

# Town of Chesapeake Beach, Maryland

Report to the Mayor and Town Council  
December 1, 2014



Assurance ■ Tax ■ Consulting



December 1, 2014

Mayor and Town Council of Chesapeake Beach, Maryland  
8200 Bayside Road  
Chesapeake Beach, Maryland 20732

Attention: Honorable Mayor Wahl and Members of Town Council

We are pleased to present this report related to our audit of the basic financial statements of the Town of Chesapeake Beach, Maryland (the Town) for the year ended June 30, 2014. This report summarizes certain matters required by professional standards to be communicated to you in your oversight responsibility for the Town's financial reporting process.

This report is intended solely for the information and use of the Mayor and Town Council and is not intended to be, and should not be, used by anyone other than these specified parties. It will be our pleasure to respond to any questions you have about this report. We appreciate the opportunity to continue to be of service to the Town.

*McGladrey LLP*

# Contents

---

Required Communications	1–4
Summary of Significant Accounting Estimates	5
Summary of Recorded Audit Adjustments	6
Summary of Uncorrected Misstatements	7
Exhibit A—Letter Communicating Significant Deficiencies in Internal Control Over Financial Reporting	
Independent Auditor's Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>	
Independent Auditor's Report on Compliance for Each Major Program; Report on Internal Control Over Compliance; and Report on Schedule of Expenditures of Federal Awards Required by OMB Circular A-133	
Schedule of Findings and Questioned Costs	
Exhibit B—Material Written Communications Between Management and Our Firm	
Representation Letter	

---

# Required Communications

Generally accepted auditing standards (AU-C 260, *The Auditor's Communication With Those Charged With Governance*) require the auditor to promote effective two-way communication between the auditor and those charged with governance. Consistent with this requirement, the following summarizes our responsibilities regarding the basic financial statement audit as well as observations arising from our audit that are significant and relevant to your responsibility to oversee the financial reporting process.

Area	Comments
<b>Our Responsibilities With Regard to the Financial Statement Audit</b>	Our responsibilities under auditing standards generally accepted in the United States of America and <i>Government Auditing Standards</i> , issued by the Comptroller General of the United States, have been described to you in our arrangement letter dated July 11, 2014.
<b>Overview of the Planned Scope and Timing of the Financial Statement Audit</b>	We have issued a separate communication regarding the planned scope and timing of our audit and have discussed with you our identification of and planned audit response to significant risks of material misstatement.
<b>Accounting Policies and Practices</b>	<p><b>Preferability of Accounting Policies and Practices</b> Under generally accepted accounting principles, in certain circumstances, management may select among alternative accounting practices. In our view, in such circumstances, management has selected the preferable accounting practice.</p> <p><b>Adoption of, or Change in, Accounting Policies</b> Management has the ultimate responsibility for the appropriateness of the accounting policies used by the Town. Following is a description of significant accounting policies or their application that were either initially selected or changed during the year or otherwise considered to be not applicable to the Town:</p> <ul style="list-style-type: none"> <li>• GASB Statement Number 65, <i>Items Previously Reported as Assets and Liabilities</i>, was required to be adopted by the Town beginning with the year ended June 30, 2014. Concepts Statement No. 4, <i>Elements of Financial Statements</i>, specified that the use of deferred outflows and inflows should be limited to instances identified in authoritative pronouncements. Consequently, this Statement provides guidance to define which balances being reported as assets and liabilities should actually be reported as deferred outflows of resources or deferred inflows of resources, according to definitions in Concepts Statement No. 4. In addition, this Statement recognizes certain items currently being reported as assets and liabilities as outflows of resources and inflows of resources. Under the new guidance, debt issuance costs are no longer presented as an asset to be amortized over the life of the debt, but are to be expensed in the year in which incurred. <i>The adoption of this Statement resulted in the restatement of previous year's beginning net position as further discussed in Note 11 to the financial statements.</i></li> </ul>

