# Methodist Children's Home Society and Methodist Children's Home Society Supporting Organization

## Financial Statements

**December 31, 2018 (with Summarized Comparative Information for 2017)**

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# Independent Auditors' Report

To the Board of Directors
Methodist Children's Home Society and Methodist
Children's Home Society Supporting Organization
Redford, MI

We have audited the accompanying combined financial statements of Methodist Children's Home Society and Methodist Children's Home Society Supporting Organization, which comprise the combined statement of financial position as of December 31, 2018, and the related combined statements of activities, functional expenses, and cash flows for the year then ended, and the related notes to the financial statements.

**Management's Responsibility for the Financial Statements**

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes 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.

**Auditors' Responsibility**

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the combined financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

## Opinion

In our opinion, the combined financial statements referred to above present fairly, in all material respects, the financial position of Methodist Children's Home Society and Methodist Children's Home Society Supporting Organization as of December 31, 2018, and the changes in their net assets and their cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

## Adoption of New Accounting Standards

As described in Note 2 to the consolidated financial statements, Methodist Children's Home Society changed its method of accounting for net assets, investment expense, and functional expenses in 2018 as required by the provisions of FASB Accounting Standards Update 2016-14 *Presentation of Financial Statements of Not-for-Profit Entities*. Our opinion is not modified with respect to that matter.

## Report on Summarized Comparative Information

We previously audited Methodist Children's Home Society and Methodist Children's Home Society Supporting Organization's financial statements, and our report dated May 18, 2018 expressed an unmodified audit opinion on those financial statements. In our opinion, the summarized comparative information presented herein as of and for the year ended December 31, 2017, is consistent, in all material respects, with the audited financial statements from which it has been derived.

Yeo & Yeo, P.C.

Ann Arbor, Michigan
May 21, 2019

# Methodist Children's Home Society and Methodist Children's Home Society Supporting Organization

## Combined Statement of Financial Position

## December 31, 2018 (with Summarized Comparative Information for 2017)

| | Operating | Board-Designated Endowment Fund | **2018** | 2017 |
|---|---|---|---|---|
| **Assets** | | | | |
| Current assets | | | | |
| Cash | $ 3,293,393 | $ - | **$ 3,293,393** | $ 2,300,611 |
| Receivables | | | | |
| Accounts receivable, net | 1,007,110 | - | **1,007,110** | 1,007,232 |
| Promises to give | - | 69,963 | **69,963** | 61,298 |
| Prepaid expenses | 62,395 | - | **62,395** | 103,145 |
| Total current assets | 4,362,898 | 69,963 | **4,432,861** | 3,472,286 |
| Investments | - | 69,906,976 | **69,906,976** | 75,786,972 |
| Property and equipment, net | 7,148,601 | - | **7,148,601** | 7,410,051 |
| **Total assets** | $ 11,511,499 | $ 69,976,939 | **$ 81,488,438** | $ 86,669,309 |
| **Liabilities and Net Assets** | | | | |
| Current liabilities | | | | |
| Accounts payable | $ 37,166 | $ 16,121 | **$ 53,287** | $ 615,263 |
| Accrued payroll and withholdings | 457,996 | - | **457,996** | 424,484 |
| Total current liabilities | 495,162 | 16,121 | **511,283** | 1,039,747 |
| Accrued pension liability | 2,479,746 | - | **2,479,746** | 2,171,958 |
| Total liabilities | 2,974,908 | 16,121 | 2,991,029 | 3,211,705 |
| Net assets | | | | |
| Without donor restrictions | | | | |
| Undesignated | 1,332,805 | 69,960,818 | **71,293,623** | 76,047,553 |
| Undesignated - invested in property and equipment | 7,148,601 | - | **7,148,601** | 7,410,051 |
| Total without donor restrictions | 8,481,406 | 69,960,818 | **78,442,224** | 83,457,604 |
| With donor restrictions | | | | |
| Purpose restrictions | 55,185 | - | **55,185** | - |
| Total net assets | 8,536,591 | 69,960,818 | **78,497,409** | 83,457,604 |
| **Total liabilities and net assets** | $ 11,511,499 | $ 69,976,939 | **$ 81,488,438** | $ 86,669,309 |

See Accompanying Notes to the Financial Statements

## Methodist Children's Home Society and Methodist Children's Home Society Supporting Organization

### Combined Statement of Activities

### For the Year Ended December 31, 2018 (with Summarized Comparative Information for 2017)

| | Without Donor Restrictions | | | | |
|---|---|---|---|---|---|
| | Operating | Board-Designated Endowment Fund | With Donor Restrictions | **Total 2018** | Total 2017 |
| **Revenue, support and gains (losses)** | | | | | |
| Government grants and fees | $ 7,368,434 | $ - | $ - | **$ 7,368,434** | $ 6,821,093 |
| Contributions | 498,252 | 229,222 | 73,000 | **800,474** | 509,031 |
| Contributions by associated organizations | 115,897 | - | - | **115,897** | 77,334 |
| United Way | 22,987 | - | - | **22,987** | 23,485 |
| Investment income (loss) | - | (4,097,232) | - | **(4,097,232)** | 11,889,852 |
| Miscellaneous income | 1,155 | - | - | **1,155** | 20,657 |
| Gain (loss) on asset disposal | (16,781) | - | - | **(16,781)** | (29,656) |
| Net assets released from restrictions | 17,815 | - | (17,815) | **-** | - |
| Total revenue and support | 8,007,759 | (3,868,010) | 55,185 | **4,194,934** | 19,311,796 |
| **Expenses** | | | | | |
| Program services | | | | | |
| Residential | 5,384,542 | - | - | **5,384,542** | 5,243,955 |
| Adoptions | 144,773 | - | - | **144,773** | 337,439 |
| Foster family care | 1,049,486 | - | - | **1,049,486** | 724,549 |
| Social services | 5,820 | - | - | **5,820** | 96,803 |
| Support services | | | | | |
| Administrative | 1,737,651 | - | - | **1,737,651** | 1,726,600 |
| Fundraising | 493,421 | - | - | **493,421** | 359,071 |
| Total expenses | 8,815,693 | - | - | **8,815,693** | 8,488,417 |
| Transfers from endowment fund | 1,991,330 | (1,991,330) | - | **-** | - |
| Change in value of defined benefit plan | (339,436) | - | - | **(339,436)** | (84,453) |
| **Change in net assets** | 843,960 | (5,859,340) | 55,185 | **(4,960,195)** | 10,738,926 |
| Net assets - beginning of the year | 7,637,446 | 75,820,158 | - | **83,457,604** | 72,718,678 |
| Net assets - end of the year | $ 8,481,406 | $ 69,960,818 | $ 55,185 | **$ 78,497,409** | $ 83,457,604 |

