

TOWN OF WINCHENDON, MASSACHUSETTS

MANAGEMENT LETTER

YEAR ENDED JUNE 30, 2013

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Board of Selectmen
Town of Winchendon
Winchendon, Massachusetts

In planning and performing our audit of the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the Town of Winchendon, Massachusetts, (the "Town") as of and for the year ended June 30, 2013, in accordance with auditing standards generally accepted in the United States of America, we considered the Town's internal control over financial reporting ("internal control") as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Town's internal control. Accordingly, we do not express an opinion on the effectiveness of the Town's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or 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.

Our consideration of internal control over financial reporting 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 financial reporting that might be control deficiencies, significant deficiencies, or material weaknesses. We identified deficiencies that we have considered material weaknesses. Those are identified as such in the body of this report.

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

Roselli Clark & Associates

Roselli, Clark & Associates
Certified Public Accountants
Woburn, Massachusetts
July 21, 2014

I. OVERVIEW

Winchendon is a community that continues to struggle to meet the financial requirements necessary to service its population. The effects of a disturbing trend that began to manifest itself in fiscal 2012 are now reaching their full impact. Adverse operating results in each of 2013 and 2014 have contributed to cause negative free cash, which presently stands as the **lowest** of all 351 communities in the Commonwealth of Massachusetts.

During the most recent fiscal year and continuing through the date of this report, the Town's biggest challenge has been liquidity to meet its basic operating needs. While the 2013 and 2014 budgets began in balance, a reduction in revenues combined with the lack of ongoing budget monitoring that resulted in major line item and fund balance deficits, contributed to this urgent situation.

Compounding this issue was the major transition that occurred with the retirement of both the Treasurer/Collector and Town Accountant. Both were long-term employees with significant operational and institutional knowledge.

The Town ended fiscal year 2013 with approximately \$2.35 million in unassigned fund balance. This was comprised mainly of the general stabilization fund balance of nearly \$1.58 million. On the surface, this appears to be a healthy reserve balance, however, the numerous deficits previously discussed in fiscal 2013 which are anticipated to grow much larger after the close of fiscal 2014 will place these reserve balances in jeopardy as the Town moves towards setting its tax rate for fiscal year 2015.

In light of this situation, management needs to be very efficient in its operations to maintain a level of service on-par with those provided by similar peer communities. Without a large general proposition 2 ½ override or a liquidation in its reserve balances, the Town will have no option but to reduce general governmental services, including public safety, public works, public library and others, which will ultimately reduce the quality in the delivery of services. As a result, management should review the recommendations included in this report and make every attempt to implement those that it feels can be effectively implemented in a cost efficient manner.

II. INFORMATIONAL ITEMS

Statement on Auditing Standards No. 115 – Audit Communications

The American Institute of Certified Public Accountants (“AICPA”) in 2009 issued Statement on Auditing Standards No. 115, *Communicating Internal Control Related Matters Identified in an Audit* (“SAS 115”). SAS 115 establishes new standards and provides guidance on communicating matters related to an entity’s internal control over financial reporting identified in an audit of financial statements. In particular, SAS 115 provides guidance on evaluating the severity of deficiencies in internal control identified in an audit of financial statements in the following order:

1. Deficiency in internal control
2. Significant deficiency
3. Material weakness

Deficiencies identified as *significant deficiencies* or *material weaknesses* are required to be communicated to those charged with governance. *Deficiencies in internal control* are not required to be communicated; however, we have chosen to also report that type of deficiency in this report.

We did not classify any of the findings as significant deficiencies, but we did determine that two of the findings in this report should be categorized as material weaknesses.

Policies and Procedures Manual

While the Town makes diligent attempts to follow standard policies as delineated by the Department of Revenue and MGLs, and formalizes some policies through interoffice memorandum, the Town does not formally document policies, procedures and controls for key financial transactions in one comprehensive manual. As a result, these transactions are at risk of being performed in an inconsistent and inefficient manner by the Town’s departments.

This became readily apparent for fiscal year 2013, when the loss of key financial personnel to retirement or resignation within various Town departments resulted in many hurdles being created that led to significant challenges and inefficiencies in closing the Town’s financial records. This was exacerbated to the point that there was a need to bring in a short-term consultant to mitigate the time lost in addressing the various accounting issues that transpired.

The Town should endeavor to create a policy and procedure manual that would establish consistency in financial policies between departments. Given the size of the Town and its limited resources, we would understand that the Town would not be able to compile such a manual within a year; however, completing the task over a 2 or 3 year period may be reasonable.

Risk Assessment and Fraud Identification Measures

As discussed at a previous year exit conference with the Board of Selectmen, we continue to caution our municipal clients like Winchendon, regarding the risks of fraud and theft. In these trying economic times, it is reasonable to expect that the frequency of fraud and theft by employees, customers and vendors may increase. The Town should be well aware of this increased risk, and accordingly should evaluate and enhance measures to better safeguard the

Town's cash and other assets. Fraud can include theft, the misappropriation of assets such as cash or easily marketable equipment like computers, the execution of transactions with related parties that are not disclosed and not completed "at arm's length," or the modification or fabrication of financial records to protect job security. The Town must increase its focus and awareness of fraud risks throughout all areas of local government. Suspicious or unusual activity, particularly in cash handling areas, should be promptly investigated.

The Board of Selectmen did take a significant step in combating this growing threat by adopting a Town government Fraud Policy. This is important because it establishes a baseline as to what the Town will define as fraud, and how the Town will approach potential fraud incidents brought to the attention of management.

In addition, we further suggest the Town consider implementing the following:

Establish a Limited Internal Audit Process – The Town does not have sufficient, existing personnel resources to dedicate to an autonomous, internal audit function. However, under Chapter 41 of Massachusetts General Law ("MGL"), the Town Accountant or equivalent position has the ability to examine books and records of any department on a periodic basis, and at least on an annual basis.

We suggest that the Accounting Office cycle audit the cash handling departments. A different department should be chosen each month, and the cash handling for that month should be reconciled independently. Such a process would provide an excellent deterrent against risk of fraud and would not take long to complete. We have previously advised the Town towards implementing this recommendation.

Additionally, we would point out that due to timing and staffing constraints within their Town Accountant Offices, some communities are instead engaging their external auditor to perform additional, departmental review procedures as part of the audit process. Generally, one or two departments are selected by Town management annually for such a review.

The ultimate goal is that over a period of a few years, all cash handling departments could be reviewed, and a report issued citing areas of needed improvement that can be used as document for evaluating corrective action implementation.

The Town should be aware that our audit procedures are designed to provide reasonable assurance that the financial statements are fairly presented and free of material misstatement. Our audit includes considerations for fraud; however, no assurances can be given that we would detect fraud through our audit. Our audit cannot be relied upon to detect fraud or illegal acts that may exist.

Student Activity Accounts

Our firm performed an audit of the Student Activity Accounts as of June 30, 2012; this was a separately issued report and the various findings relative to the operation of these accounts identified can be reviewed in detail within that report. Under MGL c.71 s.47, the School Department is next required to have the independent audit of these accounts for the year ended June 30, 2015.

