



KALAMAZOO COMMUNITY
Mental Health
& Substance Abuse
Services

Year Ended
September 30,
2016

Financial
Statements and
Single Audit Act
Compliance

KALAMAZOO COMMUNITY MENTAL HEALTH AND SUBSTANCE ABUSE SERVICES

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INDEPENDENT AUDITORS' REPORT

March 21, 2017

Board of Directors
Kalamazoo Community Mental Health and
Substance Abuse Services
Kalamazoo, Michigan

Report on the Financial Statements

We have audited the accompanying financial statements of *Kalamazoo Community Mental Health and Substance Abuse Services* (the "Authority"), a component unit of Kalamazoo County, Michigan, as of and for the year ended September 30, 2016, and the related notes to the financial statements, which collectively comprise the Authority's basic financial statements as listed in the table of contents.

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.

Independent 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 and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from 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 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 financial statements referred to above present fairly, in all material respects, the financial position of Kalamazoo Community Mental Health and Substance Abuse Services as of September 30, 2016, and the respective changes in financial position and cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and the schedules for the pension and other postemployment benefits plans, as listed in the table of contents, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated March 21, 2017 on our consideration of the Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Authority's internal control over financial reporting and compliance.

A handwritten signature in black ink that reads "Lehmann Lohman LLC". The signature is written in a cursive, flowing style.

MANAGEMENT'S DISCUSSION AND ANALYSIS

KALAMAZOO COMMUNITY MENTAL HEALTH AND SUBSTANCE ABUSE SERVICES

Management's Discussion and Analysis

This section of Kalamazoo Community Mental Health and Substance Abuse Services' (the "Authority") annual financial report presents management's discussion and analysis (MD&A) of activities and financial performance during the fiscal year ended September 30, 2016. Please review it in conjunction with the independent auditors' report, the financial statements, the notes to the financial statements, and the supplementary information presented in this financial report.

Kalamazoo Community Mental Health and Substance Abuse Services is an Authority established by the State of Michigan and Kalamazoo County, Michigan, to operate, control, and manage an integrated behavioral healthcare and substance abuse system in order to better serve its residents. The mission of the Authority is to promote and provide mental health, intellectual-developmental disability, and substance abuse resources that empower people to succeed. The vision of the Authority is to provide a welcoming and diverse community partnership which collaborates and shares effective resources that support individuals and families to be successful through all phases of life.

The County of Kalamazoo Board of Commission appoints the board members governing the Authority. The County also provides annual financial support to the Authority, and the Authority is considered a component unit for reporting purposes in the audit report of Kalamazoo County, Michigan.

As of January 1, 2014 the Authority transferred its PIHP and substance abuse coordinating agency responsibilities to a newly established regional oversight agency known as Southwest Michigan Behavioral Health ("SWMBH"). Fiscal year 2015 was the first full year in which the Authority is operating in this manner.

The information contained in this MD&A should be considered in conjunction with the information contained in the financial statements audited by Rehmann Robson for the year ended September 30, 2016. This MD&A contains information on the basic financial statements of the Authority together with any required explanation which would be essential to acquire a full understanding of the data contained therein.

Financial Position Summary

Analysis of assets, deferred outflows of resources, liabilities, deferred inflows of resources, and net position over time serves as a useful indicator of the Authority's financial position. The Authority's assets and deferred outflows of resources exceeded liabilities and deferred inflows of resources by \$22,650,548 for the period ended September 30, 2016. This represents a decrease of \$1,987,373 from the prior period ended September 30, 2015, when the Authority's assets and deferred outflows of resources exceed liabilities by \$24,637,921.

KALAMAZOO COMMUNITY MENTAL HEALTH AND SUBSTANCE ABUSE SERVICES

Management's Discussion and Analysis

A condensed summary of the Authority's statement of net position is shown below:

	Net Position			
	2016	2015	Change	% Change
Assets				
Current and other assets	\$19,510,014	\$35,847,481	\$(16,337,467)	-45.6%
Capital assets, net	10,564,488	7,368,159	3,196,329	43.4%
Total assets	<u>30,074,502</u>	<u>43,215,640</u>	<u>(13,141,138)</u>	-30.4%
Deferred outflows of resources	<u>9,431,097</u>	<u>703,811</u>	<u>8,727,286</u>	1240.0%
Liabilities				
Long-term liabilities	6,574,472	6,595,027	(20,555)	-0.3%
Other liabilities	9,862,165	12,686,503	(2,824,338)	-22.3%
Total liabilities	<u>16,436,637</u>	<u>19,281,530</u>	<u>(2,844,893)</u>	-14.8%
Deferred inflows of resources	<u>418,414</u>	<u>-</u>	<u>418,414</u>	100.0%
Net position				
Net investment in capital assets	5,003,931	2,309,232	2,694,699	116.7%
Restricted	13,646,946	15,494,987	(1,848,041)	-11.9%
Unrestricted	3,999,671	6,833,702	(2,834,031)	-41.5%
Total net position	<u>\$22,650,548</u>	<u>\$24,637,921</u>	<u>\$ (1,987,373)</u>	-8.1%

The amount of the Authority's net investment in capital assets at September 30, 2016 is \$5,003,931 or 22.1% of total net position. Unrestricted net position of \$3,999,671 represents 17.7% of total net position. The remaining net position of \$13,646,946, or 60.2% represents amounts held in trust for payment of pension benefits in excess of the actuarial accrued liability for providing such benefits. The increase in capital assets is due to the completion of the E. Crosstown Office. This resulted in a corresponding decrease in current and other assets as the related bond proceeds were expended. The increase in deferred outflows and increase in current and other assets is related to the defined benefit pension plan through Kalamazoo County. The Authority's proportion of the plan was changed for the plan year ended December 31, 2015. This change resulted in a decrease in the net pension asset of approximately \$10 million. Under GASB 68, this change is deferred and amortized over a number of years, creating an increase in deferred outflows of resources. The decrease in other liabilities is the result of a lower payable to the PIHP for the current year MDHHS contract settlement, coupled with the elimination of the State portion of the inpatient rate (included in prior year liabilities for amounts not paid as of year-end).

KALAMAZOO COMMUNITY MENTAL HEALTH AND SUBSTANCE ABUSE SERVICES

Management's Discussion and Analysis

The following summarizes the revenues, expenses, and change in net position for the years ended September 30, 2016 and 2015:

	Change in Net Position			
	2016	2015	Change	% Change
Operating revenues				
Medicaid	\$64,167,529	\$61,011,155	\$ 3,156,374	5.2%
General fund and other:				
Federal and state grants	6,831,105	7,965,965	(1,134,860)	-14.2%
Charges for services	2,088,669	1,859,034	229,635	12.4%
Other	226,320	406,157	(179,837)	-44.3%
PA2 funds	136,400	151,109	(14,709)	-9.7%
Total operating revenues	73,450,023	71,393,420	2,056,603	2.9%
Operating expenses				
Mental illness adult population	25,264,003	25,490,706	(226,703)	-0.9%
Intellectual and developmental disabilities population	28,112,327	26,845,610	1,266,717	4.7%
Youth services	10,368,341	9,519,129	849,212	8.9%
Multipopulation	3,303,048	3,054,069	248,979	8.2%
Management and general	10,025,933	7,827,867	2,198,066	28.1%
Total expenses	77,073,652	72,737,381	4,336,271	6.0%
Operating loss	(3,623,629)	(1,343,961)	(2,279,668)	-3.1%
Nonoperating revenues (expenses)				
County appropriation	1,550,400	1,550,400	-	0.0%
Capital contributions	256,166	-	256,166	100.0%
Loss on sale of capital assets	(29,735)	(8,117)	(21,618)	266.3%
Interest revenue	10,844	21,801	(10,957)	-50.3%
Interest expense	(151,419)	(215,583)	64,164	-29.8%
Total nonoperating revenues (expenses)	1,636,256	1,348,501	287,755	21.3%
Change in net position	(1,987,373)	4,540	(1,991,913)	18.3%
Net position, beginning of year	24,637,921	24,633,381	4,540	0.0%
Net position, end of year	\$22,650,548	\$24,637,921	\$ (1,987,373)	-8.1%

