

CITY OF QUINCY, MASSACHUSETTS

MANAGEMENT LETTER

JUNE 30, 2014



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To the Honorable Mayor and City Council
City of Quincy, Massachusetts

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City for the year ended June 30, 2014 and issued our report thereon dated March 25, 2015. Our opinions on the financial statements and this report, insofar as they relate to the Quincy Contributory Retirement System, are based solely on the report of other auditors. In planning and performing our audit of the financial statements of the City of Quincy, Massachusetts (the City) as of and for the year ended June 30, 2014, in accordance with auditing standards generally accepted in the United States of America, we considered the City's internal 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 City's internal control. Accordingly, we do not express an opinion on the effectiveness of the City'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.

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 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. We do not consider any of the deficiencies noted to be a material weakness in internal control.

Our consideration of internal control was for the limited purposes described in the first paragraph and was not designed to identify all deficiencies in internal control that might be significant deficiencies or material weaknesses.

During our audit we became aware of other matters that are opportunities for strengthening internal controls and operating efficiency. The memorandum that accompanies this letter summarizes our comments and suggestions concerning those matters. The City's written responses to the comments have not been subjected to the auditing procedures applied in the audit of the financial statements and accordingly, express no opinion on them.

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

March 25, 2015

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Prior Year Comments Resolved

Please refer to the fiscal years 2012 through 2013 management letters for the full original wording of this comment as the content of this comment has changed over that time period.

PRIOR YEAR COMMENTS RESOLVED

MAJOR CAPITAL PROJECT ACCOUNTING

Comment

The City is currently involved with various stages of planning, design and construction activity relative to various major capital projects including infrastructure, downtown development, buildings, building improvements and similar projects. The projects can be funded from one to several different sources including federal, state, local, and private-public partnership levels. Each of these funding components has a need for multiple levels of financial reporting to granting authorities, oversight boards and committees and external users.

At any given time the City can have multiple capital projects, each of varying scope, duration and cost, occurring at the same time. The associated activity is reported within a variety of capital project funds maintained in MUNIS. We noted that different capital project funds were being used in a manner that that did not provide a clear accounting trail of the planning, design, or construction periods and the fund names did not match up with the original and intended purpose of the funds. This may have a negative effect on future external and internal financial reporting decisions.

The accounting currently used for some of these funds was not in accordance with the Uniform Massachusetts Accounting System (UMAS) or with generally accepted accounting practices because expenditures and revenues were netted. The netting of revenues and expenditures within the same account is prohibited by UMAS and with generally accepted accounting principles. Appropriate adjustments were made to the present the information accurately in the audited financial statements.

Management indicated that the netting occurred because formal project budgets have not been established in MUNIS. By not establishing project budgets the City is unable to process invoices through MUNIS; however, by posting the revenue to the expenditure account the City is able to override the MUNIS controls which then allows the City to pay bills associated with the project. This action is a further violation of UMAS and sound internal controls.

FY2014 Update

The City has researched the histories of the non-compliant capital project funds and determined the adjustments required to MUNIS to bring the past accounting into compliance.

MAINTAINING SUPPORT FOR YEAR END BALANCES

Comment

The City has procedures in place to reconcile the Collector's summary records to the general ledger at fiscal year-end; however, the City was unable to provide us with evidence that detailed records of the Collector's office was part of the reconciliation process.

Comparing summary records to detail records acts as a control to ensure that the Collections reporting system is working as designed. Additionally, the Collector's office is responsible for analyzing taxpayer and enterprise fund

user accounts to ensure that the City is exercising all efforts to ensure future account collections. We have been told that this analysis occurs however a centralized document to support this process does not exist.

FY2014 Update

The City has in place a mechanism to determine the reasonableness of account balances at a given point in time which then drives future account collection decisions.

TIMELINESS OF CHAPTER 90 GRANT REIMBURSEMENT REQUESTS

Comment

In 2013, we noted that the city processed roughly \$1.7 million of expenditures under the Chapter 90 program but did not receive any reimbursements from the Commonwealth because the program administrators for the City did not submit the paperwork on a timely basis to the Commonwealth. This created a cash deficit within the Chapter 90 fund in MUNIS.

A cash deficit in Chapter 90 may affect the free cash calculation that is certified by the DOR and used by the City to fund the subsequent year budget. In addition to the free cash effect, the City could face, in the future, the possibility of having to reimburse the Chapter 90 fund for any reimbursements denied by the Commonwealth because of untimely submittal of the reimbursement request. Should this situation occur, it would be up to the general fund to raise the deficit in the tax rate.