Area	Comments
	<ul style="list-style-type: none"> <li> <p>GASB Statement Number 66, <i>Technical Corrections—2012</i>, was required to be adopted by the Town beginning with the year ending June 30, 2014. This Statement amends Statement No. 10, <i>Accounting and Financial Reporting for Risk Financing and Related Insurance Issues</i>, by removing the provision that limits fund-based reporting of a state and local government's risk financing activities to the general fund and the internal service fund type. As a result, governments would base their decisions about governmental fund type usage for risk financing activities on the definitions in Statement No. 54, <i>Fund Balance Reporting and Governmental Fund Type Definitions</i>. This Statement also amends Statement No. 62, <i>Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements</i>, by modifying the specific guidance on accounting for (1) operating lease payments that vary from straight-line basis, (2) the difference between the initial investment (purchase price) and the principal amount of a purchased loan or group of loans, and (3) servicing fees related to mortgage loans that are sold when the stated service fee rate differs significantly from a current (normal) servicing fee rate. These changes would eliminate any uncertainty regarding the application of Statement No. 13, <i>Accounting for Operating Leases with Scheduled Rent Increases</i>, and result in guidance that is consistent with the requirements in Statement No. 48, <i>Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues</i>, respectively. <i>The adoption of this Statement had no significant effect on the Town's financial statements as of and for the year ended June 30, 2014.</i></p> </li> <li> <p>GASB Statement No. 67, <i>Financial Reporting for Pension Plans</i>, was required to be adopted by the Town beginning with the year ending June 30, 2014. This Statement replaces the requirements of GASB Statements No. 25 and No. 50 as they relate to pension plans that are administered through trusts or similar arrangements meeting certain criteria. This Statement builds upon the existing framework for financial reports of defined benefit pension plans, which includes a statement of fiduciary net position (the amount held in a trust for paying retirement benefits) and a statement of changes in fiduciary net position. It requires enhanced note disclosures and required supplementary information for both defined benefit and defined contribution pension plans. In addition, it requires the presentation of new information about annual money-weighted rates of return in the notes to the financial statements and in ten-year required supplementary information schedules. <i>The adoption of this Statement had no significant effect on the Town's financial statements as of and for the year ended June 30, 2014.</i></p> </li> </ul>

Area	Comments
	<ul style="list-style-type: none"> <li> <p>GASB Statement No. 70, <i>Accounting and Financial Reporting for Nonexchange Financial Guarantees</i>, was required to be adopted by the Town beginning with the year ending June 30, 2014. This Statement requires a government that extends a nonexchange financial guarantee to recognize a liability when qualitative factors and historical data, if any, indicate that it is more likely than not that the government will be required to make a payment on the guarantee. The amount of the liability to be recognized should be the discounted present value of the best estimate of the future outflows expected to be incurred as a result of the guarantee. When there is no best estimate but a range of the estimated future outflows can be established, the amount of the liability to be recognized should be the discounted present value of the minimum amount within the range. This Statement requires a government that has issued an obligation guaranteed in a nonexchange transaction to report the obligation until legally released as an obligor. This Statement also requires a government that is required to repay a guarantor for making a payment on a guaranteed obligation or legally assuming the guaranteed obligation to continue to recognize a liability until legally released as an obligor. When a government is released as an obligor, the government should recognize revenue as a result of being relieved of the obligation. This Statement also provides additional guidance for intra-entity nonexchange financial guarantees involving blended component units. This Statement specifies the information required to be disclosed by governments that extend nonexchange financial guarantees. In addition, this Statement requires new information to be disclosed by governments that receive nonexchange financial guarantees. <i>The adoption of this Statement had no significant effect on the Town's financial statements as of and for the year ended June 30, 2014.</i></p> </li> </ul> <p>The Town's management has not yet determined the effect issued, but not adopted statements will have on the Town's basic financial statements. A brief summary of each of the Statements below is disclosed in Note 12 to the basic financial statements:</p> <ul style="list-style-type: none"> <li> <p>GASB Statement No. 68, <i>Accounting for Pensions by State and Local Governmental Employers</i></p> </li> <li> <p>GASB Statement No. 69, <i>Government Combinations and Disposals of Government Operations</i></p> </li> <li> <p>GASB Statement No. 71, <i>Pension Transition for Contributions Made Subsequent to the Measurement Date – an amendment of GASB Statement No. 68</i></p> </li> </ul>

Area	Comments
	<p><b>Significant or Unusual Transactions</b>  Following is a description of the method used to account for significant or unusual transactions entered into by the Town during the year ended June 30, 2014.</p> <ul style="list-style-type: none"> <li>The Maryland Department of the Environment (MDE) paid construction costs pertaining to the Enhanced Nutrient Removal (ENR) upgrade project at the wastewater treatment plant in the amount of \$3,092,467 during the year ended June 30, 2014, from a grant received through the Bay Restoration Fund. The Town recognized revenue and construction in process costs for its ownership proportionate amount of 49.66% or \$1,535,719 in the Utility Fund for the year ended June 30, 2014.</li> </ul>
	<p><b>Management's Judgments and Accounting Estimates</b>  Summary information about the process used by management in formulating particularly sensitive accounting estimates and about our conclusions regarding the reasonableness of those estimates is in the attached Summary of Significant Accounting Estimates.</p>
<b>Audit Adjustments</b>	<p>Audit adjustments proposed by us and recorded by the Town are shown in the attached Summary of Recorded Audit Adjustments.</p>
<b>Uncorrected Misstatements</b>	<p>Uncorrected misstatements are summarized in the attached Summary of Uncorrected Misstatements.</p>
<b>Disagreements With Management</b>	<p>We encountered no disagreements with management over the application of significant accounting principles, the basis for management's judgments on any significant matters, the scope of the audit, or significant disclosures to be included in the basic financial statements.</p>
<b>Consultations With Other Accountants</b>	<p>We are not aware of any consultations management had with other accountants about accounting or auditing matters.</p>
<b>Significant Issues Discussed With Management</b>	<p>No significant issues arising from the audit were discussed with or were the subject of correspondence with management.</p>
<b>Significant Difficulties Encountered in Performing the Audit</b>	<p>We did not encounter any significant difficulties in dealing with management during the audit.</p>
<b>Letter Communicating Significant Deficiencies in Internal Control over Financial Reporting</b>	<p>We have separately communicated the significant deficiencies in internal control over financial reporting identified during our audit of the basic financial statements and major awards, as required by <i>Government Auditing Standards</i> and OMB Circular A-133. This communication is attached as Exhibit A.</p>
<b>Material Written Communications Between Management and Our Firm</b>	<p>Copies of material written communications between our firm and the management of the Town, including the representation letter provided to us by management, are attached as Exhibit B.</p>