KALAMAZOO COMMUNITY MENTAL HEALTH AND SUBSTANCE ABUSE SERVICES

Management's Discussion and Analysis

Financial Operations Highlights

- Medicaid revenue increased by approximately \$3 million because the contract between SWMBH and KCMHSAS is a cost settled contract. The increase is related to an increase in costs for residential and community inpatient services.
- Federal and state grants decreased primarily due to the elimination of the State portion of the inpatient rate. This created a corresponding decrease in expenses of approximately \$1.9 million. This was offset, in part, by use of prior year general fund savings of approximately \$250,000.
- The increase in management and general expenses relates to the year-end adjustment of the net pension asset and related deferred amounts which approximated \$1.85 million in the current year.
- The Authority's contract reconciliation with the State of Michigan for 2016 identified \$4,109 of State General Fund savings available for fiscal year 2016. The Authority's contract reconciliation with the State of Michigan for 2015 identified \$267,558 of State General Fund savings available for fiscal year 2015.
- The change in net position for the year was a decrease of \$1,987,373. This was primarily the result of the year-end adjustment to the net pension asset and related deferred amounts required under GASB 68 of approximately \$1.85 million. While a necessary adjustment for GAAP-basis financial reporting, this expense is not cost-settled as it does not require the use of current resources.

Capital Assets and Long-term Debt

Capital Assets. As of September 30, 2016, the Authority had \$10.6 million invested in a variety of capital assets as reflected in the following schedule:

	Capital Assets	
	2016	2015
Not being depreciated:		
Land	\$ 751,097	\$ 690,911
Work in progress	37,870	4,311,290
Being depreciated:		
Buildings and improvements	11,455,505	4,455,150
Equipment and furnishings	2,385,353	1,717,400
Vehicles	27,000	27,000
Accumulated depreciation	<u>(4,092,337)</u>	<u>(3,833,592)</u>
Total capital assets, net	<u>\$10,564,488</u>	<u>\$ 7,368,159</u>

The most significant capital asset activity in the current year was the completion of the E. Crosstown Building at a total cost of nearly \$7 million. Over \$4 million of this cost was incurred in years prior to 2016 and carried as "Work in Progress". For more information about the Authority's capital assets, see note 3.

KALAMAZOO COMMUNITY MENTAL HEALTH AND SUBSTANCE ABUSE SERVICES

Management's Discussion and Analysis

Long-term Debt. At the end of the current fiscal year, the Authority had total debt outstanding of \$6,574,472. The decrease is the result of making debt payments in accordance with amortization schedules.

	Long-term Debt	
	2016	2015
Contracts payable	\$ 5,000,000	\$ 5,000,000
Note payable	405,000	500,000
Premium on contracts payable	155,557	155,557
Compensated absences	1,013,915	939,470
Total long-term debt	\$ 6,574,472	\$ 6,595,027

For more information about the Authority’s long-term debt, see note 4.

Factors Impacting the Future

In late 2015, the Michigan Department of Health and Human Services sought approval from the Centers for Medicare and Medicaid Services (CMS) for a 1115 Demonstration Waiver to combine under a single waiver authority all services and eligible populations served through its 1915(b) and its multiple 1915(c) waivers for persons with Serious Mental Illness (SMI), Substance use Disorders (SUD), Intellectual and Developmental Disabilities (IDD) and Children with Serious Emotional Disturbances (SED). Michigan was seeking more flexibility to develop quality, financing and integrated care (physical and behavioral health) initiatives for all Specialty Service Populations on a State wide basis. Currently, the State is awaiting approval from CMS.

The Section 298 Initiative is a statewide effort to improve the coordination of physical health services and behavioral health services and supports. The Michigan Department of Health and Human Services (MDHHS) launched this initiative in response to legislative language in the Fiscal Year 2017 approved budget. The language, known as Section 298, calls upon MDHHS to form a workgroup “to make recommendations regarding the most effective financing model and policies for behavioral health services and supports in order to improve the coordination of behavioral health and physical health for individuals with mental illness, intellectual and developmental disabilities, and substance use disorders”. Under Section 298, MDHHS and a workgroup of stakeholders are required to produce a report with recommendations for the Michigan Legislature. Last summer, MDHHS convened the 298 facilitation workgroup to gather feedback from the public and develop recommendations for the report. The interim report was submitted on January 13, 2017 and focused on recommendations for potential policy changes. The final report, due March 15, 2017, will incorporate policy recommendations from the interim report as well as additional recommendations on models, pilots, and benchmarks for implementation.

KALAMAZOO COMMUNITY MENTAL HEALTH AND SUBSTANCE ABUSE SERVICES

Management's Discussion and Analysis

In April 2014, Medicaid expansion, called Healthy Michigan, was implemented. This expansion was a result of the complete implementation of the Affordable Care Act (ACA). Most of the people who previously received service under the State CMHSP General Fund Appropriations fell within the new income eligibility levels for the program. This resulted in an expansion of eligible enrollees to the Medicaid Managed Specialty Services Program. Over six a six month period, from April, 2014 to October 1, 2014, the State's support for mental health services to persons without Medicaid coverage, in the form of State General Fund dollars to Michigan's Community Mental Health system, was reduced by 60%. This reduction of \$200 million, which coincided with the expansion of Medicaid in Michigan under the Healthy Michigan Plan, was to reflect the reduced level of demand for State general fund dollars needed to cover the cost of mental health services to persons who would be covered as of April 2014 by the Healthy Michigan Plan. However, the size of this reduction was too great and was not offset by Healthy Michigan revenues. This funding reduction created a significant hole in the State's community mental health safety net. In addition to this reduction in State General Funds, the new Trump administration has vowed to repeal and replace the ACA which could have a huge impact on KCMHSAS future funding. To accomplish this, the Congressional Republicans' American Health Care Act currently proposes major changes in Medicaid which include the following:

- Maintains the Affordable Care Act's (ACA's) higher financing for Healthy Michigan (Medicaid expansion) through the end of 2019. After that, states can only continue to receive enhanced Federal Medical Assistance Percentage (FMAP) payments for beneficiaries already covered (and continuously covered) by the Healthy Michigan Plan. Newly enrolled beneficiaries and those who rotate on and off the program (which represents almost one half of the current 650,000 people currently enrolled), the federal government would provide a lower level of financing at the standard FMAP for Michigan.
- Overhauls the broader Medicaid program to end its open-ended federal financing. Instead, each state would receive a limited per capita cap amount based on its enrollment and costs. That federal payment would be increased according to a government measure of medical inflation.

It is uncertain whether Michigan will be able to afford to maintain Healthy Michigan after the end of 2019 and restore the \$200 million in State General Funds that were removed prior to the program's implementation. These developments are good examples of why the KCMHSAS Authority needs to adapt quickly to changes in Medicaid funding, forge new opportunities, partnerships, and be willing to accept new roles and responsibilities. At the same time, the Authority needs to continue to press forward in using improved technologies and evidence based practices, become a data driven organization, and utilize the best talent under contract and in employment.

Request for Information

This financial report is designed to provide a general overview of the Authority's finances for all those with an interest in the Kalamazoo Community Mental Health and Substance Abuse Services. Questions concerning any of the information provided in this report or request for additional information may be addressed to the Finance Director at 3299 Gull Road Dr., PO Box 63, Nazareth, MI 49074-0063.