See Accompanying Notes to the Financial Statements

# Methodist Children's Home Society and Methodist Children's Home Society Supporting Organization

## Combined Statement of Functional Expenses

### For the Year Ended December 31, 2018 (with Summarized Comparative Information for 2017)

| | Program Services | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Residential | Adoptions | Foster Family Care | Social Services | Total | Administrative | Fundraising | **Total 2018** | Total 2017 |
| Salaries and wages | $ 3,205,826 | $ 98,697 | $ 445,844 | $ - | $ 3,750,367 | $ 775,816 | $ 258,780 | **$ 4,784,963** | $ 4,869,656 |
| Employee benefits | 424,568 | 18,601 | 91,578 | - | 534,747 | 112,158 | 36,445 | **683,350** | 754,648 |
| Payroll taxes and insurances | 243,711 | 7,385 | 33,286 | - | 284,382 | 55,469 | 19,817 | **359,668** | 370,351 |
| Pension benefit | 204,181 | 7,092 | 32,091 | - | 243,364 | 55,991 | 18,997 | **318,352** | 257,522 |
| Total payroll expenses | 4,078,286 | 131,775 | 602,799 | - | 4,812,860 | 999,434 | 334,039 | **6,146,333** | 6,252,177 |
| Professional fees and services | 125,300 | 1,468 | 8,003 | 2,017 | 136,788 | 231,770 | 3,696 | **372,254** | 304,760 |
| Supplies | 318,188 | 1,090 | 11,860 | - | 331,138 | 63,118 | 37,382 | **431,638** | 376,837 |
| Telephone | 3,177 | - | 680 | 2,111 | 5,968 | 49,733 | 20 | **55,721** | 56,267 |
| Occupancy | 309,179 | 665 | 27,865 | 48 | 337,757 | 132,018 | 11,535 | **481,310** | 493,994 |
| Local transportation | 50,663 | 4,840 | 21,977 | - | 77,480 | 15,680 | 1,659 | **94,819** | 82,282 |
| Conferences and meetings | 10,108 | 16 | 2,501 | 1,644 | 14,269 | 48,485 | 11,699 | **74,453** | 44,289 |
| Specific assistance to individuals | 43,722 | - | 317,198 | - | 360,920 | - | - | **360,920** | 318,704 |
| Membership | 8,697 | - | 1,122 | - | 9,819 | 56,468 | 8,470 | **74,757** | 57,188 |
| Depreciation | 435,689 | 4,703 | 8,990 | - | 449,382 | 121,031 | - | **570,413** | 433,039 |
| Miscellaneous | 1,533 | 216 | 46,491 | - | 48,240 | 19,914 | 84,921 | **153,075** | 68,880 |
| Total expenses | $ 5,384,542 | $ 144,773 | $ 1,049,486 | $ 5,820 | $ 6,584,621 | $ 1,737,651 | $ 493,421 | **$ 8,815,693** | $ 8,488,417 |

See Accompanying Notes to the Financial Statements

## Methodist Children's Home Society and Methodist Children's Home Society Supporting Organization
### Combined Statement of Cash Flows
### For the Years Ended December 31, 2018 and 2017

| | Operating | Board-Designated Endowment Fund | 2018 | 2017 |
|---|---|---|---|---|
| **Cash flows from operating activities** | | | | |
| Change in net assets | $ 899,145 | $ (5,859,340) | **$ (4,960,195)** | $ 10,738,926 |
| Items not requiring cash | | | | |
| Depreciation | 570,413 | - | **570,413** | 433,039 |
| Pension plan periodic benefit cost | 318,352 | - | **318,352** | 257,522 |
| Pension related changes other than net periodic cost | 339,436 | - | **339,436** | 84,453 |
| Net realized and unrealized gain on investments | - | 4,987,068 | **4,987,068** | (11,029,634) |
| (Gain) loss on sale of property and equipment | 16,781 | - | **16,781** | 29,656 |
| Changes in operating assets and liabilities | | | | |
| Accounts receivable | 122 | - | **122** | 221,322 |
| Promises to give | - | (8,665) | **(8,665)** | 78,180 |
| Prepaid expenses | 40,750 | - | **40,750** | 13,642 |
| Accounts payable | (549,985) | (11,991) | **(561,976)** | 549,523 |
| Accrued payroll and withholdings | 33,512 | - | **33,512** | 87,721 |
| Pension contributions | (350,000) | - | **(350,000)** | (350,000) |
| Endowment fund transfers | (1,991,330) | 1,991,330 | **-** | - |
| Net cash provided (used) by operations | (672,804) | 1,098,402 | **425,598** | 1,114,350 |
| **Cash flows from investing activities** | | | | |
| Purchases of property and equipment | (325,744) | - | **(325,744)** | (2,850,526) |
| Purchases of securities | - | (41,133,714) | **(41,133,714)** | (3,117,338) |
| Sales of securities | - | 42,026,642 | **42,026,642** | 5,320,956 |
| Net cash provided (used) by investing activities | (325,744) | 892,928 | **567,184** | (646,908) |
| **Cash flows from financing activities** | | | | |
| Endowment fund transfers | 1,991,330 | (1,991,330) | **-** | - |
| Net change in cash and cash equivalents | 992,782 | - | **992,782** | 467,442 |
| Cash and cash equivalents, beginning of the year | 2,300,611 | - | **2,300,611** | 1,833,169 |
| **Cash and cash equivalents, end of the year** | $ 3,293,393 | $ - | **$ 3,293,393** | $ 2,300,611 |

See Accompanying Notes to the Financial Statements

## Note 1 – Summary of Significant Accounting Policies

### Nature of Activities

The accompanying combined financial statements reflect the combined financial position, activities, functional expenses and cash flows of Methodist Children's Home Society (the "Society") and Methodist Children's Home Society Supporting Organization (MCHS-SO) (collectively, the "Organizations"). Significant inter-organizational transactions have been eliminated.

