

TOWN OF LUDLOW, MASSACHUSETTS

Management Letter

For the Year Ended June 30, 2015

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Additional Offices:

Nashua, NH
Manchester, NH
Andover, MA
Ellsworth, ME

To the Selectboard
Town of Ludlow, Massachusetts

In planning and performing our audit of the basic financial statements of the Town of Ludlow, Massachusetts 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 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 over financial reporting.

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 was for the limited purpose described in the first paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

During our audit we became aware of other matters that we believe represent opportunities for strengthening internal controls and operating efficiency. The recommendations that accompany this letter summarize our comments and suggestions concerning those matters.

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

The purpose of this communication, which is an integral part of our audit, is to describe for management and those charged with governance, including those overseeing the financial reporting process, the scope of our testing of internal control and the results of that testing. Accordingly, this communication is not intended to be and should not be used for any other purpose.

Melanson Heath

July 27, 2016

CURRENT YEAR ISSUES:

1. IMPROVE ACCOUNTING FOR SPECIAL ARTICLES

As noted in a prior year comment, the Town's accounting software budget module is not being used effectively in terms of special articles; in many cases the balances carry forward incorrectly or not at all. Special articles have historically been recorded in a separate fund (fund 02) and this seems to be contributing to the budget issues noted.

In the prior year we recommended the Town abandon the separate special article fund and record all general fund-related articles in the general operating fund (fund 01). In fiscal year 2015 we found that fund 02 was still being used but not consistently; in some cases a budget was entered in fund 02 when the actual expenses were recorded in fund 01. There were other cases where line items appeared over-expended because expenses were recorded in fund 01 but the budget authorized in the prior year was missing. Because this situation has existed for several years and the Town annually votes a significant number of special articles, the control and monitoring of these line items within the accounting system has been severely compromised.

We recommend the Town consolidate the accounting for special articles and ensure that all voted appropriations are entered or carried forward in the system.

Town's Response:

The Town will instruct the new Town Accountant to consolidate the accounting of special articles to allow for better monitoring of those articles and the correct voted appropriations.

2. IMPROVE PROCEDURES OVER SCHOOL LUNCH RECEIPTS

The Town sponsors the school lunch program offered at St. John the Baptist School (SJB), a private school in Town that serves grades one through eight. In our review of procedures over the school lunch program, we found that SJB is the only school that uses a token system, whereby students purchase tokens to be used for meals, rather than paying for meals at the time they are served.

SJB does not appear to have a process in place to track the money collected from tokens to amounts deposited with the Town. SJB deposits money periodically throughout the month but there is no correlation between amounts deposited on any given day or week to the tokens sold for the same period. For example, on the day tested, the amount deposited was \$1,779.30 and the record of tokens sold showed that a total of \$1,535.90 was collected.

Since these funds are part of the Town's overall school lunch program, we recommend the Town work with SJB to establish a procedure that reconciles the tokens sold with the funds deposited. This will help ensure that all funds collected for token sales are properly reported and remitted.

Town's Response:

The School Department through its Office of Food Services will work with St. John the Baptist to establish a procedure that reconciles the tokens sold with the funds deposited.

PRIOR YEAR ISSUES:

3. **RESOLVE DIFFERENCES IN SCHOOL DEPARTMENT ACCOUNTS**

Prior to fiscal year 2014, the School Department maintained their own general ledger, separate from the Town's system. Although the separate system was eliminated in fiscal 2014, there continues to be differences in certain funds' ending balances between the Town's general ledger and School's internal project records. While the differences are not material for audit purposes, they are significant enough to warrant investigation and require an ultimate resolution.

We recommend the Town and School coordinate to determine the proper disposition or resolution of these account balances, which may involve making changes to the current account and/or fund structure to provide more clarity and simplify the reconciliation process. In order to resolve this ongoing issue efficiently, the Town / School may want to consider employing a consultant to implement this recommendation.

Town's Response:

The Town and School Department will coordinate the resolution of the disparity in the balances between systems. There will be a documented change to the fund structure in order to reconcile the account balance discrepancies. The Town/School will investigate employing a consultant to implement the reconciliations, as suggested.