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BASIC FINANCIAL STATEMENTS

KALAMAZOO COMMUNITY MENTAL HEALTH AND SUBSTANCE ABUSE SERVICES

Statement of Net Position

September 30, 2016

Assets

Current assets:

Cash and cash equivalents	\$ 1,593,124
Investments	1,195,080
Accounts receivable	10,507,247
Accounts receivable - Medicaid	407,228
Due from State	364,724
Due from providers	5,280
Prepays	719,979
Total current assets	<u>14,792,662</u>

Noncurrent assets:

Long-term advances to providers	83,089
Capital assets not being depreciated	788,967
Capital assets being depreciated, net	9,775,521
Net pension asset	4,634,263
Total noncurrent assets	<u>15,281,840</u>

Total assets	<u>30,074,502</u>
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Deferred outflows of resources

Deferred pension amounts	<u>9,431,097</u>
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Liabilities

Current liabilities:

Accounts payable	4,724,107
Accrued liabilities	568,530
Due to State	1,547,039
Due to PIHP	2,345,178
Due to providers	429,310
Unearned revenue	248,001
Current portion of long-term debt	1,212,026
Total current liabilities	<u>11,074,191</u>

Noncurrent liabilities:

Long-term debt, net of current portion	<u>5,362,446</u>
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Total liabilities	<u>16,436,637</u>
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Deferred inflows of resources

Deferred pension amounts	<u>418,414</u>
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Net position

Net investment in capital assets	5,003,931
Restricted for pension benefits	13,646,946
Unrestricted	3,999,671
	<u>22,650,548</u>

Total net position	<u>\$ 22,650,548</u>
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The accompanying notes are an integral part of these financial statements.

KALAMAZOO COMMUNITY MENTAL HEALTH AND SUBSTANCE ABUSE SERVICES

Statement of Revenues, Expenses and Changes in Fund Net Position For the Year Ended September 30, 2016

Operating revenues	
Medicaid	\$ 64,167,529
Federal and state grants	6,831,105
Charges for services	2,088,669
PA2 funds	136,400
Other revenues	226,320
	<hr/>
Total operating revenues	73,450,023
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Operating expenses	
Mental health program services:	
Mental illness adult population	25,264,003
Intellectual and developmental disabilities population	28,112,327
Youth services	10,368,341
Multipopulation	3,303,048
Management and general	10,025,933
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Total operating expenses	77,073,652
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Operating loss	(3,623,629)
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Nonoperating revenues (expenses)	
County appropriation	1,550,400
Loss on disposal of capital assets	(29,735)
Interest revenue	10,844
Interest expense	(151,419)
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Total nonoperating revenues (expenses)	1,380,090
	<hr/>
Net loss before capital contributions	(2,243,539)
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Capital contributions	256,166
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Change in net position	(1,987,373)
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Net position, beginning of year	24,637,921
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Net position, end of year	\$ 22,650,548
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The accompanying notes are an integral part of these financial statements.

KALAMAZOO COMMUNITY MENTAL HEALTH AND SUBSTANCE ABUSE SERVICES

Statement of Cash Flows

For the Year Ended September 30, 2016

Cash flows from operating activities	
Cash received from providing services	\$ 68,720,630
Cash payments to suppliers	(61,462,850)
Cash payments to employees for services	<u>(14,247,798)</u>
Net cash used in operating activities	<u>(6,990,018)</u>
Cash flows from noncapital financing activities	
County appropriation	<u>1,550,400</u>
Cash flows from capital and related financing activities	
Purchase of capital assets	(3,577,670)
Capital contributions	207,056
Payments on long-term debt	(95,000)
Interest paid	<u>(151,419)</u>
Net cash used in capital and related financing activities	<u>(3,617,033)</u>
Cash flows from investing activities	
Purchases of investments	(500,000)
Sales of investments	1,263,032
Interest received	<u>8,980</u>
Net cash provided by investing activities	<u>772,012</u>
Change in cash and cash equivalents	(8,284,639)
Cash and cash equivalents, beginning of year	<u>9,877,763</u>
Cash and cash equivalents, end of year	<u>\$ 1,593,124</u>

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KALAMAZOO COMMUNITY MENTAL HEALTH AND SUBSTANCE ABUSE SERVICES

Statement of Cash Flows

For the Year Ended September 30, 2016

Reconciliation of operating loss to net cash used in operating activities	
Operating loss	\$ (3,623,629)
Adjustments to reconcile operating loss to net cash used in operating activities:	
Depreciation expense	400,716
Changes in:	
Accounts receivable	(2,887,290)
Due to/from State	(593,573)
Due to/from providers	127,102
Prepays	24,577
Net pension asset and related deferred amounts	1,848,041
Accounts payable	(1,242,348)
Accrued liabilities	130,471
Due to PIHP	(1,093,664)
Unearned revenue	(154,866)
Compensated absences	74,445
Net cash used in operating activities	<u>\$ (6,990,018)</u>

Non-cash transactions

The Authority received a donation of land. This was recorded as a capital contribution at its estimated acquisition value of \$49,110.

concluded

The accompanying notes are an integral part of these financial statements.

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NOTES TO FINANCIAL STATEMENTS

KALAMAZOO COMMUNITY MENTAL HEALTH AND SUBSTANCE ABUSE SERVICES

Notes to Financial Statements

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of Kalamazoo Community Mental Health and Substance Abuse Services (the “Authority”), established under Section 205 of the Mental Health Code, have been prepared in conformity with generally accepted accounting principles (GAAP) as applied to government units. The Government Accounting Standards Board (GASB) is the accepted standards-setting body for establishing governmental accounting and financial reporting principles. The more significant of the Authority’s accounting policies are described below.

Reporting Entity

The Authority is a community mental health authority serving the mental health needs of Kalamazoo County residents. These financial statements represent the financial condition and the results of operations of a component unit of Kalamazoo County, Michigan (the “County”) and are an integral part of that reporting entity, as defined by generally accepted accounting principals. The County also provides financial support annually to the Authority.

Financial Statements

The financial statements report information on all of the activities of Kalamazoo Community Mental Health and Substance Abuse Services.

The operations of the Authority are accounted for as an enterprise fund (a proprietary fund) which is designed to be self-supporting. Enterprise funds are used to account for operations (a) that are financed and operated in a manner similar to private business enterprises, where the intent of the governing body is that the cost of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges; or (b) where the governing body has decided that periodic determination of revenues earned, expenses incurred, and net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes.

Measurement Focus, Basis of Accounting, and Financial Statement Presentation

Enterprise fund financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

The enterprise fund is the Authority’s primary operating fund and only fund. It accounts for all financial resources of the government.

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund’s principal ongoing operations. The principal operating revenues of the Authority’s operating fund are contract revenues from the Michigan Department of Health and Human Services (MDHHS) and first and third party billings. Operating expenses include the cost of providing mental health and substance abuse services. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

When both restricted and unrestricted resources are available for use, it is the Authority’s policy to use restricted resources first, then unrestricted resources as they are needed.

KALAMAZOO COMMUNITY MENTAL HEALTH AND SUBSTANCE ABUSE SERVICES

Notes to Financial Statements

Assets, Deferred Outflows of Resources, Liabilities, Deferred Inflows of Resources, and Equity

Deposits and Investments

Cash and cash equivalents are considered to be cash on hand, demand deposits, and short-term investments with original maturities of three months or less from the date of acquisition.