FY2014 Update

The City has changed its method of invoice processing and filing of reimbursement requests with Commonwealth in a manner that resulted in timelier reimbursements.

Other Matters Previously Presented

Please refer to the fiscal years 2008 through 2013 management letters for the full original wording of these comments as the content of the comments has changed over that time period.

INTERNAL CONTROL POLICIES AND PROCEDURES MANUAL

Previous Comment

This comment addresses the fact that the City does not maintain formal internal control policy and procedures manual documenting day-to-day processing and controls. By not having a formally document set of policies and procedures, the City is at risk of not being able to complete critical tasks due to an extended or unforeseen absence. The risks arise when a department head, other departmental employees, is required to train new departmental employees, or are required to learn “on the fly” critical department operations outside of an employee’s normal course of duties. This reduces the time available to spend on regular duties and also raises the risk of misstatement or error.

Recommendation

Key financial related departments need to develop a written internal control policy and procedures manual that includes proper reviews and approvals by management and is written in a manner that allows an employee the ability to complete the task by reviewing the manual. All department heads will need to be familiar with all policies and procedures within their office and be able to complete all necessary tasks in order to sufficiently train employees. The manual will also need to be reviewed on an ongoing basis to ensure its relevancy at any given point in time.

FY2014 Update

The Municipal Finance Office and Planning Departments have developed documents that are at varying stages of completion. During 2014, management was focused on developing a long term capital plan and debt management plans for internal and external uses. A by-product of this process is that some policies and procedures have been identified and incorporated into an overall policy and procedure manual.

We continue to recommend that management continue with the progress made to date with a renewed emphasis on documented those transactions and procedures that do not occur on a routine basis throughout the year.

Management’s Response

This product is a continually evolving document. While progress has been made in this area, the expectation is that a final product will be assembled at the same time as the fraud risk assessment process is completed or soon thereafter.

FRAUD RISK ASSESSMENT

Comment

The City needs to perform a risk assessment to identify, analyze and manage the risk of asset misappropriation and/or financial reporting manipulation. Risk assessment, including fraud risk assessment, is one element of internal control. The City's internal control should include performance of this assessment.

The fraud risk assessment can be informally documented and performed by a management-level individual who has extensive knowledge of the City that might be used in the assessment. In performing the assessment a management-level individual will conduct interviews and/or lead group discussions with personnel who have extensive knowledge of the City, its environment and its processes.

Some key questions to consider when conducting the self-assessment follow:

- What individuals have the opportunity to misappropriate assets or manipulate the financial statements?
- Are there any known pressures that would motivate employees with the opportunity to misappropriate assets or manipulate the financial statements? When making this assessment an employee's personal/social life should be considered.
- What assets of the City are susceptible to misappropriation?
- Are there any known internal control weaknesses that would allow misappropriation of assets to occur and remain undetected?
- How could assets be stolen? Assets can be stolen in many ways besides merely removing them from the premises. For example, cash can be stolen by writing checks to fictitious employees or vendors and cashing them for personal use.
- How could potential misappropriation of assets be concealed? Because many frauds create accounting anomalies, the perpetrator must hide the fraud by running through an adjustment to another account. Generally, fraud perpetrators may use accounts that are not closely monitored.

Recommendation

We recommend that management develop and implement a fraud risk assessment program to identify, analyze and manage the risk of asset misappropriation.

Status – Partially Resolved

Management has drafted and assembled the necessary questionnaires needed to develop the initial assessment; other matters however, consumed managements time during the 2014 period but a renewed effort will allow for final resolution of this process.

Management's Response

The Quincy Public Schools and the Superintendents Leadership Team plan on developing and implementing a fraud risk assessment program. This program will identify areas of potential risk and identify the personnel that may have an opportunity to misappropriate assets. A particular area of focus will include principal directed funds. A similar effort will occur for all non-School departments of the City.

SETTLING OF INTERDEPARTMENTAL CHARGES

Comment

In prior audits we made note of instances in which the City would settle interdepartmental charges through a check issued from a City bank account and made payable to the City. The method of settling interdepartmental charges is time consuming, prone to error and misstatement, and generally ineffective.

MUNIS is constructed in a manner that will allow for the settling of interdepartmental charges to be handled electronically on the ledger concurrently, and if necessary, with a wire or EFT transaction between bank accounts in the Treasurer's office.

