

TOWN OF MILLBURY, MASSACHUSETTS

Management Letter

For the Year Ended June 30, 2007

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To the Board of Selectmen
Town of Millbury, Massachusetts

In planning and performing our audit of the financial statements of the Town of Millbury, Massachusetts as of and for the year ended June 30, 2007, in accordance with auditing standards generally accepted in the United States of America, we considered the Town of Millbury's internal accounting control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Town's internal control. Accordingly, we do not express an opinion on the effectiveness of the Town's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control that we consider to be significant deficiencies.

A control deficiency 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 misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control. Deficiencies considered to be significant deficiencies in internal control are noted in the table of contents and comment headings.

Additional Offices:

Greenfield, MA • Ellsworth, ME • Nashua, NH • Manchester, NH

In addition, during our audit we became aware of several matters that are opportunities for strengthening internal controls and operating efficiency. The recommendations that accompany this letter summarize our comments and suggestions concerning those matters.

The Town's written response to our comments and suggestions has not been subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

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

After you have had an opportunity to consider our comments and recommendations, we would be pleased to discuss them with you.

Melanson Heath + Company P.C.

Andover, Massachusetts

April 8, 2008

FOLLOW-UP ON PRIOR YEAR RECOMMENDATIONS:

1. Monitor Activity in Police Detail Revolving Account (Significant Deficiency)

Prior Year Issue:

In the prior year, we recommended the Town monitor all activity flowing through the police detail revolving account to assure postings are accurate and up to date.

Current Year Status:

This recommendation has not been implemented. The police detail revolving account experienced a loss for the year of approximately \$ (27,000), resulting in a June 30, 2007 accumulated deficit of approximately \$ (117,000).

Further Action Needed:

We continue to recommend the Town monitor all activity flowing through the police detail revolving account and compare the deficit balance with receivable records to determine whether a true deficit exists.

Town's Response:

The Town has taken steps to correct the activity in the account in FY2008. The Police Department purchased a billing program that provides an outstanding receivable by vendor. The General Ledger has been changed to monitor the receivable on a weekly basis. The Department sends the Finance office the accounts receivable, and we enter the receivable on our end. The Finance office reviews the file every 30 days for noncompliance.

2. Continue to Prepare for GASB Statement 45

Prior Year Issue:

In the prior year, we recommended that the Town begin the process of implementing GASB Statement 45 by budgeting and contracting for an actuarial valuation. This will assure that the Town will be prepared to meet the upcoming reporting requirements of GASB Statement 45 by fiscal year 2009.

Current Year Status:

This recommendation has not been implemented.

Further Action Needed:

We continue to recommend the Town begin the process of implementing GASB Statement 45 in order to assure compliance by fiscal year 2009.

Town's Response:

The Town issued an Invitation for Bids in January, 2008 and has awarded the contract to USI Consulting for Actuarial Services to be in compliance with Statement 45.

CURRENT YEAR RECOMMENDATIONS:

3. Improve Financial Reporting and Accounting System (Significant Deficiency)

In order for the Town's financial statements to be materially fairly stated in accordance with Generally Accepted Accounting Principles, several audit entries were required. The following is a list of entries made and/or issues encountered during the audit:

- General Fund Balance accounts needed to be analyzed in detail, and entries were required to record and reconcile operating transfers in and out.
- Non-general Fund Balance accounts needed to be analyzed in detail and entries were required to report revenue and expenditure activity.
- Capital Asset records were revised on several occasions and required material adjustments.
- Year-end encumbrances (the carryforward of available appropriation) were recorded as expenditures rather than a reservation of fund balances. Similarly, the expenditures of 2006 encumbrances were recorded as direct reductions to fund balance rather than expenditures.

Instead of relying on the year end audit to adjust balance sheet and revenues and expenditure accounts, we recommend that the Town monitor its balance sheet on a monthly basis and develop year end closing procedures in order to improve financial reporting.