State statutes authorize the Authority to invest in the accounts of federally insured banks, credit unions, and savings and loan associations; and to invest in obligations of the U.S. Treasury, certain commercial paper, repurchase agreements, bankers acceptances, and mutual funds composed of otherwise legal investments.

Receivables

Receivables consist primarily of amounts due from the State of Michigan for Medicaid billings and grant reimbursements and from other agencies, governments and organizations for services rendered.

Prepays

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaids in the financial statements.

Capital Assets

Capital assets are defined as assets with an initial cost of more than \$5,000 and an estimated useful life in excess of two years. Such assets are recorded for reporting purposes at historical cost or estimated historical cost if constructed or purchased. Donated capital assets are recorded at estimated acquisition cost at the date of donation.

Capital assets are depreciated using the straight-line method over the following estimated useful lives:

	Years
Buildings and improvements	25-40
Equipment and furniture	3-20
Vehicles	5

The Authority reviews long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset exceeds its fair value. If it is determined that an impairment loss has occurred the asset is written down to its net realizable value and a current charge to income is recognized.

KALAMAZOO COMMUNITY MENTAL HEALTH AND SUBSTANCE ABUSE SERVICES

Notes to Financial Statements

Deferred Outflows of Resources

In addition to assets, the statement of net position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, deferred outflows of resources, represents a consumption of net position that applies to a future period(s) and so will not be recognized as an outflow of resources (expense) until then. The Authority's deferred outflows of resources are related to the net pension asset. More detailed information can be found in Note 6.

Long-term Debt

Long-term debt and other long-term obligations are reported as liabilities in the statement of net position. Bond premiums and discounts, are deferred and amortized over the life of the bonds using the straight-line basis. Contracts payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as expense when incurred.

Compensated Absences

It is the Authority's policy to permit employees to accumulate paid time off, subject to certain limitations. Any earned but unused paid time off is reported as a liability in the statement of net position.

Unearned Revenue

Unearned revenue represents restricted programmatic funding not expended before year-end. It also includes that portion of the current-year MDHHS contract amount that may be carried over to and expended in subsequent fiscal years. Such carryover is generally limited to five percent of the MDHHS contract amount, and must generally be spent in the following year.

Deferred Inflows of Resources

In addition to liabilities, the statement of financial position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, deferred inflows of resources, represents an acquisition of net position that applies to one or more future periods and so will not be recognized as an inflow of resources (revenue) until that time. More detailed information can be found in Note 6.

Pensions

For purposes of measuring the net pension asset, deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about the fiduciary net position of the plan and additions to/deductions from the plan fiduciary net position have been determined on the same basis as they are reported by the plan. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

KALAMAZOO COMMUNITY MENTAL HEALTH AND SUBSTANCE ABUSE SERVICES

Notes to Financial Statements

Use of Estimates

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

2. DEPOSITS AND INVESTMENTS

Deposits and Investments

Following is a reconciliation of deposit and investment balances as of September 30, 2016:

Cash and investments

Statement of net position:	
Cash and cash equivalents	\$ 1,593,124
Investments	<u>1,195,080</u>
Total	<u>\$ 2,788,204</u>

Deposits and investments

Deposits:	
Checking/savings accounts	\$ 1,466,217
Certificates of deposit (due within one year)	1,195,080
Investments - money market funds	126,277
Cash on hand	<u>630</u>
Total	<u>\$ 2,788,204</u>

As of year-end, the Authority had the following investments:

	Carrying Amount (Fair Value)	Maturity	Rating
Money market funds - Bank of America	<u>\$ 126,277</u>	N/A	Moody's AAA-mf / S&P AAAM

Interest Rate Risk. Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of investments. The Authority's investment policy complies with State guidelines and seeks to minimize interest rate risk by investing primarily in short-term securities, liquid assets, money market funds, or similar investment pools and limiting average maturities. The policy does not place specific limitations on investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates. The investment policy states that the investment portfolio shall remain sufficiently liquid to enable the CEO, Deputy Director of Administrative Services, and Finance Director to meet all operating requirements that may be reasonably anticipated. Maturities have been identified above for all of the Authority's investments.

KALAMAZOO COMMUNITY MENTAL HEALTH AND SUBSTANCE ABUSE SERVICES

Notes to Financial Statements

Credit Risk - Investments. State law limits investments to specific government securities, certificates of deposits and bank accounts with qualified financial institutions, commercial paper with specific maximum maturities and ratings when purchased, bankers acceptances of the Authority's specific financial institutions, qualified mutual funds and qualified external investment pools as identified in the list of authorized investments in the summary of significant accounting policies. The investment policy limits investments to be made with prudent judgment as to the safety of invested capital and probable outcome of income. The investment policy states the investment portfolio shall be designed with the objective of attaining a rate of return throughout budgetary and economic cycles, commensurate with the investment risk constraints and the cash flow characteristics of the portfolio. Ratings have been identified above for all of the Authority's investments.

Custodial Credit Risk - Deposits. Custodial credit risk is the risk that in the event of a bank failure, the Authority's deposits may not be returned. State law does not require and the Authority does not have a policy for deposit custodial credit risk. As of year-end, \$1,585,039 of the Authority's bank balance of \$3,280,119 was exposed to credit risk because it was uninsured and uncollateralized.

Custodial Credit Risk - Investments. For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the Authority will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The Authority requires securities held by a third party custodian to be evidenced by safekeeping receipts. The Authority's investments are not exposed to custodial credit risk since the securities are either held by the counterparty in the name of the Authority or uncategorized as to risk.

Concentration of Credit Risk. State law limits allowable investments but does not limit concentration of credit risk. Except for U.S. Treasury Securities and authorized investment pools, the Authority limits the amount invested in a single security type or single financial institution to be no more than 60% of the total portfolio. Safety is one of the primary objectives of the Authority's investment policy, and seeks to ensure the preservation of principal in the overall portfolio. Diversification is required by the policy in order that potential losses on individual securities do not exceed the income generated from the remainder of the portfolio. At year-end, the Authority was in compliance with its approved investment policy.

Fair Value Measurements. The Authority categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The hierarchy is based on the valuation inputs used to measure the fair value of the asset. Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; Level 3 inputs are significant unobservable inputs. The Authority's investments in money market funds in the amount of \$126,277, are categorized as Level 1.

KALAMAZOO COMMUNITY MENTAL HEALTH AND SUBSTANCE ABUSE SERVICES

Notes to Financial Statements

3. CAPITAL ASSETS

Capital asset activity for the year ended September 30, 2016 was as follows:

	Beginning Balance	Additions	Disposals	Transfers	Ending Balance
Capital assets not being depreciated:					
Land	\$ 690,911	\$ 60,186	\$ -	\$ -	\$ 751,097
Work in progress	4,311,290	3,566,594	-	(7,840,014)	37,870
	<u>5,002,201</u>	<u>3,626,780</u>	<u>-</u>	<u>(7,840,014)</u>	<u>788,967</u>
Capital assets being depreciated:					
Buildings and improvements	4,455,150	-	(25,331)	7,025,686	11,455,505
Equipment and furnishings	1,717,400	-	(146,375)	814,328	2,385,353
Vehicles	27,000	-	-	-	27,000
	<u>6,199,550</u>	<u>-</u>	<u>(171,706)</u>	<u>7,840,014</u>	<u>13,867,858</u>
Less accumulated depreciation for:					
Buildings and improvements	(2,269,540)	(269,968)	24,869	-	(2,514,639)
Equipment and furnishings	(1,537,052)	(130,748)	117,102	-	(1,550,698)
Vehicles	(27,000)	-	-	-	(27,000)
	<u>(3,833,592)</u>	<u>(400,716)</u>	<u>141,971</u>	<u>-</u>	<u>(4,092,337)</u>
Total capital assets being depreciated, net	<u>2,365,958</u>	<u>(400,716)</u>	<u>(29,735)</u>	<u>7,840,014</u>	<u>9,775,521</u>
Total capital assets, net	<u>\$ 7,368,159</u>	<u>\$ 3,226,064</u>	<u>\$ (29,735)</u>	<u>\$ -</u>	<u>\$ 10,564,488</u>

Depreciation expense is allocated in the statement of revenues, expenses and changes in fund net position based on each asset's primary use.