Additional, we would note that in fiscal year 2014, the Massachusetts Department of Elementary and Secondary Education (ESE) issued formal compliance guidelines under this

MGL which now clearly requires not only the triennial independent audit, but that an annual, documented internal review be performed by the School Department over these accounts at each school building location in accordance with the Student Activity Account compliance supplement published by the ESE. The ESE is requiring immediate compliance with these guidelines; accordingly, the School Department should plan on performing and documenting their internal review of these accounts during fiscal year 2015, relative to the activities for the year ended June 30, 2014.

Health Insurance Legislation

Chapter 69 of the Act of 2011 was signed into law by the Governor on July 12, 2011. This is an Act relative to Municipal Health Insurance. The Act amends Chapter 32B and as a result of its enactment, Section 26 will be added to Chapter 32B and reads as follows:

An appropriate public authority of a political subdivision which has undertaken to provide health insurance coverage to its subscribers under this chapter shall conduct an enrollment audit not less than once every 2 years. The audit shall be completed in order to ensure that members are appropriately eligible for coverage.

This audit, which may be conducted internally, has yet to be conducted by the Town. Other Towns that have performed this audit are showing a savings on health insurance costs as these audits are uncovering ineligible participants such as those who no longer qualify due to death, divorce or termination of employment.

Deminimis Property Tax Assessments

The Town annually assesses property taxes for each tax entity for which the Town has reported taxable personal property. A large number of these personal property tax accounts have valuations less than \$10,000. At the current enacted property tax rates, these personal property tax accounts have minimal annual assessments.

In many instances, the cost to assess, collect and follow-up on these deminimis accounts can exceed the actual property tax assessment itself.

We recommend that the Town consider including an article at the next Town Meeting asking voters to exempt property up to \$10,000 from being taxed. There are over 100 communities currently employing this practice. It is important to note that the elimination of these assessments would not reduce the amount of total property tax assessments in any given tax year; the remaining property tax accounts would absorb these deminimis accounts, which will likely amount to an insignificant additional amount (pennies) to these tax payers, but will greatly increase efficiency within the Collector's Office.

Other Post-Employment Benefits

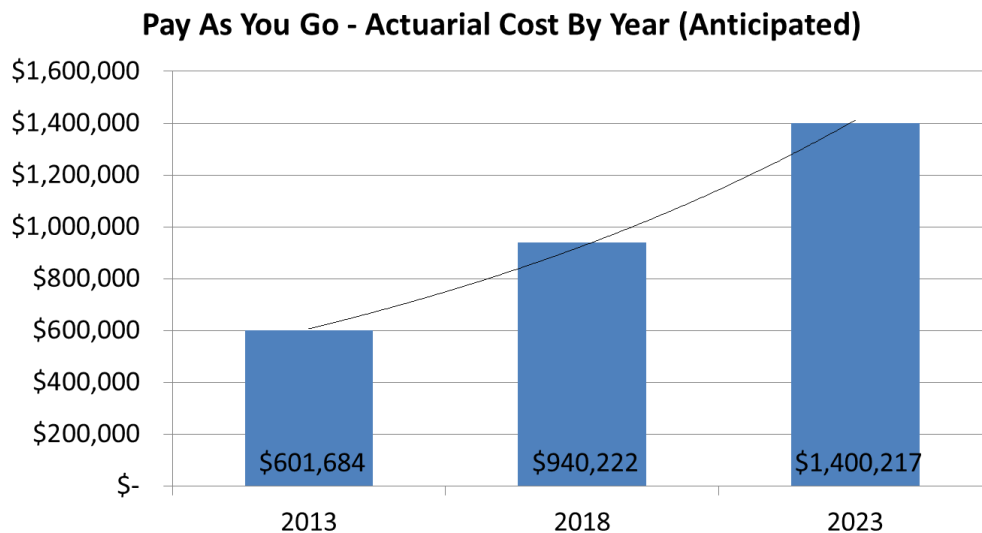
Governmental Accounting Standards Board ("GASB") No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefit Plans Other Than Pension Plans* ("GASB 45") requires communities to recognize in their financial statements a liability that recognizes postemployment benefits as this benefit is earned by employees.

The Town's most recent valuation reflected a future actuarial-estimated liability of approximately \$24.8 million. While this is a future liability, its impact to current operations

cannot be ignored. This is especially important in light of the average employment age for Winchendon employees, which is approaching fifty years old. This factor, among others, may make this an unmanageable liability in ten years (see chart below).

The credit evaluation bureaus have begun to assign an allocation of the credit evaluation to the management of long-term liabilities. OPEB qualifies as such an item. This is a reminder to management that as part of its long-term planning, the Town should begin to reflect the effects of OPEB into its plan. Other communities, although while still in the minority, are becoming more pro-active in this regard.

On a positive note, it is important to disclose that the Town has elected an OPEB trust under MGL c.32B s.20. The next step is to think about funding to this Trust. While this can be a daunting endeavor for a town like Winchendon that finds itself with significant economic impasses, we would highly encourage the Town, as it reshapes its budgetary processes and priorities that will likely ultimately be in place over the next few years, to not quickly dismiss the opportunity to establish some level of consistent funding into the Trust as part of that process so that a new budget model will acknowledge the importance of establishing a mechanism for funding these very real employee benefit costs. The Town does not have to look to meet 100% of the actuarial suggested annual funding, but to more importantly demonstrate to impacted parties and other interested outside parties that the Town has a responsible plan in place and that such a plan is followed through on. *We understand that with the many financial challenges the Town is currently facing, that this would not be a priority item until the financial house is more in order.*



Municipal Data Breaches

Within the past few years, there has been an alarming increase in the number of intrusions into municipal networks throughout the United States. These breaches, many of which targeted relatively small towns, have resulted in the unauthorized access of resident, student and employee data and the theft of several hundred thousand dollars. Given that most cities and towns lack a structured information security program their systems are increasingly at risk to this type of event. And while not a municipality, the most recent data security breach at a major retail store chain in recent months has at the very least once again brought to the

forefront the extent to which hackers can and will go, and that even entities that are aware of their exposure risk may be unable to fully prevent the loss of data in such attacks.

Recently, a select number of highly qualified companies have emerged that conduct “Data Security Audits” for municipal entities. The audit is a comprehensive examination of the administrative, technical and physical security controls that a municipality has implemented to protect personal information. The resulting audit report identifies each condition that exposes the municipality to potential unauthorized access and offers practical recommendations to remediate these conditions.

III. MATERIAL WEAKNESSES

Budget Management

General Operating Budget

The Town's budgeting process is one of the most significant functions of internal control. Not only does it provide the cornerstone for the Town's strategic direction, but it is the guideline for departments and their managers to maintain their operations within. These budgets are legally adopted, and subject to Massachusetts General Laws (MGL). Any violation of these mandates could lead to severe consequences, the minimum of which is the requirement to raise any deficits with the subsequent year tax rate. This could have a serious impact on the subsequent year budget.