Status – Unresolved

Recommendation

We recommend that the Treasurer's Office, the Director of Municipal Finance, the School Department and any other department that generates an interdepartmental chargebacks to investigate the most logical manner to effect the necessary changes in MUNIS in a manner that eliminates the need for a check to be written while recognizing the appropriate expenditure on the ledger.

Management's Response

The Quincy Public School plans on implementing a policy that will use interdepartmental chargebacks instead of issuing and/or requesting checks as settlement of charges. This will include charges relating to revolving funds.

STUDENT ACTIVITY FUNDS

Comment

Massachusetts General Laws allow for the Schools to maintain student activity funds but places certain requirements on how they are to be managed and accounted for. The School has only partially implemented the legal requirements as there has not been either an internal or external audit conducted and documented in accordance with the best practice guidance of the Massachusetts Association of School Business Officials.

Status - Unresolved

The matter remains unresolved. By not fully implementing the provisions the School is in violation of the law. From a practical standpoint, we have found that when these funds are subjected to the requirements of the law it is likely that funds are being held and spent on purposes outside the scope of the law. We have also found that many times the account detail, maintained by the principals, does not reconcile to the actual cash balances and/or the general ledger.

Recommendation

We continue to recommend that the School Department, comply with all provisions of the law, establish procedures on how each account is maintained, reconcile the detail accounts with the actual cash balances and provide the Auditor's Office with a full accounting of the activity and the reconciliations and obtain an external audit. When developing plan to comply with this comment, the City and School Department will need to work

cooperatively in a manner that is consistent with the Massachusetts Department of Elementary and Secondary Education's compliance manual that was published in the Summer of 2014.

Management's Response

The Business Office of the Quincy Public Schools has met principals of the schools to set up procedures necessary to comply with Chapter 71, Section 47. The process of implementing these accounts has also been discussed with the City Treasurer. Activity Agency Accounts are planned to be set up with the Treasurer's Office by June 30, 2015 and all deposits received after that date will go directly into the Agency Account.

The Superintendent is working with members of the Policy sub-committee to adopt a policy to accept Student Activity Funds as outlined under Chapter 71, Section 47. This policy would set maximum allowable balances, provide a standard policy and accounting manual, provide for periodic internal audit by the Business Office and provide for bonding insurance.

Additionally, the Agreed upon Procedures and Audit Guidelines issued by the Massachusetts Department of Elementary and Secondary Education will be adopted and followed for all Student Activity Accounts.

Current Year Comment

REVIEW OF PROCUREMENT POLICIES TO PREVENT SPLIT PURCHASE ORDERS

Comment

Our examination expenditures processed in fiscal year 2014 indicated that multiple invoices were paid to the same vendor during fiscal year 2014 for what appears to be the same service. The total amount paid to this one vendor totaled approximately \$30,000. In only one instance was a PO for \$9,999 processed and approved by the City prior to the City having received service from the vendor. For the remaining 11 purchases a purchase order was not requested or approved until after the vendor provided the service. Management has indicated to us that these 11 purchases were emergency related.

In those instances in which the vendor provided service without having obtained a purchase order, there were delays of between 6 weeks and two months from the time the City was invoiced for the work and up until the time the vendor was paid.

State procurement law has a very narrow definition of what constitutes an emergency procurement. Also, purchasing regulations and other publications issued by the State Inspector General's Office further discusses instances in which procurement law may be presumed to have been circumvented.

Recommendation

We recommend that management review current purchasing procedures to ensure that the City is using emergency procurement methods in a manner consistent with State law and regulations.

We also recommend that the City review all purchases, and to the extent that certain goods or services are not under contract, to determine whether or not it is feasible to bid out those services so that the vendors may be placed under contract.

Management's Response

While an employee is permitted to use "sound business practice" for purchases under the \$10,000.00 threshold; this can give cause to concern about trying to skirt the need for a contract and/ or bid. This is particularly true when a purchase order such as the aforementioned is entered more than once per fiscal year. The Purchasing Department will be more alert to any such purchases made in this fashion and we will consult with the departments entering them regarding the nature of the purchase. More specifically, we will find out if they will be in need of more of the particular material/ service in the future and is it something that should be bid.

Furthermore, with regards to purchase orders being entered after the work was completed; we have discussed this with department heads and have reiterated the legal requirement that purchase orders are entered and received prior to work being done. In an attempt to further clarify this point I have contacted the Inspector General's office in attempt to coordinate a class on procurement issues.