4. LONG-TERM DEBT

Long-term debt activity for the year ended September 30, 2016, was as follows:

	Beginning Balance	Additions	Deductions	Ending Balance	Due Within One Year
Contracts payable (Bonds held by the County)	\$ 5,000,000	\$ -	\$ -	\$ 5,000,000	\$ 100,000
Note payable	500,000	-	(95,000)	405,000	95,000
	<u>5,500,000</u>	<u>-</u>	<u>(95,000)</u>	<u>5,405,000</u>	<u>195,000</u>
Premium on contracts payable	155,557	-	-	155,557	3,111
Compensated absences	939,470	1,028,399	(953,954)	1,013,915	1,013,915
Total long-term debt	<u>\$ 6,595,027</u>	<u>\$ 1,028,399</u>	<u>\$ (1,048,954)</u>	<u>\$ 6,574,472</u>	<u>\$ 1,212,026</u>

KALAMAZOO COMMUNITY MENTAL HEALTH AND SUBSTANCE ABUSE SERVICES

Notes to Financial Statements

Contracts Payable. Kalamazoo County issued general obligation bonds in the original amount of \$5,000,000 on behalf of the Authority to finance the construction of a new complex. In accordance with an intergovernmental agreement, the Authority is required to make all principal and interest payments as they become due. The bonds are due annually beginning in 2017 in amounts ranging from \$100,000 to \$400,000 with final maturity in May 2034. Interest is payable semi-annually at a rate ranging from 2.5% to 4.0%.

Note Payable. In order to finance the purchase of a building, the Authority obtained a note payable in the original amount of \$500,000 from a local bank. The note is due in annual installments ranging from \$95,000 to \$105,000 with final maturity in June 2020. The note is secured by a first real estate mortgage on the real property financed with the debt. Interest is charged based on the one-month LIBOR rate plus 1.4% (an effective rate of 2.77% at September 30, 2016).

Annual requirements, excluding compensated absences and the unamortized premium on contracts payable, to maturity on the total long-term obligations outstanding at September 30, 2016 are as follows:

Year Ended September 30,	Principal	Interest
2017	\$ 195,000	\$ 161,678
2018	200,000	155,982
2019	255,000	150,155
2020	280,000	142,714
2021	200,000	135,250
2022-2026	1,350,000	560,464
2027-2031	1,725,000	349,188
2032-2034	1,200,000	78,000
Totals	<u>\$ 5,405,000</u>	<u>\$ 1,733,431</u>

5. UNEARNED REVENUE

At September 30, 2016, unearned revenue consisted of the following:

General fund carry-forward	\$ 4,109
Unearned youth nutritional program funds	99,008
Unearned integrated healthcare funds	65,355
Unearned local funds for neonatal prevention and treatment	32,197
Unearned housing funds	39,225
Other unearned programmatic funds	<u>8,107</u>
Total	<u>\$ 248,001</u>

KALAMAZOO COMMUNITY MENTAL HEALTH AND SUBSTANCE ABUSE SERVICES

Notes to Financial Statements

6. DEFINED BENEFIT PENSION PLAN

General Information About the Plan

Plan Description. The Authority participates in the Kalamazoo County Employees' Retirement System (the "Plan"), a single-employer, defined benefit pension plan which provides retirement and disability benefits to eligible plan members and beneficiaries. The Plan was established by the Kalamazoo County Board of Commissioners and is administered by the Kalamazoo County Retirement Investment Committee. Eligible employees include those holding regular positions, either full-time or part-time, of 20 hours or more per week. The Plan is controlled by State of Michigan law. Any changes to the plan document must be approved by the Kalamazoo County Board Commissioners and subsequently implemented by the Retirement Investment Committee and the County Administrator/Controller. The Plan issues a publicly available financial report that includes financial statements and required supplementary information. The financial report may be obtained by writing to the Office of Finance, County of Kalamazoo, Michigan, 201 West Kalamazoo Avenue, Kalamazoo, Michigan 49007.

Benefits Provided. Pension benefits vary by division/bargaining unit and are calculated as final average compensation (based on a 5 year period with a maximum benefit of 75% of final average salary) and a multiplier of 2.5% (2.0% for employees hired on or after January 1, 2016). Participants are considered to be fully vested in the plan after 8 years. Normal retirement age is 55 with 25 years of service or age 60 with 8 years of service. Early retirement is available at age 55 with 8 years of service with an age reduction factor.

Employees Covered by Benefit Terms. At December 31, 2015, plan membership consisted of the following:

Inactive employees or beneficiaries currently receiving benefits	31
Inactive employees entitled to but not yet receiving benefits	53
Active employees (vested)	73
Active employees (nonvested)	<u>117</u>
 Total membership	 <u><u>274</u></u>

Contributions. The employer is required to contribute amounts at least equal to the actuarially determined rate which is adjusted on a calendar year basis. The actuarially determined rate is the estimated amount necessary to finance the cost of benefits earned by employees during the year, with an additional amount to finance any unfunded accrued liability. Employees of the Authority are not required to contribute to the Plan. Employer contributions are expressed as a percentage of covered payroll and vary by employment class:

	Calendar Year	
	2016	2015
Managerial	9.64%	9.30%
Professional	2.45%	1.93%
TOPS	5.44%	5.80%

KALAMAZOO COMMUNITY MENTAL HEALTH AND SUBSTANCE ABUSE SERVICES

Notes to Financial Statements

Pension Expense and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions

At September 30, 2016, the Authority reported an asset of \$4,634,263 for its proportionate share of the net pension asset. The net pension asset was measured as of December 31, 2015, and the total pension asset used to calculate the net pension asset was determined by an actuarial valuation rolled forward from December 31, 2014. The Authority's proportion of the net pension asset was based on the present value of future benefits for each employer (which reflects the long-term obligation of each employer to the plan) as of December 31, 2015. At December 31, 2015, the Authority's proportion was 17.724%. This was a decrease from the Authority's proportion at December 31, 2014 of 34.414%.

For the year ended December 31, 2015, the Authority recognized pension expense of \$2,346,994. The Authority reported pension-related deferred outflows of resources and deferred inflows of resources from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources	Net Deferred Outflows (Inflows) of Resources
Net difference between projected and actual earnings on pension plan investments	\$ 2,736,341	\$ -	\$ 2,736,341
Changes of assumptions	303,304	-	303,304
Changes in proportion and differences between employer contributions and share of contributions	5,985,018		5,985,018
Differences between expected and actual experience	-	418,414	(418,414)
	<u>9,024,663</u>	<u>418,414</u>	<u>8,606,249</u>
Contributions subsequent to the measurement date	406,434	-	406,434
Total	<u>\$ 9,431,097</u>	<u>\$ 418,414</u>	<u>\$ 9,012,683</u>

The amount reported as deferred outflows of resources resulting from contributions subsequent to the measurement date will be recognized as a reduction in the net pension liability for the year ending September 30, 2017. Other amounts reported as pension-related deferred outflows of resources and deferred inflows of resources will be recognized in pension expense as follows:

Year Ended September 30,	Amount
2017	\$ 2,250,239
2018	2,250,239
2019	2,250,239
2020	<u>1,855,532</u>
Total	<u>\$ 8,606,249</u>

KALAMAZOO COMMUNITY MENTAL HEALTH AND SUBSTANCE ABUSE SERVICES

Notes to Financial Statements

Actuarial Assumptions. The total pension asset in the December 31, 2014 actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

Inflation	3.5% (including price inflation of 2.75%)
Salary increases	4.0% to 5.5%
Investment rate of return	7.5%, net investment expense and including inflation
Mortality	RP-2000 Mortality Combined Healthy Tables, projected 20 years with U.S. Projection Scale BB. This table was first used for the December 31, 2014 valuation. Rates for disabled members were set forward 7 years.

