

October 31, 2007

To the Honorable Mayor and
Members of the City Council
City of Rochester Hills
1000 Rochester Hills Drive
Rochester Hills, MI 48309-3033

Dear Mayor and Council Members:

The purpose of this letter is to follow up on our brief discussion at this year's audit presentation regarding the upcoming changes in auditing standards. Major and comprehensive changes have been made to auditing rules that will impact the City's audits beginning with the year ended December 31, 2007. Eight new auditing standards have been issued (Statements on Auditing Standards 104 through 111) that require significant changes in how audits are performed. Similar to the Sarbanes-Oxley rules that impacted publicly held corporations, these rules are intended to help audited entities strengthen their internal controls. We have recently put on a seminar explaining these new rules, which was attended by your staff. In brief, these new rules require all auditors to:

- Obtain a deeper understanding of the design and operation of internal control
- Assess the effectiveness of internal control
- Obtain corroborating evidence that the understanding is correct and the assessment is appropriate (i.e., inspection of documents, observation of procedures, or inquiry)
- Consider "what could go wrong" in the financial statement process (evaluate the risks of financial statement errors)
- Link the results to specific further audit procedures
- Communicate a summary of the results of the auditor's work to those charged with governance (the city council)

As you can see, auditors will spend significantly more time working with all aspects of your internal control (accounting processes, information technology general and application controls, and traditional internal control procedures). The intent of these new rules is to help audited organizations deal with their internal control. The thought process is that internal control is critically important to any organization, and it would be better served if the annual audit focused significant work on its effectiveness. These new rules are not limited to the public sector – they will apply to any organization that obtains an audit (non-profit organization, private company, etc.).

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These new rules will impact audited organizations in two ways:

- Your Finance and Accounting staff will incur more effort in preparation for the audit; and
- The additional audit time required will increase the cost of the annual audit.

Plante & Moran has spent the last six months creating the new audit forms and documents that will be needed to meet these new rules. The internal control and accounting process documentation documents have already been shared with Finance and Accounting staff.

We have evaluated the additional effort that we expect to incur in the upcoming audits. Our best estimate is that we will incur additional costs of \$12,000 in this first year, including the audit of the City, the Older Persons' Commission and Rochester-Avon Recreation Authority. In the second year (calendar 2008 audit), we expect this added effort to decrease to \$5,000. We would be happy to work with the City to amend our original fee quote in a manner that would minimize your budget impact; for instance, an increase of \$7,000 per year would spread these costs over a three year period.

We would like to thank the City for the continued opportunity to serve as your auditor. We would be happy to answer any questions or concerns you have regarding the new auditing standards and their impact on the services we provide to the City.

Very truly yours,

PLANTE & MORAN, PLLC



Joseph C. Heffernan