Town's Response:

The Town has addressed some of these issues and is currently monitoring. The computer system the Town uses at year-end closes the purchase orders to fund balance and charges the accounts as expenditures. We have discussed this with Unifund, and they have provided the Town with a work-around to resolve the issue with the Fund Balance account. This is an ongoing problem with the system the Town uses. The capital assets were adjusted at year-end. The Town closed the Special Revenue accounts to designated Fund Balance accounts to close the year and balance forward. The Town will provide the audit firm with the account breakdown by revenues and expenditures in excel format.

**4. Consider Implementing Internal Control Improvements
(Significant Deficiency)**

In accordance with a new generally accepted audit standard (SAS 112), which is effective for all fiscal year 2007 audits, independent auditors must now report issues (called "significant deficiencies") to the governing body. The definition of this term is included in the opening letter to this management letter.

SAS 112 specifically requires that certain situations, if present in the municipality, must be reported as a significant deficiency. Although these conditions may not be new to the municipality, and may be very common practices for Massachusetts municipalities, they must now be reported in the management letter. The governing body of the Town should evaluate the cost/benefit of these issues to determine whether corrective action is warranted.

The following summarizes certain of the current and past practices in the Town that meet the new criteria of significant deficiencies:

Establish Internal Controls over the Preparation of Audited Financial Statements:

Although the Town maintains its accounting records in accordance with standards established by the State statutes, and is able to prepare reports for internal and State purposes, historically, the annual financial statements have been drafted by the independent auditor. Because the Town must take full responsibility for the accuracy and disclosure of the financial statements, it must, either internally, or through the use of a qualified outside party (other than the independent auditor), review the financial statements and related footnote disclosures to assure compliance with generally accepted accounting principles, and to verify that no material misstatements exist. Relying on the independent auditor to perform these functions is considered a control deficiency.

Corrective Action to be Considered:

The Town should either provide additional staff training in the area of preparing financial statement prepared under the GASB 34 reporting model, or retain a service provider to prepare, assist in the preparation, or review the statements to ensure material misstatements are not present.

Document Components of Internal Control:

In order to establish an effective system of internal controls, the Town should document the policies, procedures and controls over key financial transactions, including cash, tax/excise/utility, receivable activity, departmental receipts, purchasing, vendor disbursements, employee benefit/payroll disbursements, and general ledger maintenance. This documentation could be used by departments as guidance to help safeguard assets, properly record transactions, and provide a basis for continuing operations when turnover occurs in key financial departments. Although the Town maintains certain policies and procedures, they are not complete, approved by the Board of Selectmen, and/or distributed to all applicable departmental personnel.

Corrective Action to be Considered:

Several years ago, the Committee on Sponsoring Organizations (COSO) of the President's Council on Integrity and Efficiency published comprehensive internal control guidance that has recently

- The Student Activity funds held at Elmwood Street and Raymond E. Shaw schools are currently not Massachusetts General Law (MGL) compliant. Currently, both schools are making deposits to checking accounts held by the principals, instead of agency accounts held by the Treasurer, as required by MGL's.

We recommend that the Town comply with Massachusetts General Law. This will increase the oversight the Town has over the Student Activity Funds.

- During fiscal 2007, the Jr./Sr. High School Student Activity fund checking account bank statement had not been reconciled to the School's check book records for several months. A reconciliation was subsequently provided, however it differed from the School's records by approximately \$ 10,000.

We recommend that the checking account bank statement be reconciled to the School's check book balance monthly. In addition, total student activity fund program balances should be reconciled to both the checking account, and savings accounts bank statements, monthly.

- The Town Treasurer maintains the Jr./Sr. High School savings account bank statement as per MGL, however, annually transfers any balance over \$ 10,000 to the Town's money market account. This makes the reconciliation of the savings account bank statement to both the Town's Agency general ledger balance and to the School's program records a difficult process.

We recommend that the Town Treasurer transfer the appropriate amount back to the Student Activity fund savings bank account, and monthly perform reconciliations between the bank statement and both the general ledger and the School's program records.