The actuarial assumptions used in the December 31, 2014 valuation were based on the results of an actuarial experience study conducted in 2015 covering years 2009 to 2013.

The long-term expected rate of return on pension plan investments was determined using a model method in which the best-estimate ranges of expected future real rates of return (expected returns, net of investment and administrative expenses and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. The target allocation and best estimates of arithmetic real rates of return for each major asset class are summarized in the following table:

Asset Class	Target Allocation	Long-term Expected Real Rate of Return
U.S. Small Cap (Manager 1)	5.00%	4.25%
U.S. Small Cap (Manager 2)	10.00%	4.25%
International Developed Equity	10.00%	3.95%
U.S. Large Cap (Manager 1)	30.00%	3.75%
U.S. Large Cap (Manager 2)	5.00%	3.75%
Emerging Markets	10.00%	4.65%
Domestic Fixed Income	25.00%	0.55%
Real Estate (Manager 1)	2.50%	2.75%
Real Estate (Manager 2)	2.50%	2.75%

Discount Rate. The discount rate used to measure the total pension asset was 7.5%. The projection of cash flows used to determine the discount rate assumed that plan member contributions will be made at the current contribution rate and that Authority contributions will be made at contractually required rates, actuarially determined. Based on those assumptions, the Plan's fiduciary net position was projected to be available to make all projected future benefit payments of current active and inactive employees. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

KALAMAZOO COMMUNITY MENTAL HEALTH AND SUBSTANCE ABUSE SERVICES

Notes to Financial Statements

Sensitivity of the Net Pension Asset to Changes in the Discount Rate. The following presents the net pension asset of the Authority, calculated using the discount rate of 7.5%, as well as what the Authority's net pension asset would be if it were calculated using a discount rate that is 1% lower (6.5%) or 1% higher (8.5%) than the current rate:

	1% Decrease (6.5%)	Current Discount Rate (7.5%)	1% Increase (8.5%)
Authority's net pension asset	\$ 895,420	\$ 4,634,263	\$ 7,763,955

Pension Plan Fiduciary Net Position. Detailed information about the pension plan's fiduciary net position is available in the separately issued Plan financial statements.

Payable to the Pension Plan. At September 30, 2016, the Authority reported a payable of \$19,413 for the outstanding amount of contributions to the pension plan required for the year ended September 30, 2016.

7. DEFINED CONTRIBUTION RETIREMENT PLAN

When the Authority became a separate legal entity, it elected not to participate in the Social Security System. To provide its employees a similar retirement benefit, the Authority sponsored a 401(h) plan. Under the terms of this Plan, both the Authority and its employees are required to contribute the same amounts that would be due if the Authority had elected to participate in the Social Security System. For the year ended September 30, 2016, the Authority and its employees each contributed \$639,191. The Authority is not a fiduciary with respect to the Plan, and accordingly, assets and liabilities of the Plan have been excluded from these financial statements.

8. OTHER POSTEMPLOYMENT BENEFITS

Plan Description. The Authority participates in the Kalamazoo County Retiree Healthcare Plan, an employer financed retiree health benefit plan, which is administered by Kalamazoo County. The Authority establishes and amends the benefit provisions of the participants in the Plan. Kalamazoo County issues a publicly available financial report that includes financial statements and required supplementary information for the Plan. That report may be obtained by writing to Kalamazoo County.

Funding Policy. The Authority is required to contribute at an actuarially determined rate; the current rate is 2.50% of annual covered payroll through December 31, 2015 and 2.40% of annual covered payroll in the subsequent year.

Annual OPEB Cost and Net OPEB Obligation. The Authority's annual other postemployment benefit (OPEB) cost (expense) is calculated based on the annual required contribution of the employer (ARC), an amount actuarially determined in accordance with the parameters of GASB Statement 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years. Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Actuarially determined amounts are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future.

KALAMAZOO COMMUNITY MENTAL HEALTH AND SUBSTANCE ABUSE SERVICES

Notes to Financial Statements

During the year ended September 30, 2016, the Authority made contributions to the plan totaling \$239,851, which are based on actuarial projections of funding requirements and are equal to the required contributions. The required contribution was determined as part of the December 31, 2015 actuarial valuation. The Authority's annual OPEB cost, the percentage of annual OPEB cost contributed to the Plan, and the net OPEB obligation for 2016 and the two preceding years were as follows:

Three-Year Trend Information			
Year Ended September 30,	Annual OPEB Cost	Percentage of Annual OPEB Contribution	Net OPEB Obligation
2014	\$ 290,484	100%	\$ -
2015	238,751	100%	-
2016	239,851	100%	-

Funded Status and Funding Progress. As of December 31, 2015, the most recent actuarial valuation date, the Plan was 64.2% funded. The actuarial accrued liability for benefits was \$4,800,580 and the actuarial value of assets was \$3,083,914, resulting in an unfunded actuarial accrued liability (UAAL) of \$1,716,666. The covered projected payroll (annual payroll of active employees covered by the plan) was \$10,009,846 and the ratio of UAAL to covered projected payroll was 17.1%.

The schedule of funding progress, presented as RSI following the notes to the financial statements, presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

Actuarial Methods and Assumptions. Projections of benefits for financial reporting purposes are based on the substantive plan (the Plan as understood by the employer and Plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and Plan members to the point. The actuarial methods and assumptions used to include techniques that are designed to the reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

In the December 31, 2015 actuarial valuation, the entry-age normal actuarial cost method was used. The actuarial assumptions included (a) 7.5% investment rate of return, (b) projected healthcare trend rates of 9.0% initially, reduced to 3.5% over a period of 10 years, and (c) base pay increases of 3.5%. The unfunded actuarial accrued liability is being amortized using the level dollar method on a closed basis. The remaining amortization period for all liabilities at December 31, 2015, the date of the most recent actuarial valuation, was 26 years.

9. RISK MANAGEMENT

The risks of loss arising from general liability, property and crime, are insured through participation in the Michigan Municipal Risk Management State Pool, a public entity risk pool currently operating as a common risk management program for government entities in the State of Michigan.

KALAMAZOO COMMUNITY MENTAL HEALTH AND SUBSTANCE ABUSE SERVICES

Notes to Financial Statements

The Authority pays annual premiums to the State Pool for insurance coverage up to a maximum of \$15,000,000 for aggregate general liability claims and \$13,833,164 for property and crime claims. In the event of unusually high claims, the State Pool may assess member government units on a retroactive basis. The Authority purchases commercial insurance for risks of loss arising from employee health, medical, and workers' compensation claims. The Authority has had no settled claims resulting from these risks that exceeded its commercial coverage in any of the past three fiscal years.

10. CONCENTRATIONS AND ECONOMIC DEPENDENCY

Approximately 94% of total revenue is either directly or indirectly, paid by or due from the Michigan Department of Health and Human Services.

11. CONTINGENCIES

Under the terms of various federal and state grants and regulatory requirements, the Authority is subject to periodic audits of its agreements, as well as a cost settlement process under the full management contract with the state. Such audits could lead to questioned costs and/or requests for reimbursement to grantor or regulatory agencies. The amount, if any, of expenditures which may be disallowed cannot be determined at this time, although the Authority expect such amounts, if any, to be immaterial.