# Town of Chesapeake Beach, Maryland

## Summary of Significant Accounting Estimates

### Year Ended June 30, 2014

Accounting estimates are an integral part of the preparation of financial statements and are based upon management's current judgment. The process used by management encompasses their knowledge and experience about past and current events and certain assumptions about future events. You may wish to monitor throughout the year the process used to determine and record these accounting estimates. The following describes the significant accounting estimates reflected in the Town's June 30, 2014, basic financial statements:

<b>Estimate</b>	<b>Accounting Policy</b>	<b>Management's Estimation Process</b>	<b>Basis for Our Conclusions on Reasonableness of Estimate</b>
<b>Estimated useful lives of capital assets</b>	Capital assets are depreciated over the estimated useful life.	<p>On an annual basis, the Town determines the estimated useful life based upon asset categories.</p> <p>The Town typically utilizes the following useful lives by asset category: buildings 10-75 years; improvements other than buildings 2-50 years, machinery and equipment 5-20 years, and infrastructure 5-45 years.</p>	We obtained the useful lives assigned to fixed assets in each asset category and determined that they were reasonable in relation to the actual life of similar assets (based upon disposal trends) and consistent with industry practices.



# Town of Chesapeake Beach, Maryland

## Summary of Recorded Audit Adjustments

### Year Ended June 30, 2014

Description	Effect—Increase (Decrease)				
	Assets	Liabilities	Equity	Revenue	Expense
To adjust revenue to confirmed amounts					
General Fund	\$ 45,451	\$ -	\$ -	\$ 45,451	\$ -
To correct for differences between beginning fund balance per trial balance and prior year financial statements					
General Fund	-	-	3,498	-	3,498
To record property tax receivables and unavailable revenue as deferred inflow of resources					
General Fund	46,132	11,697	-	34,435	-
To adjust accrued interest					
Utility Fund	-	(5,783)	-	-	(5,783)
To correct interfund balances					
General Fund	216	-	-	753	537
Water Park Fund	-	(607)	-	-	(607)
Utility Fund	5,574	-	-	-	(5,574)
To correct year end payroll accrual					
General Fund	-	1,972	-	-	1,972
Water Park Fund	-	(68,674)	-	-	(68,674)
To record capitalized interest on ENR Project					
Utility Fund	43,401	-	-	-	(43,401)
To remove duplicate ENR Grant revenue					
Utility Fund	(118,293)	-	-	(118,293)	-
To remove bond issuance costs upon adoption of GASB 65					
Utility Fund	(33,900)	-	(33,900)	-	-
Total Effect	-	-	80,378	\$ (37,654)	\$ (118,032)
Total Balance Sheet Effect	\$ (11,419)	\$ (61,395)	\$ 49,976		

# Town of Chesapeake Beach, Maryland

## Summary of Uncorrected Misstatements

### Year Ended June 30, 2014

#### Opinion Unit:

Governmental Activities and General Fund

Description	Effect—Increase (Decrease)				
	Assets	Liabilities	Equity	Revenue	Expense
<b><u>Carryover Impact From Previous Years</u></b>	\$ -	\$ -	\$ 19,681	\$ -	\$ 19,681
<b><u>Current Year Misstatements:</u></b>					
<u>Known Misstatements:</u>					
None.	-	-	-	-	-
<u>Differences with Estimates:</u>					
None.	-	-	-	-	-
<u>Projected Misstatements:</u>					
None.	-	-	-	-	-
Total Effect	-	-	(19,681)	\$ -	\$ 19,681
Balance Sheet Effect	\$ -	\$ -	\$ -		

#### Opinion Unit:

Water Park Fund

Description	Effect—Increase (Decrease)				
	Assets	Liabilities	Equity	Revenue	Expense
<b><u>Carryover Impact From Previous Years</u></b>	\$ -	\$ -	\$ 602	\$ -	\$ 602
<b><u>Current Year Misstatements:</u></b>					
<u>Known Misstatements:</u>					
None.	-	-	-	-	-
<u>Differences with Estimates:</u>					
None.	-	-	-	-	-
<u>Projected Misstatements:</u>					
None.	-	-	-	-	-
Total Effect	-	-	(602)	\$ -	\$ 602
Balance Sheet Effect	\$ -	\$ -	\$ -		

**Exhibit A—Letter Communicating Significant  
Deficiencies in Internal Control Over Financial  
Reporting**



**Independent Auditor's Report on Internal Control Over Financial Reporting  
and on Compliance and Other Matters Based on an Audit of Financial  
Statements Performed in Accordance With *Government Auditing Standards***

Honorable Mayor and Town Council  
Town of Chesapeake Beach, Maryland

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities, the business-type activities, and each major fund of the Town of Chesapeake Beach, Maryland (the Town), as of and for the year ended June 30, 2014, and the related notes to the financial statements, which collectively comprise the Town's basic financial statements, and have issued our report thereon dated December 1, 2014.