MANAGEMENT OF CAPITAL PROJECT ACCOUNTS

Comment

The City maintains a capital project fund relative to the construction of the new Central Middle School. At year end the fund had a deficit of \$2.34 million; however, the City had not borrowed either on a long term or short term basis before the end of fiscal year 2014. The failure to borrow timely may have had a negative effect on the City's free cash figure that was certified by DOR.

Recommendation

We recommend that management develop procedures that would require some sort of communication from construction project managers and relevant department heads to Municipal Finance that will provide the City's executive decision makers with proper basis for determining adequate levels of borrowing in order to avoid fund deficits at the end of the fiscal year.

Management's Response

The City will review the fiscal year closing procedures to determine any modifications that need to occur so that situations such as this are voided in the future.

REVIEW DORMANT BALANCES IN SPECIAL REVENUE AND CAPITAL PROJECT FUNDS

Comment

The City has various special revenue and capital project funds for which there has been minimal activity within the past several years. Capital project funds are usually funded by debt offerings that are tied to projects with costs that are reasonably known and quantifiable. Allowing unspent capital project funds to accumulate is not the most efficient use of the left over bond proceeds. Once the project the associated project is complete the fund should be closed out by obtaining a City Council authorization to use the left over funds to for another purpose.

Special revenue funds are usually created and funded through grant awards. Most grant awards that the City maintains are categorized as a reimbursable grant, that is, the City must expend its own funds first and then request and receive cash up the amount of the grant award. Most of the City's grant awards are reimbursable which means that the City must expend its own funds first prior to receiving any cash under the grant award. The fact that several of the Special Revenue grant funds maintain surpluses that have been stagnant suggests that City received a grant reimbursement that was posted to the correct fund while the related expenditure was posted to another fund. If this is truly the case, the City should be closing out the surpluses in the grant funds to the General Fund.

Recommendation

We recommend that the City analyze the dormant special revenue grant funds and capital project funds so that they can be closed out.

Management's Response

The Municipal Finance Office, the City Auditor, and the Mayor's Office, have completed a process in the spring of 2015 to utilize most, but not all, dormant capital project funds. This process will continue during the close of fiscal year 2015. The goal is to identify and close out all dormant funds by the fall of 2015.

Informational Comment

FUTURE GOVERNMENT ACCOUNTING STANDARDS BOARD (GASB) STATEMENTS FOR PENSIONS AND OPEB

Comment

The GASB has issued new pronouncements that will significantly affect the accounting and reporting requirements for Pensions and Other Postemployment Benefits (OPEB). These new standards will substantially impact your financial statements and will also affect the requirements for accumulating the necessary data to meet the reporting requirements.

The new standards that have been issued and their effective dates are as follows:

- The GASB issued Statement #67, *Financial Reporting for Pension Plans, an amendment of GASB Statement No. 25*, which is required to be implemented in fiscal year 2015.
- The GASB issued Statement #68, *Accounting and Financial Reporting for Pensions, an amendment of GASB Statement No. 27*, which is required to be implemented in fiscal year 2015.

The GASB is expected to issue additional standards following #67 & #68 for Pensions, which will similarly affect accounting and financial reporting for OPEB Plans. The GASB is encouraging earlier application of these standards.

To briefly summarize these new standards –

- GASB #67 and #68 will substantially change the reporting for pension liabilities and expenses. Changes in pension liability will be immediately recognized as pension expense or reported as deferred outflows/inflows of resources depending on the nature of the changes. Substantial changes to methods and assumptions used to determine actuarial information for GAAP reporting purposes will be required. Current actuarial methods may continue to be used to determine funding amounts. Employers will report in their financial statements a net pension liability (asset) determined annually as of the fiscal year end. Net pension liability (asset) equals the total pension liability for the plan net of the plan net position. Pension liability is the actuarial present value of projected benefits attributed to past service, and plan net position is the accumulated plan assets net of any financial statement liabilities of the plan.

The City should expect to record significant pension and OPEB liabilities in the future.

Recommendation

We recommend that management of the City begin the process of coordinating efforts with the Quincy Contributory Retirement pension board and applicable actuaries so that everyone is fully aware of the requirements of these Statements and future statements. Coordinating at this level will also ensure that management is able to assemble any and all necessary information to its actuaries in a timely manner.

Additionally, the current accounting standards require that actuary valuations be conducted every two years unless significant accounting changes or plan design change have occurred. The next OPEB valuation is required to be completed based on data as of June 30, 2014. The next pension valuation is required to be completed based on data as of January 1, 2014. Implementation of these Statements qualifies as a significant accounting change therefore consideration will need to be given to the timing of upcoming valuations so that unnecessary and duplicative costs are avoided.