As is the case with other entities, the Authority faces exposure from potential claims and legal proceedings involving environmental and other matters. No such claims or proceedings have been asserted as of September 30, 2016.

12. NET POSITION

Net Investment in Capital Assets

As of September 30, 2016, the Authority's net investment in capital assets was comprised of the following:

Invested in capital assets:	
Capital assets not being depreciated	\$ 788,967
Capital assets being depreciated, net	<u>9,775,521</u>
	<u>10,564,488</u>
Related debt:	
Contracts payable	5,000,000
Note payable	405,000
Unamortized premium	<u>155,557</u>
	<u>5,560,557</u>
Total net investment in capital assets	<u>\$ 5,003,931</u>

Restricted Net Position

The Authority's restricted net position represents amounts held in a qualified trust for the purpose of providing pension benefits to qualified employees and retirees. This amount represents an excess of assets held in trust over the actuarial accrued liability for providing pension benefits. Since these amounts are held in trust, they cannot be accessed by the Authority or used at the Board's discretion.

KALAMAZOO COMMUNITY MENTAL HEALTH AND SUBSTANCE ABUSE SERVICES

■ Notes to Financial Statements

Unrestricted Net Position

As of September 30, 2016, unrestricted net position was comprised of the following:

Designated for equipment replacement	\$ 375,696
Undesignated	<u>3,623,975</u>
Total unrestricted net position	<u>\$ 3,999,671</u>

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REQUIRED SUPPLEMENTARY INFORMATION

KALAMAZOO COMMUNITY MENTAL HEALTH AND SUBSTANCE ABUSE SERVICES

Required Supplementary Information Defined Benefit Pension Plan

Schedule of the Authority's Proportionate Share of the Net Pension Asset

	Year Ended September 30,	
	2015	2016
Authority's proportion of the net pension asset	34.414%	17.724%
Authority's proportionate share of the net pension asset	\$ 14,791,176	\$ 4,634,263
Authority's covered-employee payroll	10,422,152	10,009,846
Authority's proportionate share of the net pension asset as a percentage of its covered-employee payroll	141.9%	46.3%
Plan fiduciary net position as a percentage of the total pension liability	126.6%	115.7%

The amounts presented for each fiscal year were determined as of December 31 of the preceding year.

GASB 68 was implemented in fiscal year 2015. This schedule is being built prospectively. Ultimately, 10 years of data will be presented.

KALAMAZOO COMMUNITY MENTAL HEALTH AND SUBSTANCE ABUSE SERVICES

Required Supplementary Information Defined Benefit Pension Plan

Schedule of Contributions

Fiscal Year Ended September 30,	Actuarially Determined Contribution	Contributions in Relation to the Actuarially Determined Contribution	Contribution Deficiency (Excess)	Covered-Employee Payroll	Contributions as Percentage of Covered-Employee Payroll
2015	\$ 515,417	\$ 515,417	\$ -	\$ 9,773,277	5.3%
2016	504,126	504,126	-	10,142,610	5.0%

Note: GASB 68 was implemented in fiscal year 2015. This schedule is being built prospectively. Ultimately, 10 years of data will be presented.

KALAMAZOO COMMUNITY MENTAL HEALTH AND SUBSTANCE ABUSE SERVICES

Required Supplementary Information

Retiree Healthcare Plan

Schedule of Funding Progress

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) - Entry Age (b)	Underfunded AAL (UAAL) (b-a)	Funded Ratio (a / b)	Covered Payroll (c)	UAAL as a % of Covered Payroll ((b-a) / c)
12/31/2011	\$ 2,521,844	\$ 5,191,359	\$ 2,669,515	48.6%	\$ 9,552,465	27.9%
12/31/2013	3,148,454	4,621,935	1,473,481	68.1%	10,116,884	14.6%
12/31/2015	3,083,914	4,800,580	1,716,666	64.2%	10,009,846	17.1%

Schedule of Employer Contributions

Fiscal Year Ended September 30,	Annual Required Contribution	Percentage Contributed
2014	\$ 290,484	100%
2015	238,751	100%
2016	239,851	100%

SINGLE AUDIT ACT COMPLIANCE

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INDEPENDENT AUDITORS' REPORT ON THE
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
REQUIRED BY THE UNIFORM GUIDANCE

March 21, 2017

Board of Directors
Kalamazoo Community Mental Health and
Substance Abuse Services
Kalamazoo, Michigan

We have audited the financial statements of *Kalamazoo Community Mental Health and Substance Abuse Services* (the "Authority"), a component unit of Kalamazoo County, Michigan, as of and for the year ended September 30, 2016, and the related notes to the financial statements, which collectively comprise the Authority's basic financial statements. We issued our report thereon dated March 21, 2017, which contained an unmodified opinion 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 Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) 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 basic financial statements and certain other 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 expenditures of federal awards is fairly stated in all material respects in relation to the basic financial statements as a whole.

Rehmann Robson LLC

KALAMAZOO COMMUNITY MENTAL HEALTH AND SUBSTANCE ABUSE SERVICES

Schedule of Expenditures of Federal Awards For the Year Ended September 30, 2016

Federal Agency / Cluster / Program Title	CFDA Number	Passed Through	Pass-through / Grantor Number	Total Subawards	Federal Expenditures
U.S. Department of Housing and Urban Development Emergency Shelter Grant Program	14.231	MSHDA	HML-2015-Housing-5395-ESF	\$ -	\$ 31,342
Continuum of Care Program:					
HUD Grant (HBI) - Renewal 10 (1 yr.)	14.267	Direct	MI0183L5F071407	-	213,731
HUD Grant (HBI) - Renewal 11 (1 yr.)	14.267	Direct	MI0183L5F071508	-	79,123
HUD Grant (HBII) - Renewal 7 (1 yr.)	14.267	Direct	MI0184L5F071407	-	67,890
HUD Grant (HBII) - Renewal 8 (1 yr.)	14.267	Direct	MI0184L5F071508	-	191,910
HUD Grant (HBIII) - Renewal 7 (1 yr.)	14.267	Direct	MI0185L5F071407	-	52,305
HUD Grant (HBIII) - Renewal 8 (1 yr.)	14.267	Direct	MI0185L5F071508	-	3,242
HUD Grant (Full Count) - Renewal 7 (1 yr.)	14.267	Direct	MI0182L5F071407	-	37,695
HUD Grant (Full Count) - Renewal 8 (1 yr.)	14.267	Direct	MI0182L5F071508	-	3,103
HUD Grant (Home Run) - Renewal 5 (1 yr.)	14.267	Direct	MI0332L5F071405	-	30,961
HUD Grant (Home Run) - Renewal 6 (1 yr.)	14.267	Direct	MI0332L5F071506	-	16,334
HUD Grant (1st Base) - Renewal 5 (1 yr.)	14.267	KCPHC	MI0295L5F071305	-	7,553
HUD Grant (1st Base) - Renewal 6 (1 yr.)	14.267	KCPHC	MI0295L5F071406	-	34,429
HUD Grant (2nd Base) - Renewal 5 (1 yr.)	14.267	Direct	MI0296L5F071406	-	37,249
HUD Grant (3rd Base) - Renewal 3 (1 yr.)	14.267	Direct	MI0346L5F071302	-	12,354
HUD Grant (3rd Base) - Renewal 4 (1 yr.)	14.267	Direct	MI0346L5F071403	-	46,542
HUD Grant (Grand Slam) - Renewal 4 (1 yr.)	14.267	Direct	MI0178L5F071405	-	25,642
HUD Grant (Grand Slam) - Renewal 5 (1 yr.)	14.267	Direct	MI0178L5F071506	-	32,031
HUD Transitional Housing - 15/16	14.267	Direct	MI0187L5F071407	41,742	51,812
				<u>41,742</u>	<u>943,906</u>
Total U.S. Department of Housing and Urban Development				<u>41,742</u>	<u>975,248</u>
U.S. Department of Education Race to the Top - Early Learning Challenge	84.412	MDHHS	20161208-00	10,077	10,077
U.S. Department of Health and Human Services Comprehensive Community Mental Health Services for Children with Serious Emotional Disturbances (SED)	93.104	Direct	1U79SM062448-01	-	450,277
Projects for Assistance in Transition from Homelessness (PATH)	93.150	MDHHS	2X06SM016023-15	-	35,062
Substance Abuse and Mental Health Services - Projects of Regional and National Significance	93.243	Direct	1H79SM062205-01	-	297,100
Medical Assistance Program:					
OBRA - PASARR	93.778	MDHHS	n/a	151,946	151,946
University of Michigan Liaison Grant	93.778	UofM	3003839663	-	42,866
University of Michigan MAP Grant	93.778	UofM	3003738641	-	11,815
Community Health Access Program (CHAP)	93.778	UofM	n/a	-	9,144
				<u>151,946</u>	<u>215,771</u>
Block Grants for Community Mental Health Services:					
Behavioral Health Consultant Grant	93.958	MDHHS	20161208-00	-	38,662
Parent Management Training - Statewide Coordination	93.958	MDHHS	20161209-00	-	258,898
				<u>-</u>	<u>297,560</u>
Total U.S. Department of Health and Human Services				<u>151,946</u>	<u>1,295,770</u>
Total Expenditures of Federal Awards				<u>\$ 203,765</u>	<u>\$ 2,281,095</u>