The Society primarily provides shelter, residential care, treatment to emotionally impaired children, adoption services, and foster family care services. A significant portion of the Society's revenue is received from two sources: the Michigan Department of Human Services (MDHS) and public contributions. The current contracts with MDHS expire on September 30, 2020 and September 30, 2021. The MCHS-SO is a separate legal entity formed to manage certain investment activity and to provide financial support to the Society. The Organizations share common board members.

### Fund Accounting

The financial statements are prepared on the accrual basis of accounting. The Organizations have determined that the use of fund accounting to segregate assets, liabilities, net assets, income, and expenses although not required by accounting principles generally accepted in the United States of America, is a meaningful practice to continue. The financial activities of the Organizations are recorded in separate funds, described as follows:

<u>Current Operating Fund</u> - The Current Operating Fund is used to record the general operations of the Organizations. Revenue for general operations is derived primarily from per-diems and other fees for services, the rates for which are set by the State of Michigan, and the fees paid by the state and county government agencies. All accounts receivable are due from these sources. The Current Operating Fund also includes any designated amounts for specific purposes and the property and equipment of the Organizations.

<u>Board-designated Endowment Fund</u> - The Board-designated Endowment Fund includes assets designated by the Organizations for long-term investment. Investment earnings are transferred within the spending policy.

### Basis of Presentation

Net assets, revenues, gains, and losses are classified based on the existence or absence of donor or grantor imposed restrictions. Accordingly, net assets and changes therein are classified and reported as follows:

<u>Net assets without donor restrictions</u> – Net assets available for use in general operations and not subject to donor (or certain grantor) restrictions. The governing board has designated, from net assets without donor restrictions, net assets for a board-designated endowment.

<u>Net assets with donor restrictions</u> – Net assets subject to donor (or certain grantor) imposed restrictions. Some donor imposed restrictions are temporary in nature, such as those that will be met by the passage of time or other events specified by the donor. Other donor imposed restrictions are perpetual in nature, where the donor stipulates that resources be maintained in perpetuity.

The Organization reports contributions restricted by donors as increases in net assets without donor restrictions if the restrictions expire (that is, when a stipulated time restriction ends or purpose restriction is accomplished) in the reporting period in which the revenue is recognized. All other donor restricted contributions are reported as increases in net assets with donor restrictions, depending on the nature of the restrictions. When a restriction expires, net assets with donor restrictions are reclassified to net assets without donor restrictions and reported in the statements of activities as net assets released from restrictions.

**Comparative Financial Information**

The financial information for the year ended December 31, 2017 is presented for comparative purposes and is not intended to be a complete financial statement presentation.

**Cash**

The Organizations consider all highly liquid investments purchased with maturity of three months or less to be cash. The carrying amount of the Organizations deposits with financial institutions at year end was $3,293,393. The actual bank balance amounted to $3,323,311, and $250,000 was fully insured by the FDIC.

**Accounts Receivables**

The Organizations record program revenue for days of care. The Organizations use the allowance method for accounting for doubtful accounts. Management regularly reviews the collection history of its receivables balances with particular attention given to those amounts greater than 90 days old. Based on management's review, an allowance of $8,700 was deemed necessary as of December 31, 2018 and 2017.

It is the Organizations' policy to charge off uncollectible accounts receivable when management determines the receivable will not be collected.

**Investments**

Investments are stated at fair value based on quoted prices in active markets. Realized gains and losses on sales of investments represent the difference between the net sales price and the cost of securities sold. Unrealized gains and losses on investments represent the net change for the reported year in unrealized appreciation between the balance at the beginning and the end of the year. Donated investments are reflected as contributions at their fair values at date of receipt.

**Property and Equipment**

The Organizations follow the practice of capitalizing all expenditures in excess of $2,500 for property and equipment at cost; the fair value of donated fixed assets is similarly capitalized.

Furniture and equipment are stated at cost or fair market value at the date received. Major improvements are capitalized while ordinary maintenance and repairs are expensed.

Depreciation is computed using the straight-line method over the estimated useful lives of the related assets.

Gifts of land, buildings, equipment and other long-lived assets are also reported as revenue without donor restrictions and net assets, unless subject to time restrictions. Absent explicit donor stipulations for the time long-lived assets must be held, expirations of restrictions resulting in reclassification of net assets with donor restrictions as net assets without donor restrictions are reported when the long-lived assets are placed in service.

**Grants**
Grant revenue determined to be exchange transactions is recognized as services are provided. Grant revenue received in excess of that earned is recorded as deferred revenue.

**Contributions**
Contributions of cash and other assets, including unconditional promises to give in the future, are reported as revenue when received, measured at fair value.

Contributions without donor restrictions and contributions with donor restrictions of time or purpose that are met in the same period as the gift are both reported as support without donor restrictions. Other restricted gifts are reported as support with donor restrictions. Per the MCHS-SO bylaws, all legacies and bequests, not otherwise restricted are deposited into the board-designated endowment fund to be used exclusively for the benefits of the Society.

Contributions receivable are expected to be collected within one year. The Organizations have not recorded a provision for doubtful accounts since it is the opinion of management that those receivables are collectible in full.

**Prepaid Expenses**
Prepaid expenses are amounts paid for insurance and miscellaneous items in advance. The amounts are expected to be utilized within the next fiscal year.

**Compensated Absences**
Employees of the Organizations are entitled to paid vacation and paid sick days, depending on length of service.