The following General Fund appropriation deficits existed as of June 30, 2013:

<u>Department</u>	<u>Amount</u>
Treasurer	\$ (15,581)
Town Clerk	(2,390)
Registrar of Voters	(5,591)
Police Department	(60,351)
Highway Department	(13,097)
Snow & Ice Removal	(158,721)
Tree Trimming	(1,915)
Veterans Service	(52,849)
Debt Service Interest	(10,139)
Workers' Compensation	(3,268)
Health Insurance	(122,847)
Medicare	(7,128)
School Budget	(869)
	<u>\$ (454,746)</u>

Only \$246,090 of the amount listed above was properly reported to the Department of Revenue (DOR) during the tax rate setting process for fiscal year 2014. (This was due to the accounting records not being closed timely and not due to willful intent). Thus these amounts were not legally raised.

This is not the first time this has occurred; during 2012, a very similar, although not as severe situation occurred, but those deficits were cured through year-end transfers. In addition, the current Town Accountant has made us aware that this occurred in fiscal year 2014 as well, and the line item deficits are much more severe, and, like fiscal 2013 were not cured before year-end.

This accumulation of deficits, when combined with deficits in other areas, such as the Health Insurance Trust, Circuit Breaker, and Transfer Station discussed later in detail, will have a material adverse impact on the fiscal year 2015 tax rate and could force the Town to make significant budget cuts, as well as, liquidate all current reserves. In addition, the expenditure budgeting estimation process used to establish the budget for Town Meeting this past May

needs to be evaluated since the existence of deficits for three straight years calls into question whether the 2015 expenditures have been properly projected.

While it is expected that deficits in the snow and ice account are unavoidable due to unpredictable seasonal weather conditions, it is unacceptable and contrary to MGL to incur deficits in other appropriation line items. In light of the fact that this has occurred three straight years and has gotten worse each year, it points to a severe structural deficiency in the budget monitoring process, both at the department level and within the financial offices.

This is evident through the observation of an inordinate number of manual adjusting journal entries that are noted within the general ledger. Such adjustments are usually a sign of:

- A misunderstanding of the budget organization,
- Expenditure invoices are not being accurately assigned the correct, initial general ledger account number by departments for the Town Accountant to process the bill to.
- Transactions are not being properly entered into the system by the Treasurer and Accounting Offices at time of input, and/or
- The system's automated entries are not properly or accurately setup.

We suggest that an evaluation of the budget process be conducted to ascertain the true cost of operations and to appropriate budget amounts that are necessary to sustain operations at desired or statutorily responsible levels; if those levels cannot be afforded, then the Town will have little choice but to make budget cuts that will have to be adhered to. There are some instances within the deficits above that demonstrate the Town cannot necessarily force operations to remain with a budget of convenience, if such a budget is truly insufficient.

With no available free cash and the Town's present and subsequent budgets resulting effectively in structural deficits, the options to correct this recurring and potentially devastating situation are limited:

- Appropriate from Stabilization.
- Budget cuts.
- Proposition 2 ½ override to bring taxation levels up to meet the sustainable level of services.

Health Insurance Budget

A more in-depth discussion of the Health Insurance Trust Fund occurs later in this report; however, we observed that increasing health insurance claims were significantly in excess of expectations. Since there was no increase in rates, a closer approximation to set sufficient matching contributions would have been expected from the budgeting process. Of greater concern, is the fact that the Health Insurance Trust Fund is significantly being underfunded on an annual basis (particularly in 2013 and 2014), and if the Town intends on keeping a self-insurance health plan, the Town will likely have to increase the budgeted contributions significantly above the present actual amounts in order for the fund to maintain solvency.

Education Budget

Based on a review of the School Department's End of Year Financial Report and as represented to us by Town personnel, for the last couple of years, the ESE has determined that the overall spending required for qualifying education activities has not met the threshold

statutorily required under the Commonwealth's net school spending formula. It is our understanding that Town and School officials have met with the ESE about this recurring situation; furthermore, we understand that the Town personnel may be in disagreement with the conclusions reached by the ESE. However, the net school spending formula is applied to all school districts throughout the state and the formula as established and maintained by the ESE is the only official determining factor in concluding compliance. There have been different individuals at the School Department charged with completing the End of Year Financial Report over the last five years and therefore, consistency in the annual compilation of the report has been lacking based on our findings. In particular, the fiscal year 2013 report reflected numerous categorical and total errors in the transition of the amounts calculated by the School and Town into the report; and these errors may likely have significant impacts to the net school spending calculation. While the Town does maintain some rather unique methods of accounting and budgeting for net school spending, the process itself does not appear to be flawed relative to achieving accurate reporting results; however, the unique methods are challenging and make some aspects more difficult and time consuming than in other communities. No matter what methods are employed, the most imperative issue is that the status of not meeting net school spending be corrected – either through amendments to previously filed reports if errors have been identified subsequently, changes to the indirect cost methodology between the Town and School to reflect more accurate amounts, or changes to the overall school budgeting process to ensure compliance. What should be noted is that the net school spending formula is extremely difficult to follow and cannot be easily interpreted; therefore, any evaluation process of how the Town and School will meet net school spending should involve an expert in this area of financial reporting so as to ensure that once corrected, the new budgeting process will allow for future compliance.

Water Enterprise Budget

As a final note, while not within the General Fund operations, it is our understanding that for fiscal year 2014, the Water Enterprise Fund is expected to meet its fiscal operational needs through the use of nearly all of its accumulated retained earnings. This can be a high risk decision by the Town, since similar to stabilization funds, retained earnings are one time sources and typically one time sources should not be used for operations. In addition, surplus reserves won't be available for unforeseen events.

Accounts Receivable Reconciliation Process (Material Weakness)

The Treasurer/Collector was not able to produce a receivable report out of the MUNIS collections module for the water and sewer user charge balances owed as of June 30, 2013. Accordingly, the Town was unable to validate that the water and sewer receivable balances as shown on the general ledger agreed to a detailed sub-ledger of customers. The amounts unable to be audited were \$355,573 and \$414,798 for water and sewer charges, respectively.

The following is what we determined as the cause for this issue:

- The MUNIS collections module operates as a perpetually updating system and does not have a “look back” option whereby once new billings or collections are entered into the system, it is impossible to obtain reports showing amounts before those transactions were entered. Accordingly, as these reports were not run on July 1, 2013 once all of the June 2013 transactions were entered, the option to obtain balances through June 30, 2013 was permanently lost.

- Upon inquiry, when the Town moved to the MUNIS system for water and sewer receivables collections a few years ago, apparently the past Town Accountant was the only person who knew how to run the receivable reports (and who knew of the inability to obtain receivables balances retroactively from the system), so they would run the receivable reports on-behalf of the Treasurer/Collector Office. It would appear that the Treasurer/Collector Office personnel were never trained in how to run their own reports in MUNIS. Not only is this inefficient, but it compromises segregation of duties between the two departments.

We would note that the issues surrounding obtaining the reports on a timely basis from within the Treasurer/Collector's Office should be corrected in time for fiscal year 2014 year end reporting and reconciliation. Additionally, while we were not able to reconcile the two receivable amounts noted above, there are true receivable amounts for water and sewer services that were due on June 30, 2013 and it would be incorrect to interpret that those amounts are completely in error. However, we could not verify whether or not those amounts are significantly accurate as reported within the fiscal year 2013 financial statements.