See accompanying notes to schedule of expenditures of federal awards.

KALAMAZOO COMMUNITY MENTAL HEALTH AND SUBSTANCE ABUSE SERVICES

Notes to Schedule of Expenditures of Federal Awards

1. BASIS OF PRESENTATION

The accompanying schedule of expenditures of federal awards (the "Schedule") includes the federal grant activity of Kalamazoo Community Mental Health and Substance Abuse Services (the "Authority") under programs of the federal government for the year ended September 30, 2016. The information in this Schedule is presented in accordance with the requirements of Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Because the Schedule presents only a selected portion of the operations of the Authority, it is not intended to and does not present the financial position, changes in net position or cash flows of the Authority.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Expenditures reported on the Schedule are reported on the modified accrual basis of accounting, which is described in Note 1 to the Authority's financial statements. Such expenditures are recognized following the cost principles contained in the Uniform Guidance, wherein certain types of expenditures are not allowable or are limited as to reimbursement. Pass-through entity identifying numbers are presented where available.

For purposes of charging indirect costs to federal awards, the Authority has not elected to use the 10% de minimis cost rate as permitted by §200.414 of the Uniform Guidance.

3. PASS-THROUGH AGENCIES

The Authority receives certain federal grants as subawards from non-federal entities. Pass-through entities, where applicable, have been identified in the Schedule with an abbreviation, defined as follows:

Abbreviation	Pass-through Agency Name
KCPHC	Kalamazoo County Public Housing Commission
MDHHS	Michigan Department of Health and Human Services
MSHDA	Michigan State Housing Department Authority
UofM	University of Michigan



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INDEPENDENT AUDITORS' 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*

March 21, 2017

Board of Directors
Kalamazoo Community Mental Health and
Substance Abuse Services
Kalamazoo, Michigan

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 *Kalamazoo Community Mental Health and Substance Abuse Services* (the "Authority"), a component unit of Kalamazoo County, Michigan, as of and for the year ended September 30, 2016, and the related notes to the financial statements, which collectively comprise the Authority's basic financial statements, and have issued our report thereon dated March 21, 2017.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Authority'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 opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control. Accordingly, we do not express an opinion on the effectiveness of the Authority's internal control.

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 a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. 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 first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Authority'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*.

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 Authority'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 entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Rehmann Robson LLC

INDEPENDENT AUDITORS' REPORT ON COMPLIANCE FOR
EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER
COMPLIANCE REQUIRED BY THE UNIFORM GUIDANCE

March 21, 2017

Board of Directors
Kalamazoo Community Mental Health and
Substance Abuse Services
Kalamazoo, Michigan

Report on Compliance for Each Major Federal Program

We have audited the compliance of *Kalamazoo Community Mental Health and Substance Abuse Services* (the "Authority"), a component unit of Kalamazoo County, Michigan, with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on each of the Authority's major federal programs for the year ended September 30, 2016. The Authority's major federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with federal statutes, regulations, and the terms and conditions of its federal awards applicable to its federal programs.

Independent Auditors' Responsibility

Our responsibility is to express an opinion on compliance for the Authority's major federal programs 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 the requirements of Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Those standards and the Uniform Guidance 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 a major federal program occurred. An audit includes examining, on a test basis, evidence about the Authority'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 each major federal program. However, our audit does not provide a legal determination of the Authority's compliance.

Opinion on Each Major Federal Program

In our opinion, the Authority complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended September 30, 2016.

Report on Internal Control Over Compliance

Management of the Authority 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 Authority's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, 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 Authority'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 a 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 and therefore, material weaknesses or significant deficiencies may exist that were not identified. 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.

Purpose of this Report

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 the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

Rehmann Lobson LLC

KALAMAZOO COMMUNITY MENTAL HEALTH AND SUBSTANCE ABUSE SERVICES

Schedule of Findings and Questioned Costs For the Year Ended September 30, 2016

SECTION I - SUMMARY OF AUDITORS' RESULTS

Financial Statements

Type of auditors' report issued: Unmodified

Internal control over financial reporting:

Material weakness(es) identified? yes X no

Significant deficiency(ies) identified? yes X none reported

Noncompliance material to financial statements noted? yes X no

Federal Awards

Internal control over major programs:

Material weakness(es) identified? yes X no

Significant deficiency(ies) identified? yes X none reported

Type of auditors' report issued on compliance for major programs: Unmodified

Any audit findings disclosed that are required to be reported in accordance with 2 CFR 200.516(a)? yes X no

Identification of major programs:

<u>CFDA Number</u>	<u>Name of Federal Program or Cluster</u>
93.104	Comprehensive Community Mental Health Services for Children with Serious Emotional Disturbances (SED)
93.150	Projects for Assistance in Transition from Homelessness (PATH)

Dollar threshold used to distinguish between Type A and Type B programs: \$ 750,000

Auditee qualified as low-risk auditee? X yes no

KALAMAZOO COMMUNITY MENTAL HEALTH AND SUBSTANCE ABUSE SERVICES

Schedule of Findings and Questioned Costs For the Year Ended September 30, 2016

SECTION II - FINANCIAL STATEMENT FINDINGS

No matters were reported.

KALAMAZOO COMMUNITY MENTAL HEALTH AND SUBSTANCE ABUSE SERVICES

Schedule of Findings and Questioned Costs For the Year Ended September 30, 2016

SECTION III - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

No matters were reported.

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KALAMAZOO COMMUNITY MENTAL HEALTH AND SUBSTANCE ABUSE SERVICES

Summary Schedule of Prior Audit Findings

For the Year Ended September 30, 2016

2015-001 - Written Policies Required by the Uniform Grant Guidance
CFDA #14.267 - Continuum of Care Program

The Uniform Grant Guidance requires a non-federal entity that has expended federal awards for a grant awarded on or after December 26, 2014 to have various written policies. These policies were documented in writing in the current year. This matter is considered resolved.