**Retirement Plan**
The Society sponsors a defined benefit plan for all eligible employees. The Society contributed $350,000 to the pension plan in December 31, 2018 and 2017.

**Donated Services and Goods**
The Society records the value of donated goods as contributions using estimated fair values at the date of receipt. The Society recognized donated food of $84,810 and $42,942 as well as donated fixed assets of $122,439 and $0 for the years ended December 31, 2018 and 2017, respectively. Amounts are not recorded for items that are not used by the Society or benefit the residents of the society directly.

**Functional Expenses**
The costs of program and supporting services activities have been summarized on a functional basis in the statements of activities. The statements of functional expenses present the natural classification detail of expenses by function. Accordingly, certain costs have been allocated among the programs and supporting services benefited. Those expenses include pension expense, depreciation and amortization, and occupancy. Pension expenses are allocated based on the departmental percentages of actual employee effort, depreciation, amortization and occupancy are allocated based on a square footage basis.

**Income Tax Status**
The Organizations qualified as a tax-exempt organization under Section 501(c)(3) of the Internal Revenue Code, and are classified as organizations other than a private foundation, as described in Section 509(a). The Organizations file information returns in the U.S. Federal and Michigan jurisdiction.

**Risks and Uncertainties**

The Organizations invest in various investment securities. Investment securities are exposed to various risks such as interest rate, market, and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the amounts reported in the combined statement of financial position.

**Use of Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

**Collective Bargaining Agreement**

Approximately 32% of employees were covered by a collective bargaining agreement during December 31, 2018 and 2017. The agreement expired on December 31, 2021.

**Subsequent Events**

Management has evaluated subsequent events through May 21, 2019, which is the date the financial statements were available to be issued.

**Change in Accounting Principle**

On August 18, 2016, FASB issued ASU 2016-14, Not-for-Profit Entities (Topic 958) – *Presentation of Financial Statements of Not-for-Profit Entities*. The update addressed the complexity and understandability of net asset classification, deficiencies in information about liquidity and availability of resources, and the lack of consistency in the type of information provided about expenses and investment return. The Organization has adjusted the presentation of these statements accordingly.

## Note 2 – Investments

Investments consisted of the following at December 31:

| | 2018 | 2017 |
|---|---|---|
| Money market funds | $ 378,971 | $ 1,231,274 |
| Bonds | 1,769,337 | 5,098,646 |
| Equity securities | 67,758,668 | 69,457,052 |
| Total investments | $ 69,906,976 | $ 75,786,972 |

Investment expenses included in the statement of activities investment income was $376,850 and $337,280 or the years ended December 31, 2018 and 2017, respectively.

## Note 3 – Liquidity and Availability

Financial assets available for general expenditure, that is, without donor or other restrictions limiting their use, within one year of the statement of financial position date, comprise the following:

| | Total |
|---|---|
| Cash and cash equivalents | $ 3,293,393 |
| Accounts receivable | 1,007,110 |
| Promises to give | 69,963 |
| | $ 4,370,466 |

The Organization's goal is generally to maintain financial assets to meet 90 days of operating expenses (approximately $2.375 million). If cash reserves were to be deemed insufficient, the Organization has the ability to request a transfer of funds from the Supporting Organization which has custody of the endowment funds.

**Note 4 – Property and Equipment**

Property and equipment as of December 31 consist of the following:

| | 2018 | 2017 |
|---|---|---|
| Land | $ 82,045 | $ 82,045 |
| Land improvements | 2,510,490 | 2,510,490 |
| Building | 11,634,381 | 11,460,267 |
| Vehicles | 413,359 | 323,588 |
| Furniture and fixtures | 633,061 | 727,319 |
| Construction in progress | 20,625 | - |
| Total cost | 15,293,961 | 15,103,709 |
| Accumulated depreciation | (8,145,360) | (7,693,658) |
| Net property and equipment | $ 7,148,601 | $ 7,410,051 |

Depreciation expense was $570,413 and $433,039 for the years ended December 31, 2018 and 2017, respectively.

**Note 5 – Pension and Other Post Retirement Benefit Plans**

The Society sponsors a defined benefit plan that covers substantially all employees. The Plan provides defined benefits based on years of services and final average salary.

Details of the obligations and funded status for December 31 are as follows:

| | 2018 | 2017 |
|---|---|---|
| Projected benefits obligation | $ 11,960,554 | $ 13,072,537 |
| Fair value of plan assets | 9,480,808 | 10,900,579 |
| Funded status at end of year | $ (2,479,746) | $ (2,171,958) |

Amounts recognized in the combined statement of financial position consist of accrued pension liability of $2,479,746 and $2,171,958 at December 31, 2018 and 2017, respectively.

Amounts not yet recognized as components of net periodic benefit costs consist of the following:

| | 2018 | 2017 |
|---|---|---|
| Net loss | $ 3,394,337 | $ 3,341,341 |
| Unrecognized prior service costs | (82,388) | (100,738) |
| Total | $ 3,311,949 | $ 3,240,603 |

The accumulated benefit obligation for the defined benefit pension plan was $11,569,181 and $12,486,573 at December 31, 2018 and 2017, respectively.

The net periodic benefit cost, employer contributions, participant contributions and benefits paid in December 31 are as follows:

| | 2018 | 2017 |
|---|---|---|
| Net periodic benefit costs | $ 318,352 | $ 257,522 |
| Employer contributions | 350,000 | 437,500 |
| Benefits paid | 295,199 | 273,408 |
| SFAS No. 88 Settlement | 944,170 | 997,809 |

The weighted average assumptions used to determine benefit obligations at December 31 are as follows:

| | 2018 | 2017 |
|---|---|---|
| Discount rate | 3.50% | 3.50% |
| Rate of compensation increase | 3.50% | 3.00% |

The weighted average assumptions used to determine net periodic benefits cost for the years ended December 31 are as follows:

| | 2018 | 2017 |
|---|---|---|
| Discount rate | 3.50% | 4.00% |
| Expected long-term return on plan assets | 7.00% | 7.00% |
| Rate of compensation increase | 3.50% | 3.00% |

The expected rate of return assumption was selected as an estimate of anticipated future long-term rates of return on plan assets as measured on a market value basis. Factors considered in making this selection include (a) historical long term rates of return for broad asset classes, (b) actual past rates of return achieved by the plan, (c) the general mix of assets held by the plan, and (d) the stated investment policy for the plan. The selected rate of return is net of anticipated investment-related expenses.