IV. FINDINGS AND RECOMMENDATIONS: GENERAL OPERATIONS

Health Insurance Trust Fund

The Town's self-insured health program had a devastating fiscal year for 2013. Below, we will attempt to highlight the major impacts, events, and status concerns that resulted at the conclusion of our audit for fiscal year 2013 within the Health Insurance Trust Fund (the Trust). As the audit was unable to be completed until the end of fiscal year 2014 for reasons previously addressed, it is imperative that management understand that some of what is being discussed below is nearly a year old and that discussions with management relative to perceived fiscal year 2014 activities within the fund did nothing to improve the stability of the Trust and that the condition of the Trust will likely be more severe than that described below once the general ledger is closed for fiscal year 2014.

Deficit Fund Balance

The Trust ended fiscal year 2013 with a fund balance deficit of \$745,344. This was the result of recognizing a loss of over \$1 million from current year operations. Recorded expenses were nearly \$4.7 million up from the previous year by over \$1.0 million while revenues remained constant at about \$3.6 million. The Town's practice in fiscal year 2013 of recording warrants payable at year-end rather than factoring this through a higher IBNR liability contributed to this increase in expenses (see below).

At June 30, 2010, the Trust had a fund balance surplus of \$939,753. Since then, the Trust has posted annual losses of \$495,799; \$124,532; and \$1,146,363 over the last three years. Accordingly, the trend demonstrates that the contribution rate calculations have not kept pace with the ever increasing costs of providing health care.

Posting and Timing Issues

Journal Entries

A notable number of additional journal entries within the general ledger moving insurance contribution amounts into the Trust, particular at the beginning and end of the fiscal year were noted because the timing of contributions relative to payroll periods can be challenging. When there are multiple journal entries crossing and overlapping amongst each other in such a fashion, it can be difficult to follow the reasoning and purpose of each one. This was made additionally burdensome because of the loss of the previous Town Accountant's institutional knowledge relative to these previous postings. We noted that there were two journal entries posted in error into the Trust during the year which totaled about \$114,000. The impact of correcting these entries resulted in lowering contribution revenues and simultaneously the fund balance for fiscal year 2013; this was not identified until late into the next year. We went over these with the Town Accountant and believe that it will be possible to reduce the number of journal entries for fiscal year 2014. This should help preclude such posting errors to occur in the future.

IBNR Calculation and Reporting

Over the past few years, the Town's ability to obtain a reasonably accurate amount for reporting its Incurred But Not Reported (IBNR) claims liability at year-end has proven challenging which has led to some confusion and irregularity year to year. Generally, we as

auditors have the benefit of more time passing from the end of the year until we perform our fieldwork, than the Town Accountant has since the Balance Sheet is submitted to DOR with an IBNR calculated amount that usually involves a shorter period of time in which to evaluate this liability. With the Trust presently in a deficit position, it is imperative that the IBNR amount reported to the DOR be as accurate as possible, so as to reflect the most correct fund balance surplus or deficit. A variance of \$100,000 in the calculation (which has been noted in previous years between the DOR report and the audit report) could make a significant difference as to what impact the Trust may have on the Tax Recap. We are pleased to report that with the Town now having direct access to the raw claims data at Blue Cross Blue Shield, the necessary reports can be efficiently obtained from them, and we will be showing the Town Accountant how to utilize these reports to calculate the most accurate IBNR liability possible moving forward. We would note that with improvements to billing systems, the IBNR for fiscal year 2013 was over 87% recorded by August 31st, so the Town should be able to calculate a materially accurate IBNR annual in time for reporting its Balance Sheet to DOR on a timely basis in future years.

Accounts Payable

The Town's IBNR has historically been calculated at \$350,000 - \$450,000, which always appeared conservative based on a rate that should approximate 8.2% of claims or most likely below \$200,000 based on the level of prior years' claims. However, in those years, the Town did not record a warrants payable so the thought process was that the insurance administrator was offsetting the lack of recording warrants payable by inflating the IBNR. In addition, the Town never recorded a stop loss receivable amount so at the prior year much lower claim levels, the activity appeared materially stated.

With the increase in claim balances in fiscal 2013, and the appointment of a new insurance administrator, it became increasingly important to record warrants payable and a more accurate IBNR as discussed above. Therefore, expenses for fiscal year 2013 were increased as a result in a change in accounting and reporting methods by the new Town Accountant to reflect this methodology. We concur with this change in methodology, and while it effectively resulted in more than 12 months of claims activity being recognized in fiscal year 2013, we do believe it provides for a more accurate year-end reporting on the financial status of the Trust.

Recalculation of Working Deposit

Presently, the Town maintains a working deposit of \$499,000; this deposit is set by Blue Cross Blue Shield. Historically, this amount has been based on claim costs over a period of time. With the claims for fiscal year 2013 and apparently 2014 having risen dramatically, Blue Cross Blue Shield has determined that this working deposit is no longer satisfactory and has exercised its option to increase the deposit at least \$50,000 for fiscal year 2015. This places an additional financial and cash liquidity burden on the Town as this deposit represents monetary resources that it presently does not have earmarked for such use, and is in fact a pre-payment before having been billed for the services.

Lack of an Insurance Administrator/Consultant

In the first half of fiscal year 2014, the Town concluded its relationship with its insurance administrator/consultant. Since that time, the Town has solely relied on Blue Cross Blue Shield, its claims processing agent, to provide it with insurance claim data and administrative

guidance as requested. However, their duties as a claims processing agent is a vastly diminished service over what an insurance administrator/consultant can offer the Town for guidance relative to insurance plan evaluations, contribution rate calculations, long-term budgetary planning and analysis assistance, compliance with new and changing Affordable Care Act mandates, and act as professional representation of the Town on insurance matters. While there is a cost for these services which the Trust has borne in the past; we would highly suggest that given the present financial state of the Trust, there is likely a positive cost benefit result to re-acquiring a replacement insurance administrator/consultant if the Town's self-insured health program continues much longer. If the Town decides to eliminate its self-insured health program, we would highly suggest that a knowledgeable consultant in this area be engaged to assist in efficiently closing down the program and transitioning the Town to a premium based plan.

Stop Loss Management

Stop loss insurance is in place to cover health insurance claims by individuals when such claims accumulate to exceed \$70,000; this effectively limits the Town's overall exposure to large and unpredicted claims costs. During our discussion with Town representatives, it was noted that claims costs have been rising over the last couple of years which they had anticipated through their personal knowledge of various health issues faced by some of the Town employees. Some of these health issues have incurred significant claims costs for which stop loss insurance was activated. The past insurance consultant had been actively participating in the process to manage stop loss claims; with the ending of their services, this responsibility moved to Blue Cross Blue Shield, the claims agent in fiscal year 2014. There are certain timing aspects relative to the recognition of claims costs versus receipt of stop loss reimbursements; however, our analysis indicates that stop loss reimbursements were down from fiscal year 2012 to fiscal year 2013 by almost \$50,000 (16%); however, during that same period of time claims costs rose significantly. As part of our audit procedures for fiscal year 2013, we made inquiries regarding stop loss activities in fiscal year 2014, and it appears that in early fiscal year 2014 stop loss reimbursements (which would be reimbursements of fiscal year 2013 claims) were less than anticipated based on the increase in claims.. Analytically, this is not the expected result; therefore, we suggest that the Town request a review of the stop loss activity by an insurance professional to determine if any qualifying claims may not have been overlooked or possibly are pending with the stop loss insurance provider. To further complicate the process, in mid-fiscal year 2014, the stop loss reimbursement process was changed from actual receipts of reimbursement checks, to "netting" down of monthly claims costs within the invoices. While neither process is inherently flawed, it does make an analytical evaluation of the stop loss process more difficult to apply and evaluate. Additionally, it is difficult to ascertain what if any impact the rather quick transition from the past insurance administrator/consultant to the insurance claims agent may have had on the continuity of information and claim statuses on this process. While our audit did not identify any specific errors in this stop loss process; this comment is a result of actual activity not meeting anticipated results.

