly capitalized, reported, and, if applicable, depreciated.

30. We acknowledge our responsibility for the required supplementary information (RSI). The RSI is measured and presented within prescribed guidelines and the methods of measurement and presentation have not changed from those used in the prior period. We have disclosed to you any significant assumptions and interpretations underlying the measurement and presentation of the RSI.
31. In regards to the nonattest services performed by you listed below, we have 1) made all management decisions and performed all management functions; 2) designated an individual with suitable skill, knowledge, or experience to oversee the services; 3) evaluated the adequacy and results of the services performed, and 4) accepted responsibility for the results of the services.
 - a. Financial statement preparation
 - b. Adjusting journal entries
 - c. Schedule of Expenditures of Federal and State Awards preparation
 - d. Compiled TIF financial statements
 - e. Compiled regulatory reports
 - f. Civic Systems software
32. With respect to federal and state award programs –
 - a. We are responsible for understanding and complying with and have complied with the requirements of the Single Audit Act Amendments of 1996, OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, the State Single Audit Guidelines, including requirements relating to preparation of the schedule of expenditures of federal and state awards.
 - b. We have, in accordance with OMB Circular A-133, identified in the schedule of expenditures of federal and state awards, expenditures made during the audit period for all awards provided by federal and state agencies in the form of grants, federal and state cost-reimbursement contracts, loans, loan guarantees, property (including donated surplus property), cooperative agreements, interest subsidies, food commodities, direct appropriations, insurance and other assistance received for the purpose of administering federal and state programs. We have also made records available to you relating to such financial awards received directly, as well as indirectly, as pass-through awards.
 - c. We acknowledge our responsibility for presenting the schedule of expenditures of federal awards (SEFA) in accordance with the requirements of OMB Circular A-133 §310.b, and we believe the SEFA, including its form and content, is fairly presented in accordance with the Circular. The methods of measurement and presentation of the SEFA have not changed from those used in the prior period and we have disclosed to you any significant assumptions and interpretations underlying the measurement and presentation of the SEFA.
 - d. We have identified and disclosed to you all of our government programs and related activities subject to OMB Circular A-133 and the State Single Audit Guidelines.
 - e. We are responsible for understanding and complying with, and have complied with in all material respects, the requirements of laws, regulations, and the provisions of contracts and grant agreements related to each of our federal and state programs and have identified and disclosed to you the requirements of laws, regulations, and the provisions of contracts and grant agreements that are considered to have a direct and material effect on each major federal and state program.

32.(cont.)

- f. We are responsible for establishing and maintaining, and have established and maintained, effective internal control over compliance requirements applicable to federal and state programs that provide reasonable assurance that we are administering our federal and state awards in compliance with laws, regulations, and the provisions of contracts and grant agreements that could have a material effect on our federal and state programs. We believe the internal control system is adequate and is functioning as intended. Also, no changes have been made in the internal control over compliance or other factors to the date of this letter that might significantly affect internal control, including any corrective action taken with regard to control deficiencies reported in the schedule of findings and questioned costs.
- g. We have made available to you all contracts and grant agreements (including amendments, if any) and any other correspondence relevant to the programs and related activities subject to the governmental audit requirement.
- h. We have received no requests from a federal or state agency to audit one or more specific programs as a major program.
- i. We have complied, in all material respects, with the compliance requirements, including when applicable, those set forth in the OMB Circular A-133 Compliance Supplement and the State Single Audit Guidelines, relating to federal and state awards and have identified and disclosed to you all amounts questioned and any known noncompliance with the requirements of federal and state awards, including the results of other audits or program reviews.
- j. We have disclosed to you all known noncompliance with the applicable compliance requirements subsequent to the period covered by the auditors' report.
- k. We are not aware of any instances of noncompliance with the applicable compliance requirements subsequent to the period covered by the auditors' report.
- l. We have disclosed any communications from grantors and pass-through entities concerning possible noncompliance with the applicable compliance requirements, if any, including communications received from the end of the period covered by the compliance audit to the date of the auditors' report.
- m. We have disclosed to you the findings received and related corrective actions taken for previous audits, attestation agreements, and internal or external monitoring that directly relates to the objectives of the compliance audit, if any, including findings received and corrective actions taken up to the date of the auditors' report.
- n. Amounts claimed or used for matching were determined in accordance with relevant guidelines in OMB Circular A-87, *Cost Principles for State, Local, and Tribal Governments*, and OMB's *Uniform Administrative Requirements for Grants and Cooperative Agreements to State and Local Governments*.
- o. We have disclosed to you our interpretation of compliance requirements that are subject to varying interpretations, if any.
- p. We have charged costs to federal and state awards in accordance with applicable cost principles.
- q. We have made available to you all documentation related to the compliance requirements, including information related to federal and state program financial reports and claims for advances and reimbursements.

Baker Tilly Virchow Krause, LLP

(Date)
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32.(cont.)

- r. Federal and state program financial reports and claims for advances and reimbursements are supported by the books and records from which the financial statements have been prepared.
- s. The copies of federal and state program financial reports provided you are true copies of the reports submitted, or electronically transmitted, to the respective federal and state agency or pass-through entity, as applicable.
- t. We are responsible for and have accurately prepared the summary schedule of prior audit findings to include all findings required to be included by OMB Circular A-133 and the State Single Audit Guidelines and we have provided you with all information on the status of the follow-up on prior audit findings by federal and state awarding agencies and pass-through entities, including all management decisions.
- u. We are responsible for and have accurately prepared the auditee section of the Data Collection Form as required by OMB Circular A-133.
- v. We are responsible for preparing and implementing a corrective action plan for each audit finding.

To the best of our knowledge and belief, no events, including instances of noncompliance, have occurred subsequent to the balance sheet date and through the date of this letter that would require adjustment to or disclosure in the aforementioned financial statements.

Sincerely,

CITY OF STOUGHTON

Signed: Donna Olson
Donna Olson, Mayor

Signed: Laurie Sullivan
Laurie Sullivan, Finance Director