The Society's pension plan weighted average asset allocations at December 31, 2018 and 2017 by category are as follows:

| | 2018 | 2017 |
|---|---|---|
| Equity securities | 67.08% | 66.73% |
| Fixed income | 32.92% | 33.26% |
| Cash | 0.00% | 0.00% |

The target allocation range of percentages for each major category of plan assets as prescribed in the Society's investment charter is as follows:

| | |
|---|---|
| Equity securities | 55-65 |
| Fixed income | 35-45 |
| Cash | 0-1 |

Investments in equities and fixed income securities are confined to a diversified portfolio of mutual funds. The cash equivalent securities are confined to securities with a minimum rating of AI/PI.

The fair values of the Society's pension plan assets by major asset classes are as follows:

| | Balance at December 31, 2018 | Fair Value Measurements using: Quoted Prices in Active Markets for Identical Assets (Level 1) |
|---|---|---|
| Cash and cash equivalents | $ 403 | $ 403 |
| Mutual funds: | | |
| International equities fund | 1,527,480 | 1,527,480 |
| Emerging markets | 389,741 | 389,741 |
| U.S. equity fund | 4,432,240 | 4,432,240 |
| Fixed income mutual funds | 3,115,874 | 3,115,874 |
| Total | $ 9,465,738 | $ 9,465,738 |

| | Balance at December 31, 2017 | Fair Value Measurements using: Quoted Prices in Active Markets for Identical Assets (Level 1) |
|---|---|---|
| Cash and cash equivalents | $ 299 | $ 299 |
| Mutual funds: | | |
| International equities fund | 1,158,234 | 1,158,234 |
| Emerging markets | 201,497 | 201,497 |
| U.S. equity fund | 5,917,736 | 5,917,736 |
| Fixed income mutual funds | 3,622,813 | 3,622,813 |
| Total | $ 10,900,579 | $ 10,900,579 |

The preceding tables represent information about the pension and postretirement benefit plan assets measured at fair value on a recurring basis at December 31, 2018 and 2017, and the valuation techniques used by the Organizations to determine those fair values.

In general, fair values determined by Level 1 inputs use quoted prices in active markets for identical assets or liabilities that the Organizations have the ability to access.

Fair values determined by Level 2 inputs use other inputs that are observable, either directly or indirectly. These Level 2 inputs include quoted prices for similar assets and liabilities in active markets, and other inputs such as interest rates and yield curves that are observable at commonly quoted intervals.

Level 3 inputs are unobservable inputs, including inputs that are available in situations where there is little, if any, market activity for the related asset or liability.

There are no level 2 or 3 pension and postretirement benefit plan assets.

In instances where inputs used to measure fair value fall into different levels in the above fair value hierarchy, fair value measurements in the entirety are categorized based on the lowest level input that is significant to the valuation. The Organizations' assessment of the significance of particular inputs to these fair value measurements requires judgment and considers factors specific to each asset or liability.

The society is required to contribute $0 to its pension plan in 2019 per actuarial valuations, but expects to contribute $350,000 to its pension plan in 2019.

The benefit payments, which reflect expected future service, as appropriate, are expected to be paid as follows:

| Year Ended December 31, | Pension Benefits |
|---|---|
| 2019 | $ 407,271 |
| 2020 | 560,878 |
| 2021 | 479,328 |
| 2022 | 511,145 |
| 2023 | 879,947 |
| 2024-2028 | 3,396,052 |

## Note 6 – Fair Value Measurements

The fair value valuation techniques are listed in footnote 5. The same valuation techniques apply to the investments in the board-designated endowment. There are no level 3 investments in the board-designated endowment.

The Organizations' policy is to recognize transfers in and out of Level 1, 2 and 3 fair value classifications as of the end of the reporting period. As of December 31, 2018 and 2017, there were no transfers in or out of Level 1, 2 and 3 fair value classifications.

As of January 1, 2015, the Organizations implemented new guidance that changes the required disclosures for investments at net asset value (NAV) per share (or its equivalent) as a practical expedient. Previously, investments measured at fair value using the NAV practical expedient were classified in the fair value hierarchy based on the redemption features associated with the investment. Under the new guidance, investments measured at fair value using net asset value per share (or its equivalent) as a practical expedient are no longer classified in the fair value hierarchy below.

Disclosures concerning assets measured at fair value on a recurring basis for the year ended December 31 are as follows:

| | | Fair Value Measurements using: | |
|---|---|---|---|
| | Balance at December 2018 | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) |
| Money market funds | $ 378,971 | $ 378,971 | $ - |
| Equity securities: | | | |
| Large-cap value | 12,632,437 | 12,632,437 | - |
| Large-cap growth | 10,022,633 | 10,022,633 | - |
| Large-cap core | 3,199,614 | 3,199,614 | - |
| Small/Mid cap | 7,412,423 | 7,412,423 | - |
| Emerging markets | 1,602,533 | 1,602,533 | - |
| Mutal funds | 9,910,562 | 9,910,562 | - |
| Total return bond fund | 8,313,575 | 8,313,575 | - |
| Debt: | | | |
| Debt securities issued by the U.S. Treasury and other U.S. government corporations and agencies | 157,000 | - | 157,000 |
| Debt securities issued by the United States of America and political subdivisions of the states | 1,098,746 | - | 1,098,746 |
| Corporate fixed income | 513,591 | - | 513,591 |
| Total | 55,242,085 | $ 53,472,748 | $ 1,769,337 |
| Investments valued at NAV | 14,664,891 | | |
| Total investments | $ 69,906,976 | | |