Increase in Contribution Rates

It is our understanding that the employee and employer contribution rates remained the same for fiscal year 2014 as in the past few years. However, the Town is increasing the contribution rate for fiscal year 2015 by 4%. While we applaud the Town taking steps to modify the contribution rates, we would point out that the average annual claim costs for the last few years has been exceeding 4%, combined with the fact that the Town is already within

a structural contribution deficit position, it is more than likely that the 4% increase will not suffice in maintaining a balance of revenue versus expense, or generate a reserve surplus within the Trust to mitigate unexpected and significant claim costs.

Ability to Absorb Unpredictable Costs

As noted throughout this letter, the Town is facing some significant financial decisions as it looks to re-establish a budget methodology that precludes deficit spending within the General Fund appropriation lines. The Town's health insurance contributions expenditure budget line is one of those lines noted as being in deficit. The Town has maintained its status as a self-insured health employer for many years; but, most municipalities within Massachusetts are not self-insured but are on a premium based health insurance program. In the past, self-insured plans provided communities with both the control and flexibility over health insurance they desired and in the right situations saved in overall health insurance costs. However, there has been a noticeable trend over the last dozen years as health costs for doctor visits, prescriptions, and hospital/surgical services have spiked upwards at a non-stop pace. Some communities are finding that the risk reward of maintaining a self-insured health program no longer exists and is not financially prudent for them. Many of the communities that are presently successful in maintaining their self-insurance programs do so as a result of having significant free cash resources available to them to mitigate the unexpected high costs or have a much larger employee pool over which to disseminate the costs and smooth out the claim impacts. Winchendon presently finds itself in neither of those situations; and in fact based on the financial results over the last few years both within the Trust account and the overall Town financial health, it would be prudent by management to evaluate whether or not a self-insurance program remains the best option for the Town moving forward, or whether a pooled group plan such as the State's Group Insurance Commission (GIC) or other regional municipal group would be more workable and budget friendly. In performing this evaluation, the challenge for the Town will be to ascertain what the reasonably true future, annual employer contribution costs (General Fund health insurance budget appropriation) are under the current situation. Based on most recent data, and as previously noted, the present annual contribution in actual dollars would appear insufficient to maintain the self-insurance program and the fiscal year 2015 increase of 4% to the contribution budget line is more than likely not going to be sufficient to keep the Trust out of deficit in the future. Whatever the decision, it will take many years of future activity to determine which decision was the correct one; however, given the present budget crunch impacted by the Town's economy, the predictableness and consistency of a premium based plan may be of great value in the future planning and management of the Town's annual budget.

Cash

Reconciliation Processes

The timely, complete, and accurate reconciliation of cash between the bank statements, Treasurer's cashbook, and Accountant's general ledger is probably the most important part of maintaining a reliable and valid set of financial records and is the biggest deterrent to preventing or detecting fraudulent acts relative to Town funds. We observed that while the Treasurer was able to reconcile their cashbook balance to the bank statements on a monthly basis throughout 2013 and continued to do so in fiscal year 2014, the reconciliation between the Treasurer and Town Accountant was not performed timely. This was a result of management turnover and the substantial challenges in closing and adjusting the MUNIS general ledger for fiscal year 2013 (which are detailed throughout this letter). As a result of

the fiscal year 2013 challenges preventing the accounting records from being closed until March 2014, this had the result of impeding this same phase of the cash reconciliation process for fiscal year 2014 activity.

We want to specifically note, that the fiscal year 2013 audit did not identify errors in the cash reconciliations provided by the Treasurer and Accountant; and therefore this comment should not be interpreted or assumed that cash balance variances exist. We are presenting this item relative to the timeliness of the reconciliation process and to bring awareness to management that sufficient resources should be provided so as to allow for the Treasurer and Accountant to catch up in their reconciliation process, which we would reasonably suggest, should be performed on a quarterly basis.

Fair Value Reporting

GASB 31 which became effective for fiscal year 1998 required that cash and investments be reported within financial statements at their fair values (which are more generally referred to and in-line with market values); historically this was recorded as part of the annual audit adjustments for GASB reporting purposes only. However, within the last few years, the Massachusetts Department of Revenue revised its policy on investment reporting and as delineated in their Year End Letter to Accountants, required the reporting of such amounts at fair value; thereby making it a requirement under UMAS reporting that the Town follows.

Presently, the Town records their investments at an amount that does not represent the fair value; the difference for fiscal year 2013 was not material and did not require audit adjustment. However, we would encourage the Town to implement a policy to record its investments at fair value by June 30, 2014.

Tax Collection Process

Financial policies need to be developed with respect to the collection of real estate tax bills once committed. Cash flow is critical to the viability of any community and especially funds collected prior to June 30, as these would impact the free cash calculation.

It is clear that the Town does not have such a policy, and if it does, it is not being followed consistently. It is important that the new Collector endeavor to create a very strict policy using the guidelines described below:

The following balances were outstanding at June 30, 2013:

	Real Estate	Personal Property	Total
2006	\$ -	\$ 77	\$ 77
2007	662	69	730
2008	2,239	90	2,330
2009	44,971	1,285	46,255
2010	75,273	2,054	77,327
2011	153,643	2,252	155,895
2012	220,541	2,826	223,367
2013	491,088	4,002	495,090
	<u>\$ 988,417</u>	<u>\$ 12,656</u>	<u>\$ 1,001,072</u>

In addition, the Town has \$1,178,799 in outstanding Tax Title and \$288,077 in Tax Foreclosure. All told the Town had almost \$2.5 million in outstanding receivable balances as of June 30, 2013. The statute of limitations with respect to a Town being able to secure its position through the recording of a lien with the Registry of Deeds on outstanding real estate is 42 months subsequent to the end of the levy year. As a result, the Town has lost its ability to secure a tax title on any of the 2010 and prior outstanding balances listed above, and the 2011 statutory deadline is quickly approaching.

A solid collection policy includes all legally acceptable means of collecting taxes in the most expedient manner possible. This would include (1) the use of a quarterly billing system, which the Town uses; (2) the use of a lock box to expedite cash flow and recording which the Town uses; (3) the use of demand letters at their earliest possible time. In the instance of a quarterly billing community, a courtesy two week period should be allowed after the due date, so for example, bills due on May 1 should be demanded May 15 to assure collections are maximized for June 30. (4) Amounts not paid within the 30 day demand period should be committed to tax title immediately. (5) Once in tax title, the Town should use foreclosure and auction means to further expedite the collection process.