**Internal Control Over Financial Reporting**

In planning and performing our audit of the financial statements, we considered the Town's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Town's internal control. Accordingly, we do not express an opinion on the effectiveness of the Town's internal control.

*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 Town's financial statements will not be prevented, or detected and corrected, on a timely basis. A *significant* deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

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 material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. We did identify certain deficiencies in internal control, described in the accompanying schedule of findings and questioned costs as findings 2014-001 and 2014-002 that we consider to be significant deficiencies.

**Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the Town's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, 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 was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

**Town of Chesapeake Beach, Maryland's Response to Finding**

The Town's response to the findings identified in our audit is described in the accompanying schedule of findings and questioned costs. The Town's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

**Purpose of this Report**

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Town's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Town's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

A handwritten signature in black ink that reads "McGladrey LLP". The signature is written in a cursive, flowing style.

Frederick, Maryland  
December 1, 2014



**Independent Auditor's Report on Compliance for Each Major Program;  
Report on Internal Control Over Compliance; and Report on Schedule of  
Expenditures of Federal Awards Required by OMB Circular A-133**

Mayor and Town Council  
Town of Chesapeake Beach, Maryland

**Report on Compliance for Each Major Federal Program**

We have audited the Town of Chesapeake Beach, Maryland's (the Town) compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on the Town's major federal program for the year ended June 30, 2014. The Town's major federal program is identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

***Management's Responsibility***

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its federal programs.

***Auditor's Responsibility***

Our responsibility is to express an opinion on compliance for the Town's major federal program based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on the major federal program occurred. An audit includes examining, on a test basis, evidence about the Town's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for the major federal program. However, our audit does not provide a legal determination of the Town's compliance.

***Opinion on Each Major Federal Program***

In our opinion, the Town complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on its major federal program for the year ended June 30, 2014.

**Report on Internal Control Over Compliance**

Management of the Town is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the Town's internal control over compliance with the types of requirements that could have a direct and material effect on its major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for the major federal program and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Town's internal control over compliance.

*A deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.

#### **Report on Schedule of Expenditures of Federal Awards Required by OMB Circular A-133**

We have audited the financial statements of the governmental activities, the business-type activities, and each major fund of the Town as of and for the year ended June 30, 2014, and the related notes to the financial statements, which collectively comprise the Town's basic financial statements. We issued our report thereon dated December 1, 2014, which contained unmodified opinions on those financial statements. Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the basic financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of expenditure of federal awards is fairly stated in all material respects in relation to the basic financial statements as a whole.



Frederick, Maryland  
December 1, 2014

**Town of Chesapeake Beach, Maryland**

**Schedule of Findings and Questioned Costs  
Year Ended June 30, 2014**

---

**Section I. Summary of Auditor's Results**

Financial Statements

Type of auditor's report issued:

Unmodified

Internal control over financial reporting:

- Material weakness(es) identified?
- Significant deficiency(ies) identified?

       Yes        X   No  
  X   Yes             None Reported

Noncompliance material to financial statements noted?

       Yes        X   No

Federal Awards

Internal control over major programs:

- Material weakness(es) identified?
- Significant deficiency(ies) identified?

       Yes        X   No  
       Yes        X   None Reported

Type of auditor's report issued on compliance  
for major programs:

Unmodified

Any auditor findings disclosed that are required  
to be reported in accordance with Section 510(a)  
of OMB Circular A-133?

       Yes        X   No

Identification of major programs:

CFDA Number

66.202

Name of Federal Program or Cluster

EPA Congressionally Mandated  
Projects

Dollar threshold used to distinguish between  
Type A and Type B programs:

\$ 300,000

Auditee qualified as low-risk auditee?

       Yes        X   No

(Continued)



**Town of Chesapeake Beach, Maryland**

**Schedule of Findings and Questioned Costs (Continued)**  
**Year Ended June 30, 2014**

---

**Section II. Financial Statement Findings**

*Internal Control*

***Finding 2014-001: Financial Reporting in Accordance With Generally Accounting Principles (GAAP) – Significant Deficiency***

*Criteria:* Management is responsible for the financial statements in accordance with GAAP and related internal controls. As such, the Town's internal controls over accounting reconciliations and financial reporting should ensure accurate financial statements prepared in a timely manner and audit adjustments should be few, if any.