- There appears to be a lack of segregation of duties at all schools. For example, the same individual assigned to prepare the monthly bank reconciliations is also responsible for preparing deposits, recording and maintaining the ledger, and writing and maintaining the checks.

We recommend another individual review the monthly reconciliations and initial or sign the actual reconciliations to provide documented evidence of the review. In addition, the monthly reconciliations should be provided to the Town Treasurer's office.

- The Town has not performed internal audits of the student activity funds over the last several years.

We recommend that the Town perform an annual review of the student activity funds at all schools. This will help ensure that errors and irregularities do not go undetected.

Town's Response:

When the Massachusetts General Law was changed several years ago to require schools to develop certain procedures for the managing of student activity accounts, the audit firm, at the time, felt that the volume of transactions in the small accounts at both the Elmwood Street School and the Shaw Elementary School were insignificant and not required to have agency and district accounts set up. The volume of transactions has increased, and we will comply with the requirement for both those schools.

The Jr./Sr. High School Student Activity Account is managed well by the Principal's Office with oversight by the Business Office. Expenditures made from this account must be submitted through the warrant process to the Business Office, then to the Finance Office in order for the Student Activity Account to be reimbursed. The account is normally reconciled monthly, some confusion as to how to handle a \$ 10,000 adjustment left the account unreconciled. This will be corrected, and we will set up a process wherein those reconciliations are transmitted to the Treasurer's Office for her review. This will help mitigate issues with the segregation of duties. It should be noted that the clerk who writes out the checks and manages the account is not the same individual who sets up the reimbursement.

The Town will work with the School Department on this issue and will be performing audits of their records to the General Ledger.

6. Revise Budget Procedures

The Town has historically used unbudgeted local revenues from the current fiscal year as a funding source for subsequent year budget appropriations. However, Massachusetts General Law does not permit such an action.

We recommend that the Town budget all anticipated local revenue sources and use only legitimate financing sources; such as free cash, overlay surplus, and other available sources allowed by Massachusetts General Laws to be used to fund budget appropriations. This will result in compliance with state statutes and provide the Town with a more accurate revenue budget.

Town's Response:

The FY2009 will be in compliance with Massachusetts General Laws, the Town will not transfer current year revenues to offset the operating budget in the next fiscal year as past practice.

7. Improve Controls over Petty Cash and Departmental Receipts

Petty Cash

The Town currently has established various departmental petty cash funds to deal with short-term disbursements needs. However, we noted that no formal policies or procedures exist to provide departments with guidance in the proper maintenance and uses of petty cash funds. We also noted that departments are not providing signed receipts to indicate reimbursement has been received.

We recommend that the Town create and implement formal documented policies and procedures to address the weaknesses noted above.

Departmental Receipts

The Town has created policies and procedures for remitting departmental receipts to the Treasurer, however, as of the date of the audit, this policy has neither been approved by the Board of Selectmen, nor distributed to

the departments for implementation. We noted the following weaknesses while reviewing departmental receipts:

- The log maintain by the DPW department does not include dollar amounts paid. Therefore, turnovers to the Treasurer cannot be traced easily back to departmental records.
- Departments are not stamping checks for "deposit only". This is being performed only at the Treasurer's office.
- Departments are not reconciling departmental records to the Town's general ledger to ensure accuracy.
- Prenumbered receipts are not being provided to customers upon payment.
- There is a lack of segregation of duties. The same individual is responsible for multiple tasks related to the collection, reporting, and turnover of receipts with limited or no oversight.

We recommend that the Town approve, implement, and adhere to policies and procedures to address the weaknesses noted above.

Town Response:

The Town had addressed this issue in FY2007, but had not fully implemented the program until FY2008. The Board of Selectmen adopted a departmental receipts policy in December 2007. We have distributed the policy to all departments and have reviewed the procedures with the departments. The Finance Office is in the process of auditing departmental receipts with each department.