An effective policy has many positive and collateral impacts. (1) Cash flow is increased, (2) revenues are increased, (3) free cash is positively impacted, (4) receivable balances are reduced, requiring the Town to maintain less in its overlay accounts, and (5) the excess overlay balances may be transferred to a general stabilization account thereby increasing the Town's reserves.

Similarly, the Town should send demand letters on Motor Vehicle Excise as soon as it is legally permissible to do so. The Town currently has \$269,000 in outstanding Motor Vehicle Excise.

Per discussion with the new Treasurer/Collector, the last year that the Town performed a tax title taking to lien properties for real estate taxes was for levy year 2010 during fiscal year 2011 (except for properties already in tax title for a previous year which were automatically moved to tax title as allowed by law). The tax taking process is one of the most powerful tools the Town has to enforce collection against delinquent taxpayers and to best preserve the Town's right to collect those taxes in the future. While some of the 2013 taxes were collected in fiscal year 2014, it is likely that their balance remained as high as or higher than the 2012 balance.

It was represented to us that the Treasurer's Office has not received a budget line appropriation for the last few years with which to fund the tax taking process; accordingly, even if management personnel were so motivated to perform this process they would have been precluded from doing so without any money to pay the costs associated with the advertisement of and lien filings. We would encourage the Town to identify a funding source for the Treasurer/Collector and revise their budget to allow this process to occur. Even if the process were to cost \$20,000 it would very likely generate at least ten times that amount in revenue given the large amounts owed as delineated above and the costs are billable to the delinquent. Additionally, it would likely have an impact on the more timely collection of current year taxes and Town cash flow if property owners became aware that the Town fully intended to aggressively pursue delinquent taxpayers as a new philosophy.

Another option that many municipalities are now pursuing is the selling, or assigning, of tax titles under Massachusetts General Law Chapter 60, Sections 2C and 52. Under this MGL,

the Town is essentially transferring its interest to a private entity through an auction or bid process. The law gives the Town the flexibility to assign or keep whichever tax title accounts it chooses and may assign single tax titles or groups of tax titles. Assigning tax title accounts gives the Town the ability to immediately recover the taxes owed, avoid the cost and delay of collections and foreclosure actions and increase its property tax collection rates. We would also recommend the Town consider this tool for managing tax title collections and highly encourage Town financial management to contact other towns that have sold tax titles as part of this process.

Ambulance Receivable Monitoring and Write-Off Policy

The Town uses a well-established, third-party billing company to administer the general ambulance billing and collection duties so we believe it is sound. We also acknowledge that year-to-year, the total ambulance receivables remained very consistent at approximately \$375,000; however, from fiscal 2012 to fiscal 2013, the percentage of significantly delinquent accounts (greater than 180 days in arrears) increased from about 45% to over 60% of the receivable balance. We suggest the Town review its policies and practices for collecting delinquent amounts in order to ascertain if procedures can be changed to encourage more timely collection; and furthermore, to develop a write-off policy that should be approved by the Board of Selectmen for delinquent accounts.

Liabilities

Accrued Payroll

The Town is not properly budgeting and charging payroll in accordance with required DOR guidelines which states that a payroll period that crosses between fiscal years is to be allocated to the applicable fiscal years in which it is earned. Accordingly, either a split payroll warrant should be utilized (which MUNIS can do automatically) for the first payroll warrant of the subsequent fiscal year, or the Town should manually calculate an accrued payroll liability and book the amount to the applicable expenditure and liability accounts. Presently, the Town is posting the payroll expenditures on a cash basis, based on the day paid. The Town pays wages bi-weekly, and as of June 30, 2013, there was about one week of that two week period ended July 6, 2013, that should have been allocated against budgeted payroll for fiscal year 2013. It is our understanding that the Town intends to correct this for their June 30, 2014, reporting; however, given that the Town did not budget in fiscal year 2014 for the value of the accrued wages (which will be 9 days of the payroll period), many payroll budget lines should be expected to go into deficit within the General Fund.

Agency Accounts

The following were noted relative to liability account balances maintained by the Town on-behalf of other parties within the general ledger:

- The Town's Balance Sheet provided during the audit reported a health insurance withholding deficit of \$96,578; however, during the audit, it was discovered that an amount equal to \$86,757 was incorrectly transferred from this account to the Health Insurance Trust during fiscal year 2013. An audit entry was made reversing this double posting; yet, there is still a \$9,821 deficit remaining thereafter. Further review of the withholding account balances indicate that there are other smaller deficits and surpluses (some within accounts that no longer appear used by the Town), which the Town

Accountant should research and adjust as necessary. Any remaining deficits at the conclusion of that project will likely require the Town to fund through the tax rate.

- None of the \$17,800 beginning balance in the Fire Arm License account that was due to the Commonwealth was paid out in fiscal year 2013; furthermore, none of the fiscal year 2013 collections were paid either. Therefore, at June 30, 2013, there is \$38,075 owed to the Commonwealth.
- The Police Details account continues to maintain a deficit balance (\$14,865 at June 30, 2013); this is not uncommon as certain regulations require the payment of those monies to officers in advance of collection from the serviced parties. Many communities to do not record this offsetting receivable; however, we would highly suggest the Police Department be required to provide sufficient receivable records detailing to the Town Accountant on a monthly basis that the deficit is equally offset or exceeded by amounts owed.
- A performance bond account has maintained a deficit balance of \$2,850 over multiple years; this should not be possible, as these are deposits which when returned should never exceed the account balance. We suggest the Town Accountant reconcile performance bond deposits with the departments who oversee the activities relative thereto.
- FD Special Agency account was put into a deficit position of \$1,300 in fiscal year 2013.

Compensated Absences Calculation Procedures

Both the Town and School did not have a well-documented procedures or calculation schedules readily in place with which to efficiently determine and calculate the dollar value of the compensated absence accounting liability for unused sick and vacation time as of June 30, 2013. Previous documents and institutional knowledge of the processes were lost in the transition of the Town Accountant and School Payroll Clerk personnel. While the information was ultimately compiled by Town and School personnel for fiscal year 2013, we would strongly suggest that more formal and documented processes be developed and implemented for annual financial statement reporting purposes that also ensures that Town and School policies and union agreements which define vesting and accumulated time limits are fully incorporated within the year-end financial statement calculation schedules.

Indirect Cost Accounting

Water, sewer, and transfer station indirect costs are approved at Town Meeting and transfers are made into the General Fund on the general ledger; however, they are not reflected as transfers on the tax recap, but instead as revenues and expenses. The more proper accounting methodology is to show these as transfers between funds and not as revenues and expenses.

It is also suggested that every few years, a formal evaluation of the indirect cost calculations be performed so as to ascertain that the amounts being allocated as such are valid.

Fund Balance Deficits

The following deficits existed relative to fund balance accounts and activities external of those previously addressed with regards to General Fund and the Health Insurance Trust Fund. As a result of our audit procedures we would strongly encourage the Town to adopt strict policies preventing the expenditure of monies out of Special Revenue Funds when adequate funding is not presently available within the fund or guaranteed through the receipt of a grant award letter or in-hand donation.