*Condition:* There were significant delays in the receipt of final reconciled trial balances in order to begin the audit of the financial statements for the year ended June 30, 2014.

*Context:* During our current year audit testing, we noted that various general ledger accounts were not reconciled in a timely fashion, as such there were numerous audit adjustments posted to the unadjusted trial balances in order for the general ledger to be in accordance with GAAP.

*Effect:* The Town's ability to produce timely accurate financial statements in accordance with GAAP was hampered. Several year-end receivables and intergovernmental revenues as well as year-end accrued liabilities were either not recorded or were recorded in duplicate. Overall audit adjustments resulted in a decrease of assets by \$11,419, increase in net position of \$49,976, and an increase in change in net position of \$80,378.

*Cause:* The Town's key financial position (Town Treasurer) in the oversight of internal control and financial reporting processes was vacant a majority of the year with a new Town Treasurer being hired the week before the commencement of the audit fieldwork, which was delayed nearly four weeks from previous years.

*Recommendation:* We recommend that the Town ensure that the appropriate resources are available at all times in order to provide adequate internal control over accounting reconciliation and financial reporting processes to provide timely accurate financial statements in accordance with GAAP.

*Views of Responsible Officials and Planned Corrective Actions:* Management acknowledges the breakdown of controls associated with the lack of resources during the year. The Town has filled the vacant Treasurer position and will develop procedures to ensure appropriate resources are available at all times.

**Town of Chesapeake Beach, Maryland**

**Schedule of Findings and Questioned Costs (Continued)**  
**Year Ended June 30, 2014**

---

***Finding 2014-002: Segregation of Duties – Significant Deficiency***

*Criteria:* Management is responsible for internal controls over financial reporting. As such, the Town's internal controls over financial reporting should ensure that accounting functions allow for segregation of duties in the processing of transactions.

*Condition:* During a portion of the year ended June 30, 2014, there was a lack of segregation of duties over certain accounting functions.

*Context:* During our understanding of internal controls, we noted that during the vacancy of the Treasurer's position, from November 2013 through October 2014, the Acting Treasurer was performing the functions of both the Treasurer and Assistant Treasurer. As such, the Acting Treasurer had the ability to record general journal entries, record and process invoices for payment, sign checks, authorize payroll transmissions with ADP, and perform monthly bank reconciliations without an independent review and approval. Even though the Acting Treasurer did have these incompatible capabilities, we also noted that the Mayor and Town Administrator increased their oversight and review roles during the vacancy. However, we noted that this increased review process was not always formally documented.

*Effect:* The risk of financial reporting misstatements and the risk of misappropriation of assets due to fraud or an employee's unintentional error are greatly heightened when someone with financial reporting responsibilities has the ability to perform incompatible functions within the internal control system.

*Cause:* The Town's Treasurer position was vacant a majority of the year. During this time period, the Acting Treasurer was required to perform the functions of both the Treasurer and Assistant Treasurer.

*Recommendation:* We recommend that the Town implement procedures to ensure that appropriate segregation of duties is maintained at all times. Subsequent to June 30, 2014, we noted that Town Treasurer position as filled and the Acting Treasurer resumed their role of Assistant Treasurer.

*Views of Responsible Officials and Planned Corrective Actions:* Management acknowledges the breakdown of controls associated with the lack of resources during the year. The Town has filled the vacant Treasurer position and will develop procedures to ensure appropriate segregation of duties is maintained at all times.

**Compliance**

No matters were reported.

**Section III. Findings and Questioned Costs for Federal Awards**

No matters were reported.

## **Exhibit B—Material Written Communications Between Management and Our Firm**



OFFICE OF THE MAYOR AND TOWN COUNCIL

December 1, 2014

McGladrey LLP  
5291 Corporate Drive, Suite 100  
Frederick, Maryland 21703

This representation letter is provided in connection with your audit of the basic financial statements of the Town of Chesapeake Beach, Maryland which comprise the governmental activities, the business-type activities, and each major fund as of and for the year-ended June 30, 2014 for the purpose of expressing an opinion on whether the financial statements are presented fairly, in all material respects, in accordance with accounting principles generally accepted in the United States (U.S. GAAP).