| | Balance at December 2017 | Fair Value Measurements using: Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) |
|---|---|---|---|
| Money market funds | $ 1,231,274 | $ 1,231,274 | $ - |
| Equity securities: | | | |
| Large-cap value | 13,031,663 | 13,031,663 | - |
| Large-cap growth | 11,853,198 | 11,853,198 | - |
| Large-cap core | 11,402,441 | 11,402,441 | - |
| Small/Mid cap | 9,776,624 | 9,776,624 | - |
| | 925,329 | 925,329 | - |
| Total return bond fund | 13,928,386 | 13,928,386 | - |
| Debt: | | | |
| Debt securities issued by the U.S. Treasury and other U.S. government corporations and agencies | 782,541 | - | 782,541 |
| Debt securities issued by the United States of America and political subdivisions of the states | 2,605,990 | - | 2,605,990 |
| Corporate fixed income | 1,644,064 | - | 1,644,064 |
| Municipal bonds | 66,051 | - | 66,051 |
| Total | 67,247,561 | $ 62,148,915 | $ 5,098,646 |
| Investments valued at NAV | 8,539,411 | | |
| Total investments | $ 75,786,972 | | |

The Organizations hold interest in investment companies where fair value of the investments are measured on a recurring basis using net asset value per share (or its equivalent) of the investment companies as a practical expedient. At year end, the fair value, unfunded commitments, and redemption rules of those investments is as follows:

| | December 31, 2018 Fair Value | December 31, 2017 Fair Value | December 31, 2016 Fair Value | Redemption Frequency, if Eligible | Redemption Notice Period |
|---|---|---|---|---|---|
| Earnest International Investment Trust Fund | $ 14,664,891 | $ 8,539,411 | $ 6,530,394 | Monthly, last business day of the month | 5 business days |

## Note 7 – Net Assets With Donor Restrictions

Net assets with donor restrictions are restricted for the following purposes and periods at December 31:

| | 2018 | 2017 |
|---|---|---|
| Subject to expenditure for specified purpose: | | |
| Sound system in gymnasium | $ 4,000 | $ - |
| Animal assisted therapy | 9,000 | - |
| Aftercare aide | 32,185 | - |
| Prevention specialist | 10,000 | - |
| Total net assets with donor restrictions | $ 55,185 | $ - |

**Note 8 – Net Assets Released from Restrictions**

Net assets were released from donor restrictions by incurring expenses satisfying the restricted purpose or by occurrence of the passage of time or other events specified by the donors as follows for the years ended December 31, 2018 and 2017:

| | 2018 | 2017 |
|---|---|---|
| Satisfaction of purpose restrictions | | |
| Aftercare aide | $ 17,815 | $ - |

**Note 9 – Endowment Funds**

The Organizations' endowment is made up of funds designated by the board of directors to function as endowments. The board-designated endowment fund net assets are without donor restriction.

The board-designated endowment fund columns on the combined statement of financial position and combined statement of activities reflect the activity of the fund for the year.

The endowment net asset composition by type of fund as of December 31, 2018 is as follows:

| | Without Donor Restriction | With Donor Restrictions | Total |
|---|---|---|---|
| Board-designated endowment funds | $ 69,960,818 | $ - | $ 69,960,818 |

Changes in endowment net assets for the year ended December 31, 2018 are as follows:

| | Without Donor Restriction | With Donor Restrictions | Total |
|---|---|---|---|
| Beginning of year | $ 75,820,158 | $ - | $ 75,820,158 |
| Contributions | 229,222 | - | 229,222 |
| Investment income | 1,266,686 | - | 1,266,686 |
| Net appreciation (realized and unrealized) | (4,987,068) | - | (4,987,068) |
| Investment fees | (376,850) | - | (376,850) |
| Appropriation of endowment assets for expenditure | (1,991,330) | - | (1,991,330) |
| End of year | $ 69,960,818 | $ - | $ 69,960,818 |

The endowment net asset composition by type of fund as of December 31, 2017 is as follows:

| | Without Donor Restriction | With Donor Restrictions | Total |
|---|---|---|---|
| Board-designated endowment funds | $ 75,820,158 | $ - | $ 75,820,158 |

The changes in endowment net assets for the year ended December 31, 2017 are as follows:

| | Without Donor Restriction | With Donor Restrictions | Total |
|---|---|---|---|
| Beginning of year | $ 67,074,383 | $ - | $ 67,074,383 |
| Investment income | 1,197,498 | - | 1,197,498 |
| Net depreciation (realized and unrealized) | 11,029,634 | - | 11,029,634 |
| Investment fees | (337,280) | - | (337,280) |
| Appropriation of endowment assets for expenditure | (3,144,077) | - | (3,144,077) |
| End of year | $ 75,820,158 | $ - | $ 75,820,158 |

**Return Objectives and Risk Parameters**
The Organization has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Under this policy, as approved by the board of trustees, the endowment assets are invested in a manner that is intended to produce results that exceed the price and yield results of market while assuming a moderate level of investment risk. The Organizations expect the endowment funds to provide an average rate of return of approximately 8 percent annually. Actual returns in any given year may vary from this amount.

**Strategies Employed for Achieving Objectives**
To satisfy their long-term rate-of-return objectives, the Organizations rely on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Organizations target a diversified asset allocation that places a greater emphasis on equity-based investments to achieve long-term return objectives within prudent risk constraints.

**Spending Policy and How the Investment Objectives Relate to Spending Policy**
The Organizations adopted a policy in 2009 limiting the annual distribution from the board-designated endowment fund to 4.5 percent of the fund's average fair value over the prior five years through the calendar year end, preceding the fiscal year in which the distribution is planned, using start-of-year balances. In establishing this policy, the Organizations considered the long-tern expected return on the endowment. This is consistent with the Organizations' objective to maintain the purchasing power of the endowment assets held in perpetuity or for a specified term as well as to provide additional real growth through new gifts and investment returns.

