

CITY OF QUINCY, MASSACHUSETTS

MANAGEMENT LETTER

JUNE 30, 2015



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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, 2015 and issued our report thereon dated March 28, 2016. 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, 2015, 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 28, 2016

CITY OF QUINCY, MASSACHUSETTS

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JUNE 30, 2015

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Other Matters Previously Presented

Please refer to the fiscal years 2008 through 2015 management letters for the full original wording of these comments as the content of the comments has changed over that time period.

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.

Status

Resolved -- Our review of documents processed in the procurement and expenditure cycles showed no evidence of the City having received goods or services prior to the related purchase order being approved. We will continue to monitor the procurement and expenditures cycles for indications of transactions being processed in a manner that violates municipal finance laws of the Commonwealth; however, for purposes of this management letter we consider the matter to be resolved.

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.

Status

Resolved – During the 2015 the City closed out a variety of old capital and special revenue funds. This trend continued into early 2016.

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.

Status – Partially Resolved

The Municipal Finance Office and Planning Departments have developed documents that are at varying stages of completion. Management has developed long term capital 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 documenting those transactions and procedures that do not occur on a routine basis throughout the year.

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 2015 period but a renewed effort will allow for final resolution of this process.

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.

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 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.

Status – Unresolved

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.

Informational Comment

FUTURE GOVERNMENT ACCOUNTING STANDARDS BOARD (GASB) STATEMENTS FOR 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 start to phase in during fiscal year 2017 and 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 #74, *Financial Reporting for Postemployment Benefits Other Than Pension Plans*, which is required to be implemented in 2017.
- The GASB issued Statement #75, *Accounting and Financial Reporting for Postemployment Benefits Other than Pensions*, which is required to be implemented in 2018.

The GASB is encouraging earlier application of these standards. To briefly summarize these new standards –

- GASB #74 and #75 will substantially change the reporting for other postemployment benefit liabilities and expenses. Changes in the OPEB liability will be immediately recognized as an 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 OPEB liability (asset)* determined annually as of the fiscal year end. The *net OPEB liability (asset)* equals the total OPEB liability for the OPEB plan net of the OPEB plan's fiduciary net position. The OPEB liability is the actuarial present value of projected benefits attributed to for each plan member individually, from the period when the plan member first provides service under the benefit terms through the period in which the member is assumed to exit service. The OPEB plan's fiduciary net position is the accumulated plan assets net of any financial statement liabilities of the plan.

The City should expect to record significant OPEB liabilities in the future and should begin planning to be prepared to implement the new standards.

Recommendation

The City is currently using a discount rate of 3.5% and an investment rate of return of 7.5% in the actuarial valuation that determines the annual OPEB expense and unfunded accrued actuarial liability. This is acceptable under current accounting standards; however, GASB Statement #74 will require future benefit payments to be discounted in a manner that reflects 1) a rate of return that can actually be achieved given the balance of OPEB plan's fiduciary net position and 2) a rate that is reflective of a tax-exempt high quality municipal bond rate when consideration is given to the possibility that other stated long term rates of returns are not met.

We recommend that 1) management study and evaluate the necessary changes for financial statement reporting and disclosure purposes 2) formulate plans to meet with actuaries and financial advisers to discuss the processes required to implement the changes. Management should consider how and when this information gets communicated to constituents and other financial statement users.