We confirm, to the best of our knowledge and belief, that as of December 1, 2014:

*Financial Statements*

1. We have fulfilled our responsibilities, as set out in the terms of the audit arrangement letter dated July 11, 2014, for the preparation and fair presentation of the financial statements referred to above in accordance with U.S. GAAP.
2. We acknowledge our responsibility for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.
3. We acknowledge our responsibility for the design, implementation, and maintenance of internal control to prevent and detect fraud.
4. Significant assumptions used by us in making accounting estimates, including those measured at fair value, are reasonable and reflect our judgment based on our knowledge and experience about past and current events and our assumptions about conditions we expect to exist and courses of action we expect to take.
5. Related party relationships and transactions have been appropriately accounted for and disclosed in accordance with the requirements of U.S. GAAP. Specifically we represent that we have appropriately recorded the Town's portion of operating and capital costs associated with the wastewater treatment plant within the Utility Fund and have provided all members of the interjurisdictional agreement a detailed accounting of each member's respective share of operating and capital costs of the treatment plant.
6. All events subsequent to the date of the financial statements and for which U.S. GAAP requires adjustment or disclosure have been adjusted or disclosed.
7. The effects of all known actual or possible litigation and claims have been accounted for and disclosed in accordance with U.S. GAAP.
8. We have not completed the process of evaluating the effect that will result from adopting the guidance in Governmental Accounting Standards Board (GASB) Statement No. 68, *Accounting for Pensions by State and Local Governmental Employers*, Statement No. 69, *Government Combinations and Disposals of Government Operations*, and Statement No. 71, *Pension Transition*

*for Contributions Made Subsequent to the Measurement Date – an amendment of GASB Statement No. 68, as discussed in Note 25. The Town is therefore unable to disclose the effect that adopting these GASB Statements will have on its financial statements. We believe that the adoption of GASB Statement No. 65 as disclosed in Note 11 is appropriate and clearly stated.*

9. We have no direct or indirect, legal or moral obligation for any debt of any organization, public or private.
10. We have complied with all aspects of contractual agreements that would have a material effect on the financial statements in the event of noncompliance.
11. We have informed you of all uncorrected misstatements.

As of and for the Year Ended June 30, 2014

We believe that the effects of the uncorrected misstatements aggregated by you and summarized below are immaterial, both individually and in the aggregate, to the financial statements taken as a whole. For purposes of this representation, we consider items to be material, regardless of their size, if they involve the misstatement or omission of accounting information that, in light of surrounding circumstances, makes it probable that the judgment of a reasonable person relying on the information would be changed or influenced by the omission or misstatement.

**Opinion Unit:**

Governmental Activities and General Fund

Description	Effect — Increase (Decrease)				
	Assets	Liabilities	Equity	Revenue	Expense
<b>Carryover Impact From Previous Years</b>	\$ -	\$ -	\$ 19,681	\$ -	\$ 19,681
<b>Current Year Misstatements:</b>					
<u>Known Misstatements:</u>					
None.	-	-	-	-	-
<u>Differences with Estimates:</u>					
None.	-	-	-	-	-
<u>Projected Misstatements:</u>					
None.	-	-	-	-	-
<b>Total Effect</b>	-	-	(19,681)	\$ -	\$ 19,681
<b>Balance Sheet Effect</b>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>		

**Opinion Unit:**  
**Water Park Fund**

Description	Effect — Increase (Decrease)				
	Assets	Liabilities	Equity	Revenue	Expense
<b><u>Carryover Impact From Previous Years</u></b>	\$ -	\$ -	\$ 602	\$ -	\$ 602
<b><u>Current Year Misstatements:</u></b>					
<u>Known Misstatements:</u>					
None.	-	-	-	-	-
<u>Differences with Estimates:</u>					
None.	-	-	-	-	-
<u>Projected Misstatements:</u>					
None.	-	-	-	-	-
<b>Total Effect</b>	-	-	(602)	\$ -	\$ 602
<b>Balance Sheet Effect</b>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>		

*Information Provided*

12. We have provided you with:
  - a. Access to all information, of which we are aware that is relevant to the preparation and fair presentation of the financial statements such as records, documentation, and other matters.
  - b. Additional information that you have requested from us for the purpose of the audit.
  - c. Unrestricted access to persons within the entity from whom you determined it necessary to obtain audit evidence.
  - d. Minutes of the meetings of Town Council and committees thereof, or summaries of actions of recent meetings for which minutes have not yet been prepared.
13. All transactions have been recorded in the accounting records and are reflected in the financial statements.
14. We have disclosed to you the results of our assessment of risk that the financial statements may be materially misstated as a result of fraud.
15. We have no knowledge of allegations of fraud or suspected fraud, affecting the Town's financial statements involving:
  - a. Management.
  - b. Employees who have significant roles in the internal control.
  - c. Others where the fraud could have a material effect on the financial statements.
16. We have no knowledge of any allegations of fraud or suspected fraud affecting the Town's financial statements received in communications from employees, former employees, analysts, regulators, short sellers, or others.
17. We have no knowledge of noncompliance or suspected noncompliance with laws and regulations whose effects should be considered when preparing financial statements.

18. We are not aware of any pending or threatened litigation and claims whose effects should be considered when preparing the financial statements.
19. We have disclosed to you the identity of the Town's related parties and all the related-party relationships and transactions of which we are aware.
20. We have informed you of all significant deficiencies, including material weaknesses, in the design or operation of internal controls that could adversely affect the Town's ability to record, process, summarize, and report financial data.
21. There have been no communications from regulatory agencies concerning noncompliance with, or deficiencies in, financial reporting practices.