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May 21, 2019

Management and the Board of Directors
Methodist Children's Home Society and Methodist
Children's Home Society Supporting Organization
26645 West Six Mile Road
Redford, MI

We have completed our audit of the financial statements of Methodist Children's Home Society and Methodist Children's Home Society Supporting Organization (the "Organization") as of and for the year ended December 31, 2018, and have issued our report dated May 21, 2019. We are required to communicate certain matters to you in accordance with auditing standards generally accepted in the United States of America that are related to internal control and the audit. The appendices to this letter set forth those communications as follows:

I Auditors' Communication of Significant Matters with Those Charged with Governance

In addition, we have identified additional matters that are not required to be communicated but we believe are valuable for management:

II Matters for Management's Consideration

We discussed these matters with various personnel in the Organization during the audit and we would also be pleased to meet with you to discuss these matters at your convenience.

These communications are intended solely for the information and use of management, the Board of Directors, and others within the Organization, and are not intended to be and should not be used by anyone other than those specified parties.

Yeo & Yeo, P.C.

Ann Arbor, Michigan

Appendix I

Auditors' Communication of Significant Matters with Those Charged with Governance

Professional standards require that we provide you with information about our responsibilities under auditing standards generally accepted in the United States of America, as well as certain information related to the planned scope and timing of our audit. We have communicated such information in our engagement letter dated March 5, 2019. Professional standards also require that we communicate to you the following information related to our audit.

<u>Significant Audit Findings</u>

*Qualitative Aspects of Accounting Practices*

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by the Organization are described in Note 1 of the financial statements. The Organization have adopted FASB ASU 2016-14, Not-for-Profit Entities (Topic 958) – *Presentation of Financial Statements of Not-for-Profit Entities*. ASU 2016-14 is effective for years ending December 15, 2018 and later. The update addressed the complexity and understandability of net asset classification, deficiencies in information about liquidity and availability of resources, and the lack of consistency in the type of information provided about expenses and investment return. We noted no transactions entered into by the Organization during the year where there is lack of authoritative guidance or consensus. All significant transactions have been recognized in the proper period.

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 Organization's financial statements were:

- Management's estimate of the functional allocation of expenses is based on the Organization's cost allocation methodology using allocation bases including actual salaries for pension related expenses and square footage for occupancy costs.
- Management's estimate of the useful lives of depreciable capital assets is based on the length of time it is believed that those assets will provide some economic benefit in the future.
- The net pension liability estimate which is based on a third party actuary report.

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

Disclosures in the financial statements are neutral, consistent and clear.

*Accounting Standards and Regulatory Updates*

- *Tax Reform*
  Everyone is well aware that tax reform has become law. There are two sets of potential direct effects on nonprofits that could have significant taxable impacts, even to entities that previously had no taxable income.

  The first major direct effect is taxable nondeductible expenses. The impact of this started on January 1, 2018, *regardless* of fiscal year end date. In order to put nonprofits and for-profits on a level playing field, the following expenses are not only nondeductible when incurred in an unrelated trade or business, but nondeductible (i.e. taxable expenditures) when incurred in a related or excluded trade or business. These expenses include qualified transportation fringe benefits, parking facilities used in connection with qualified parking, and on-premises athletic facilities. The law *still* states that these amounts are *excluded* from *employees'* wages; if the expense meets the definition, there appears to be no leeway to push the expense to the employee. However, when the expense is excluded from employees' wages, it triggers the nondeductibility aspect. For-profits and unrelated trades or businesses see this as a nondeductible expense, thus increasing taxable income. Related trades or businesses or excluded income have no taxable income to begin with, so to get the same impact, these expenses get *added* as taxable income.

The biggest issue tends to be the qualified parking (one of the qualified transportation fringe benefits.) In general, if your organization owns or rents parking spaces for your employees you have to consider if there is taxable income. If there are employee reserved spots, there is taxable income. If 50% or more of the parking lot spots are typically used by employees, there is taxable income. The entire 990-T form gets a $1,000 standard deduction. So if the total of taxable expenditures plus gross unrelated business income is $1,000 or less, there is no tax impact. If it is greater than $1,000, there is likely a tax impact. These qualified transportation expenses, parking facilities used in connection with qualified parking, and on-premises athletic facilities expenses could be the only items on Form 990-T and could cause you to have a Form 990-T when you have never had one in the past.

The second direct effect is on traditional unrelated business income. Starting with the 2018 return, each activity will have to be tracked separately. One activity's losses cannot offset another activity's income. Net operating loss carryforwards will only be applicable to the activity that generated the net operating loss carryforward. In addition, the other nondeductible expense rules which apply to corporations, such as entertainment being nondeductible, will also apply to unrelated business income.

We are working through the tax law and trying to determine how it will impact the nonprofit industry and our clients in particular. However, the IRS is still in the process of issuing regulations on all the different tax law changes. The IRS regulations, once issued, may confirm or change interpretations of the law. We suggest paying close attention to developments with respect to these matters, considering the impact they could have to your organization, and, generally, planning for more taxable income than you've had in the past.

- *Impact of Decision in South Dakota v. Wayfair*

  In June of 2018, the Supreme Court overturned the 1992 case of *Quill Corp. v. North Dakota*, as part of their decision in deciding *South Dakota v. Wayfair*. This potentially affects any organization making sales of goods or services. Formerly, you needed to be physically present in a state to have a responsibility to collect sales tax on purchases or services provided in that state; that is no longer always the case. Further, goods and services in that are not taxable in Michigan, may be taxable in another state. Exemption rules and reporting requirements also vary by state. If you are party to transactions with out of state purchasers, you may be required to collect and remit sales tax for another state. Also, if you make purchases from out of state vendors, you may be required to remit use tax to the state of Michigan. We recommend that your sales and use tax exposure be evaluated regularly to limit exposure of non-compliance.