- Circuit Breaker Special Revenue Fund – The School Department overspent the available grant funding by \$159,943. This grant is effectively for the purpose of supplementing the School Department’s General Fund appropriations for special education. Accordingly, if this transfer of expenditures had been made properly so as to not put the fund into deficit, the School Department would have had to leave these expenditures allocated to the budget, and the School Department’s General Fund deficit would have increased by \$159,943.
- CDBG 2010 Grant Special Revenue Fund – At June 30, 2013, this grant had been concluded and closed out, but the general ledger still maintained a deficit of \$26,898 with no further funding remaining. It is our understanding that the Town Accountant is researching the past history of the activity in the fund to determine if the deficit was incorrectly caused by a misposting. If the deficit is determined to be real, then the Town will have to identify a funding source to cure the deficit; if the deficit is related to CDBG activities, the Town will be able to fund it through the CDBG Program Income Fund.
- Chapter 90 Special Revenue Fund – Per review of the subsequent year reimbursements to the Town for Chapter 90 roadway improvement projects, it would appear that an approximate \$2,000 deficit exists within the fund for which reimbursements are not expected to be received.
- USDA Police Cruiser Special Revenue Fund – During fiscal year 2013, the Police Department purchased a vehicle which was partially charged to this general ledger account in an amount of \$15,226 thereby putting the account in deficit. Subsequent procedures performed on intergovernmental receipts did not indicate that funds had been timely received during fiscal year 2014. If the reimbursement was received in fiscal year 2014, we would encourage the Town to adopt a policy whereby departments are responsible for requesting and following through on receiving any reimbursement funds as quickly as possible after completing the purchase transaction. If the reimbursement is still not received, then the department should be tasked with investigating the status of their reimbursement; as if the funding is not ultimately received, local taxpayer funding will likely be necessary to eliminate the deficit.
- Urban Self-Help Grant Special Revenue Fund – This grant account has been in deficit by \$23,980 since at least fiscal year 2008. At this point, any grant funding has likely been lost as a result of the expiration of the grant award. The Town should investigate whether or not the funding of this grant was truly received in a previous fiscal year and potentially misposted; otherwise, it would appear that the Town should budget for the elimination of this deficit.
- Ambulance Donations Special Revenue Fund – This fund was overspent by \$31,535 during fiscal year 2013. The expenditure out of this fund was primarily used to fund a

portion of the purchase of a new ambulance during the year. As there are no guarantees that sufficient donations will be received in the future to eliminate a deficit within a donation account, the Town is not allowed to overspend a donation account. Accordingly, the Town should evaluate where the deficit in this fund presently stands and should budget for the elimination of this deficit or find another presently available funding source.

- Other Special Revenue Funds – A few other insignificant deficits existed within the Special Revenue Funds at June 30, 2013. We suggest that the Town investigate whether these deficits continue to exist and take the proper action to correct those that may exist as a result of previous year mispostings or transfer available funds to eliminate them.
- Library Gift Trust Fund – This trust account was expended down to a deficit of \$19,328. Since there is no remaining corpus upon which to eliminate the deficit or earn investment income to cover the deficit, it appears the Town should investigate whether some of the expenditures posted to this fund that caused the deficit can be transferred to other library trust funds that have available monies.
- Wheeler Poor Trust Fund – This trust account was put into deficit by \$4,652 during fiscal year 2013. Our audit procedures discovered that it was in deficit because Town Meeting had voted transfers out of the Wheeler Poor Trust and Cemetery Trust of \$2,000 and \$8,000 respectively and into the General Fund. However, when these journal entries were recorded to transfer the monies, the amounts were transposed between the two trust funds and the Wheeler Poor Trust was decreased by \$8,000; thereby causing the deficit. This can be easily corrected through a journal entry on the general ledger transferring \$6,000 from the Cemetery Trust to the Wheeler Poor Trust. In addition, the Treasurer should be notified of this correction so that they may also physically move this amount between the two trust funds' segregated bank accounts – if the banking transfer was also originally recorded incorrectly.
- Transfer Station Enterprise Fund – The Town increased the accumulated equity deficit by \$3,070 to a total of \$9,710 at June 30, 2013. This indicates that the transfer station is consistently not generating sufficient revenues to maintain its present operational levels.

Payroll Warrants

During the fiscal year 2013 audit, we modified some of our audit procedures regarding our review of the processing of payroll. As a result, we were able to specifically identify that significant differences exist between the actual amount of payroll wages being earned versus the amounts shown on the payroll warrant signed by the Town Accountant and Board of Selectmen. These differences totaled nearly \$3,000,000 for the year. Through our inquiries we were able to determine that these variances were caused by the “netting down” of the payroll warrant for certain employee withholdings that are held back by the Town in Agency accounts, which are at a later date included on a vendor warrant as a distribution to the applicable employee benefit providing parties. The payroll amounts due to employees appear to be processed correctly. This comment is isolated to the documents used to authorize the payroll expenditure.

We believe that the payroll warrant total that is signed and approved by Town Accountant and Board of Selectmen should be adjusted to equal the total wages being paid out plus only the employer portion share of Medicare. Whether the amounts are being withheld for future

distribution or paid directly to the employee, the Town is at the time of the processing of the payroll warrant, responsible to recognize the gross payroll amount as the expenditure; therefore, it is more accurate and proper for the Town to document the authorization of that gross payroll amount, effectively through the signing of the payroll warrant.

Information Technology – Electronic Accounting Systems

User Access and Permissions

Prior to the conclusion of the fiscal year 2013 audit in early 2014, the Town was made aware by MUNIS, their electronic general ledger system vendor, that certain changes to data relative to previously processed transactions were attempted to be made. Such changes ultimately proved as no consequence as internal controls and programmed checks within MUNIS alerted the Town Accountant to the changes and the changes were effectively canceled with what appears to have been no residual impact to the financial data and reporting integrity. Further investigation led to the discovery that a number of employees had been granted user permissions to access, enter, and potentially alter data in areas of the MUNIS system where their position within the Town as a whole would not justify such access. Additionally, it was also noted that previous employees' user accounts (some with high levels of access) still existed as active accounts on the MUNIS system; use by unauthorized individuals of these accounts may not only give them access to portions of the MUNIS system they might not otherwise have but could also provide for an effective method of hiding their true identity to the system.

This has in-turn brought to light for the Town a concern that it is looking to address in the immediate future, which is the potential need to review, validate, and re-establish user access and permissions within the MUNIS system for all employees. While no other actual incidents relative to the altering of system data other than what was originally identified appear to have been made, we cannot emphasize strongly enough that user access limits are properly set and established as a key to the prevention of fraud and reporting errors. Such unbridled accesses by those without need are textbook examples of actual fraud cases.

Once user accounts are validated and access permissions set, in order to maintain the integrity of the system, it will be imperative that the Town limit the ability to create or adjust MUNIS user accounts to very few trusted individuals. In the future, in addition to the establishment of new user accounts for newly hired employees, policies and procedures must be put in place so that those tasked with controlling user access must also be made aware at the time an employee is terminated or resigns so as to be able to efficiently and timely close out their access to the MUNIS system.

General Ledger System

Receipts Postings

The following two items were brought to our attention during the audit process:

- Presently, the Town Accountant uses the MUNIS system for the general ledger and the Treasurer/Collector uses the Point system for most of their collections processing. These two systems do not have a “bridge” to automatically/electronically share transaction data between them; accordingly, the same transaction data must be manually entered by the

Treasurer/Collector's Office personnel no less than 4 separate times. This impedes the timeliness, consistency, and accuracy of sharing data throughout the Town.