*Supplementary Information*

22. With respect to supplementary information presented in relation to the financial statements as a whole:
  - a. We acknowledge our responsibility for the presentation of such information.
  - b. We believe such information, including its form and content, is fairly presented in accordance with accounting principles generally accepted in the United States of America.
  - c. The methods of measurement or presentation have not changed from those used in the prior period.
  - d. There are no underlying significant assumptions or interpretations regarding the measurement or presentation of such information.
  - e. When supplementary information is not presented with the audited financial statements, we will make the audited financial statements readily available to the intended users of the supplementary information no later than the date of issuance of the supplementary information and the auditor's report thereon.
23. With respect to Management's Discussion and Analysis presented as required by Governmental Accounting Standards Board to supplement the basic financial statements:
  - a. We acknowledge our responsibility for the presentation of such required supplementary information.
  - b. We believe such required supplementary information is measured and presented in accordance with guidelines prescribed by accounting principles generally accepted in the United States of America.
  - c. The methods of measurement or presentation have not changed from those used in the prior period.
  - d. There are no underlying significant assumptions or interpretations regarding the measurement or presentation of such information.

*Compliance Considerations*

24. In connection with your audit, conducted in accordance with *Government Auditing Standards*, we confirm that management:
  - a. Is responsible for compliance with the laws, regulations, and provisions of contracts and grant agreements applicable to the Town.
  - b. Has no knowledge of any instances that have occurred, or are likely to have occurred, of fraud and noncompliance with provisions of laws and regulations that have a material effect on the



financial statements or other financial data significant to the audit objectives, and any other instances that warrant the attention of those charged with governance.

- c. Has no knowledge of any instances that have occurred, or are likely to have occurred, of noncompliance with provisions of contracts and grant agreements that have a material effect on the determination of financial statement amounts or other financial data significant to the audit objectives.
- d. Has no knowledge of any instances that have occurred or are likely to have occurred of abuse that could be quantitatively or qualitatively material to the financial statements or other financial data significant to the audit objectives.
- e. Has no knowledge of any fraud; noncompliance with provisions of laws, regulations, contracts, and grant agreements; or abuse to be reported by the auditor.
- f. Has a process to track the status of audit findings and recommendations.
- g. Has identified for the auditor previous audits, attestation engagements, and other studies related to the audit objectives and whether related recommendations have been implemented.
- h. Has provided views on the auditor's reported findings, conclusions, and recommendations, as well as management's planned corrective actions, for the report.
- i. Acknowledges its responsibilities as it relates to non-audit services performed by the auditor, including a statement that it assumes all management responsibilities; that it oversees the services by designating an individual, Laurie Smith, Town Treasurer, who possesses suitable skill, knowledge, or experience; that it evaluates the adequacy and results of the services performed; and that it accepts responsibility for the results of the services. Specifically:
  - i. Laurie Smith has supervised, reviewed, approved, and takes full responsibility for the basic financial statements and related notes and acknowledges the auditor's role in the preparation of this information.
  - ii. Laurie Smith has supervised, reviewed, approved and takes full responsibility for all audit adjustments attached as Appendix A and government wide conversion entries attached as Appendix B and acknowledges the auditor's role in the preparation of those adjustments.
  - iii. Laurie Smith has supervised, reviewed, approved and takes full responsibility for the City's Annual Uniform Financial Report and acknowledges the auditor's role in the preparation of this information.

25. In connection with your audit of federal awards conducted in accordance with OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, we confirm:

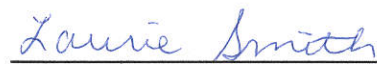
- a. Management is responsible for complying, and has complied, with the requirements of Circular A-133.
- b. Management is responsible for understanding and complying with the requirements of laws, regulations, and the provisions of contracts and grant agreements related to each of its federal programs.
- c. Management is responsible for establishing and maintaining, and has established and maintained, effective internal control over compliance for federal programs that provides reasonable assurance that the Town is managing federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements that could have a material effect on its federal programs.