- *Contributions Received and Contributions Made*

  Standards delineating between exchange revenue and contribution revenue, as well as those delineating between unconditional and conditional contributions, have been updated and are applicable for the fiscal year ending December 31, 2019. In general, if the resource provider does not receive commensurate value in return for the resources transferred, the revenue is contribution revenue. However, this standard goes on to explain that if the value is received by the general public, and not the resource provider, it is a contribution. In addition, conditional contributions are those contributions which have a barrier that must be overcome before the recipient is entitled to the assets and there is a right of return or right of release on those assets by the resource provider. This standard will cause many Federal grants to be considered conditional contributions, rather than exchange transactions. This will increase disclosures, but may not significantly impact the timing of revenues. Contributions made (expense transactions), will also be similarly accounted.

- *Revenue Recognition*
  There is a new revenue recognition (exchange transactions not contributions) standard that will be applicable for the fiscal year ending December 31, 2019. However, if comparative financial statements are presented, all years shown will need to follow the same guidance. Therefore, for comparative financial statements, this new standard may need to be run side by side with the existing standard for the year ending December 31, 2018. The new standard has a five step process for recognizing revenue. 1) Identify the contract with the customer. 2) Identify the performance obligations within the contract. 3) Determine the transaction price. 4) Allocate the transaction price to the performance obligation. 5) Recognize revenue when the performance obligation is met. This standard aligns all revenue recognition to similar concepts, rather than industry specific standards. In addition, it discusses some concepts, such as material rights and performance obligations for "free" goods and services that may not have been covered in previous standards. Look for additional guidance to be released in the future as the Financial Accounting Standards Board (FASB) wrestles with implementation of many nuances of this standard.

- *Cybersecurity Posture*
  Cybersecurity posture, an overall measure of cybersecurity strength, is more prevalent than ever as organization continue to face cybersecurity risks. Billions of emails are sent every day, some of which contain attachments with malicious files or malicious embedded links aimed at negatively impacting unsuspecting organization. A recent study showed as many as four out of five US Companies have suffered from an attack. Not only can a successful attack cost thousands of dollars and put a strain on IT resources while remediation efforts are underway, but sensitive information may be breached.

  Risk assessment is a first step in mitigating cybersecurity risks and improving your organization's overall cybersecurity posture. The National Institute of Standards and Technology published Framework for Improving Critical Infrastructure Cybersecurity, which "enables organization, regardless of size, degree of cybersecurity risk, or cybersecurity sophistication, to apply the principles and best practices of risk management to improving the security and resilience of critical infrastructure." The framework is designed to cover five areas including identification, protection, detection, responsiveness and recovery. The publication can be found at www.nist.gov.

  Placing significant emphasis on evaluating your organization's cybersecurity posture, and channeling sufficient resources towards proper risk assessment, implementation, and education will reduce the likelihood of a cybersecurity threat, and help lessen the impact of a breach.

- *Leases*
  There is a new Accounting Standards Update which will significantly change accounting for leases by both lessors and lessees. The new guidance, requires the right of use model in accounting for all leases, with limited exceptions. As a result, lessees will be required to recognize assets and liabilities arising from operating leases. Lessees will recognize interest expense on the liability and amortization of the right-to-use asset in their results of operations. Capital lease accounting will also change due to changes in guidance related to options and contingent rentals. Rules may be simplified for leases with terms of twelve months or less but will be applied to all existing leases upon adoption. The guidance could have implications, not only for the Organization's financial statements, but also for any applicable debt covenants. The standard that will be applicable for the fiscal year ending December 31, 2020. However, if comparative financial statements are presented, all years shown will need to follow the same guidance. Therefore, for comparative financial statements, this new standard may need to be run side by side with the existing standard for the year ending December 31, 2019.

*Difficulties Encountered in Performing the Audit*

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

*Corrected and Uncorrected Misstatements*

Professional standards require that the auditor accumulate all known and likely misstatements identified during the audit, other than those the auditor believes to be trivial. The adjustments identified during the audit have been communicated to management and management has posted all adjustments.

There were no uncorrected misstatements that were more than trivial.

*Disagreements with Management*

For purposes of this letter, professional standards define a disagreement with management as a financial accounting, reporting or auditing matter, whether or not resolved to our satisfaction that could be significant to the financial statements or the auditors' report. We had no disagreements with management during the audit.

*Management Representations*

We have requested certain representations from management that are included in the management representation letter dated as of the date of the audit report.

*Management's Consultations with Other Accountants*

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the Organization's financial statements or a determination of the type of auditor's 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.

*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 Organization's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

*Emphasis of Matters in Independent Auditors' Report*

Our report will include the following emphasis of matter:

**Adoption of New Accounting Standard**

As described in Note 1 to the financial statements, Methodist Children's Home Society and Methodist Children's Home Society Supporting Organization changed its method of accounting for net assets, investment expense, and functional expenses in 2018 as required by the provisions of FASB Accounting Standards Update 2016-14 *Presentation of Financial Statements of Not-for-Profit Entities*. Our opinion is not modified with respect to this matter.

Appendix II

Communication of Internal Control Matters Identified During the Audit

In planning and performing our audit of the financial statements of the Organization as of and for the year ended December 31, 2018, in accordance with auditing standards generally accepted in the United States of America, we considered the Organization's internal control over financial reporting as a basis for designing our audit procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Organization's internal control. Accordingly, we do not express an opinion on the effectiveness of the Organization's internal control.

However, during out audit we became aware of a matter for management's consideration that is an opportunity for strengthening internal controls. This letter does not affect our report dated May 21, 2019, on the financial statements of the Organization. Our comment and recommendation regarding that matter is:

**Segregation of Duties**

We are sensitive to the fact that the entity is a smaller organization and segregation of duties may be difficult to obtain in all scenarios. In our walkthrough of internal controls related to payroll, we noted that the payroll accountant posts the payroll without any prior review. The same employee also has administrator rights in the Paychex timesheet system.

Even within very small organization there is the ability to gain some amount of segregation of duties. We recommend that someone independent of the payroll accountant review the payroll prior to posting in order to detect and correct errors before processing, and that the payroll accountant is no longer assigned administrator rights in the timesheet system. These procedures will help prevent human errors as well as being a deterrent to fraud. If you would like further information on how to segregate duties as they specifically relate to the organization's situation, we would be happy to provide you with additional information and consultation.