- The Treasurer/Collector's Office posts receipts transactions to the MUNIS general ledger system which are then later verified by the Town Accountant. It was identified by Town representatives that the MUNIS system has never been set up properly so that receipt postings can automatically be made to all necessary general ledger accounts during the entry process; some of the automated journal entry links are not completely programmed. Accordingly, even though the Treasurer/Collector's Office has been entering the receipts to assist in the general ledger posting process, the Town Accountant is forced to go into the system and make manual journals to fully and properly record receipt transactions as required under UMAS and GAAP accounting. Specifically, one of these manual journal entries is the actual recording of revenue; therefore, revenue reporting is not as efficient or timely as could be if the system was properly setup. A revision to the account linkages would not result in any additional input time by the Treasurer/Collector's Office once established in the system.

Closing to Fund Balances

The new Town Accountant brought to our attention that as presently setup, the MUNIS system cannot close equity within the Special Revenue, Capital Project, and Trust Fund accounts to the specific purpose fund balance accounts established within them. For example, the general ledger may have a Federal Grants Special Revenue Fund with 30 different grants being tracked within it. When the Town Accountant closes the year, the MUNIS system has been setup to close to only one fund balance account for all 30 grants combined; this results in having to manually calculate the amount to be closed out to each of the 30 grant accounts and then make a manual journal entry to distribute those amounts to each of the individual 30 grants' equity accounts from the one pooled fund balance account. This is highly inefficient, subject to error, and completely unnecessary if the MUNIS system were properly setup.

Evaluation of System Needs and Status

As has been noted in different portions of this letter, some of the more significant challenges being faced by the Town as it performs its financial processing and reporting functions revolves around issues with how the MUNIS system was setup many years ago. These situations are appearing more often with changes in personnel as they look to understand and streamline their operations, and are occurring at inconvenient times such as when the MUNIS software required upgrading in fiscal year 2014 and resulted in changed and incorrect data anomalies which required significant time for the new Town Accountant and a consultant to correct within the system before fiscal year 2013 could be properly closed and a balance sheet submitted to DOR.

Accordingly, we would suggest that the Town evaluate its electronic software systems and determine a course of action to be pursued within the coming year or two. If the Town wishes to stay with MUNIS (which is the most broadly implanted system for municipalities in Massachusetts but can be costly to maintain), then it should budget funds to perform a system re-build so that the financial modules can be properly setup and be more reliable for reporting without the need of correcting journal entries. However, this would also be the ideal time for the Town to evaluate the cost benefit of "fixing" the MUNIS system versus contracting with another reputable software vendor

that may also provide a suitable system for less cost as an option. Such decisions should be made involving the most involved users of the system; however, we strongly encourage that the cost of any such endeavors not be a deterrent to performing this evaluation, as there are many things about the present electronic system operations that are unnecessarily costing the Town in time and money – the Town is already losing time and resources at this moment by not acting on it.

Outsourcing of Payroll Processing

It was brought to our attention during the audit that the Town may be considering investigating a move from performing payroll processing in-house to outsourcing it to a vendor. Many Massachusetts municipalities process their payroll either way and ultimately the right and wrong method would appear to come down to preferences or operational efficiencies. If the Town were to decide to move forward with an evaluation of its options, the one thing that we would initially offer the Town given our experience with other communities who process payroll as a centralized function within one or two offices as Winchendon does, is the personnel needs whether processed in-house or outsourced rarely result in any notable salary or cost savings, since the need for a human to enter the data into either system exists for both. Therefore, cost benefit should rarely be a motivating factor in making a change.

V. FINDINGS AND RECOMMENDATIONS: SINGLE AUDIT

School Lunch – Free and Reduced Meal Applications

As a special test, the School Food Service Office is annually required to perform random verifications of approved free and reduced meal applications to ascertain the validity of reported household information on the applications.

The Food Service Office selected a sample of approved applications from which to require proof of family income. Three of the applications selected during the verification process were approved without documentation of all sources of income. Furthermore, the documentation for one application showed higher income than the original application, which should have changed that student's eligibility from free to reduced.

The Food Service Office lacked review procedures to ensure that eligibility requirements were determined properly and that all documentation from the verification of income was maintained. The Food Service Office should implement procedures to perform a detailed review of all eligibility determinations as part of the verification process and that documentation support all sources of income are maintained.

School Lunch – Employee Purchases

We determined that Food Service Department employees were purchasing items from vendors and reimbursing the Food Service Revolving Fund as payment. This activity is not appropriate as the revolving fund is only to be used for school related purchases. Furthermore, employees' are unfairly gaining access to favorable contract pricing and may be avoiding applicable sales taxes.

We recommend that the Food Service Department cease to allow employees to purchase items from School vendors and reimburse the revolving fund as payment.

School Lunch – Cash Reconciliations

Cash should be reconciled to supporting records to ensure federal, state and local funds are properly recorded and safeguarded.

We determined cash receipts are not reconciled to monthly reports from the Food Service Department's point of sale system for the Murdock Middle/High School.

Online payments, catering revenue and employee reimbursements for non-food service purchases are potential reconciling items between the point of sale system and the recorded cash receipts of the Town. The lack of formal cash reconciliation procedures does not properly safeguard the cash assets of the program.

We recommend that formal reconciliations between the point of sale system and the cash received by the Food Service Department be documented and maintained for all cash deposited with the Town Treasurer/Collector.

Special Education – Period of Eligibility

Grant funds must be obligated by the end of the grant period and liquidated within 90 days of the end of the period of availability.

We determined that disbursements were charged to the 2011 Special Education Cluster grant nearly one year after the end of the period of availability. Accordingly, the planned use of grant funds did not occur in a timely manner at the close of the grant, which caused the delayed payments of grant related invoices.

We recommend that grant administrators plan and adjust the timing of grant activities to ensure that grant funds will be fully liquidated within the period of availability.

Special Education – Time and Effort Certifications

OMB Circular A-87 requires all employees paid in full from federal grant funds to furnish semi-annual certifications that they have been engaged solely in activities supported by the grant. These certifications must be signed by the employee or supervisor with knowledge of the work performed. In addition, this OMB requires employers to document the portion of time worked on the grant and portion of time worked in areas not related to the grant, if not solely charged to the federal grant.

We discovered that only annual time and effort certifications were maintained. This caused an inability for federal grant program compliance to be verified. We recommend that the School implement procedures to ensure that the required certifications are completed semi-annually.

CDGB – Reconciliations

Allowable costs of federal and state grants should be separately identified, charged and reconciled to the Town's general ledger.

The grant administrators and the Town Accountant do not periodically reconcile grant activity and available balances.

Lack of periodic reconciliations of grant activity to the Town's general ledger may cause grant activity to be incorrectly posted and not identified and corrected in a timely manner. Furthermore, financial information submitted to the pass-through agency should be adequately supported by the financial records of the Town.

Formal monthly reconciliation procedures of grant activity should be implemented, with approvals from both the Town Accountant and the grant program administrator.