- d. Management has prepared the schedule of expenditures of federal awards in accordance with Circular A-133 and has included expenditures made during the period being audited for all awards provided by federal agencies in the form of grants, federal cost-reimbursement contracts, loans, loan guarantees, property (including donated surplus property), cooperative agreements, interest subsidies, insurance, food commodities, direct appropriations, and other assistance.
- e. Management has identified and disclosed to the auditor 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 program.
- f. Management has made available all contracts and grant agreements (including amendments, if any) and any other correspondence relevant to federal programs and related activities that have taken place with federal agencies or pass-through entities.
- g. Management has no knowledge of any amounts questioned or any noncompliance with the direct and material compliance requirements of federal awards.
- h. Management believes that the Town has complied with the direct and material compliance requirements.
- i. Management has made available all documentation related to compliance with the direct and material compliance requirements, including information related to federal program financial reports and claims for advances and reimbursements.
- j. Management has no knowledge of any compliance requirements that are subject to varying interpretations.
- k. Management has no knowledge of any communications from grantors and pass-through entities concerning possible noncompliance with the direct and material compliance requirements, including communications received from the end of the period covered by the compliance audit to the date of the auditor's report.
- l. Management has no knowledge of any findings received and related corrective actions taken for previous audits, attestation engagements, and internal or external monitoring that directly relate to the objectives of the compliance audit, including findings received and corrective actions taken from the end of the period covered by the compliance audit to the date of the auditor's report.
- m. Management is responsible for taking corrective action on audit findings of the compliance audit.
- n. Management has no knowledge of any prior audit findings by federal awarding agencies or pass-through entities.
- o. Management has no knowledge of any subsequent events that provide additional evidence with respect to conditions that existed at the end of the reporting period that affect noncompliance during the reporting period.
- p. Management has no knowledge of any noncompliance with direct and material compliance requirements occurring subsequent to the period covered by the auditor's report or stating that there were no such known instances.
- q. Management has disclosed whether any changes in internal control over compliance or other factors that might significantly affect internal control, including any corrective action taken by management with regard to significant deficiencies and material weaknesses in internal control over compliance, have occurred subsequent to the date as of which compliance is audited.
- r. Federal program financial reports and claims for advances and reimbursements are supported by the books and records from which the basic financial statements have been prepared.

- s. The copies of federal program financial reports provided to the auditor are true copies of the reports submitted, or electronically transmitted, to the federal agency or pass-through entity, as applicable.
  - t. Management has charged costs to federal awards in accordance with applicable cost principles.
  - u. Management is responsible for, and has accurately prepared, the summary schedule of prior audit findings to include all findings required to be included by Circular A-133.
  - v. Management has accurately completed the appropriate sections of the data collection form.
26. During the course of your audit, you may have accumulated records containing data that should be reflected in our books and records. All such data have been so reflected. Accordingly, copies of such records in your possession are no longer needed by us.

**Town of Chesapeake Beach, Maryland**

  
\_\_\_\_\_  
Bruce A. Wahl, Mayor  
\_\_\_\_\_  
Laurie Smith, Town Treasurer  
\_\_\_\_\_  
Cheri Beard, Assistant Town Treasurer

## Appendix A

**Town of Chesapeake Beach, Maryland**  
**Summary of Adjusting Journal Entries**  
**June 30, 2014**

Description	Effect — Increase (Decrease)				
	Assets	Liabilities	Equity	Revenue	Expense
To adjust revenue to confirmed amounts					
General Fund	\$ 45,451	\$ -	\$ -	\$ 45,451	\$ -
To correct for differences between beginning fund balance per trial balance and prior year financial statements					
General Fund	-	-	3,498	-	3,498
To record property tax receivables and unavailable revenue as deferred inflow of resources					
General Fund	46,132	11,697	-	34,435	-
To adjust accrued interest					
Utility Fund	-	(5,783)	-	-	(5,783)
To correct interfund balances					
General Fund	216	-	-	753	537
Water Park Fund	-	(607)	-	-	(607)
Utility Fund	5,574	-	-	-	(5,574)
To correct year end payroll accrual					
General Fund	-	1,972	-	-	1,972
Water Park Fund	-	(68,674)	-	-	(68,674)
To record capitalized interest on ENR Project					
Utility fund	43,401	-	-	-	(43,401)
To remove duplicate ENR Grant revenue					
Utility fund	(118,293)	-	-	(118,293)	-
To remove bond issuance costs upon adoption of GASB 65					
Utility fund	(33,900)	-	(33,900)	-	-
<b>Total Effect</b>	-	-	80,378	<u>\$ (37,654)</u>	<u>\$ (118,032)</u>
<b>Total Balance Sheet Effect</b>	<u>\$ (11,419)</u>	<u>\$ (61,395)</u>	<u>\$ 49,976</u>		

**Town of Chesapeake Beach, Maryland**  
**Summary Of Fund Conversion Adjustments**  
**Year Ended June 30, 2014**

Description	Effect – Increase (Decrease)				
	Assets	Liabilities	Equity	Revenue	Expenses
<b><u>Government Wide Conversion</u></b>					
To record effects of governmental activities long term debt	-	2,629,936	(3,548,811)	-	(918,875)
To record effect of governmental activities capital assets	10,902,663	-	11,440,654	-	537,991
To record increase in accrued compensated absences and related payroll costs.	-	(3,453)	-	-	(3,453)
To record deferred revenue effect	-	(51,162)	86,022	(34,860)	-
To record current year effect in accrued interest payable	-	(6,262)	-	-	(6,262)
To remove bond issuance costs upon adoption of GASB 65	(44,567)	-	(44,567)	-	-
<b>Total Effect</b>	-	-	355,739	<b><u>\$ (34,860)</u></b>	<b><u>\$ (390,599)</u></b>
<b>Balance Sheet Effect</b>	<b><u>\$10,858,096</u></b>	<b><u>\$2,569,059</u></b>	<b><u>\$8,289,037</u></b>		