4. **IMPROVE CONTROLS OVER POLICE OUTSIDE DETAIL FUNDS**

Similar to prior years, the police outside detail accounts receivable report run from the Police Department's software system as of year-end was incomplete because it only reflected bills issued during fiscal year 2015. Consequently, older bills were not included in the total balance due. There was also no reconciliation to the general ledger balance and no transactions had been posted to the general ledger receivable account during the fiscal year.

To determine the receivable balance due at year end, we used various reports prepared at the time of fieldwork in May 2016 to calculate the total balance due for services provided in fiscal year 2015 and prior. The balance due for older bills, which are either erroneous or almost certainly uncollectible, totaled roughly \$100,000, which approximates the total bad debt estimate that has been reported to the Town since 2013.

Because the Town has already paid the officers, unpaid fees result in a deficit in this fund (which the Town would need to appropriate money to fund) as well as a negative cash flow to the Town.

We continue to recommend the Town fund this deficit at its next Annual Town Meeting. We also recommend that once the deficit is eliminated, procedures be established to ensure this situation does not reoccur in the future. These should include requiring the Police Department to generate an accounts receivable report at least quarterly, and that the report be reviewed by the Board of Selectmen and reconciled to the general ledger. Any delinquent accounts should be reviewed to determine whether they should be written off (and funded through an appropriation).

Town's Response:

The Police Chief has committed to printing a quarterly report for review and further collection. The Town intends to fund this deficit at the next annual town meeting.

5. DEVELOP A MORE FORMAL RISK ASSESSMENT PROCESS

The Town informally performs its own risk assessment for possible fraud or material misstatement through various policies and procedures and regular reviews of trends in the financial statements. Risk assessment is a management function designed to identify where an organization may be vulnerable to errors and/or irregularities. A complete risk assessment process involves a written description of risk areas identified by those charged with governance (management and elected officials) and a description of how the organization intends on responding to the risks.

We recommend that the Town implement a more formal risk assessment process that includes internal audits and written identification of areas where potential fraud or material misstatements to the basic financial statements may occur. Regular department head meetings could be used as a starting point for documenting risk assessment discussions and assessments.

In evaluating risk areas, particular consideration should be given to situations where a single employee is responsible for performing most or all accounting

responsibilities, since this could create opportunities for fraud to occur and go undetected. The Town should evaluate major transactional cycles in all applicable departments to ensure an adequate segregation of duties exists. If staffing levels do not permit an adequate segregation of duties, the Town should provide additional oversight, which should include review and documented sign-off of the key accounting records.

We also recommend the Town establish a formal employee fraud policy to provide staff with guidance in the event they observe or suspect fraud in the workplace.

We further recommend that the Town Accountant perform periodic internal audits of the various departments to ensure compliance with the policies and procedures that are adopted. This should result in improved controls over departmental receipts and reduce the likelihood of irregularities occurring.

Town's Response:

With the hiring of a new Town Accountant, that individual will meet with both the Treasurer and Town Administrator to develop "Best Practices" for a more formal risk assessment.

6. OTHER ISSUES

The following section of the management letter identifies several other current and prior year recommendations for improvements. We report these issues here in a summarized manner and are available to discuss their status with the Town in more detail if desired.

Current year:

- At the time of our audit in May 2016, general ledger cash had not been reconciled to the Treasurer's records since October 2015. Our inquiry found the cause of the delay to be related to a change in how ambulance billings were collected (from the Town Collector to an outside service), which prompted the Accountant to perform a very detailed reconciliation before posting the receipts. This in turn delayed the overall cash reconciliation process.

Since the timely reconciliation of cash is a critical internal control, we recommend a more efficient process for posting ambulance receipts be adopted.

- The overlay (allowance for abatements and exemptions) balance in the general ledger was approximately \$25,000 more than the Assessor's balance as of June 30, 2015. The general ledger balance should be reconciled with the Assessor's Office at least annually.

- In our review of escrow deposits, we found that the Public Works department had received \$18,000 in guarantee bonds (checks written to the Town) in June 2015, which were not turned over to the Treasurer's office as of our audit in May 2016. Any deposits received by a department should be promptly remitted to the Treasurer.
- In our review of Selectboard meeting minutes we noted that as of May 2016, none of the calendar year 2016 minutes were available and one meeting each from October and November 2015 were missing. Minutes of these meetings should be available to the public and be kept as current as possible.

Prior year:

- For the last four fiscal years, the annual budgeted transfer from the Ambulance Subscription fund to the general fund has not been recorded in the general ledger. The amount of the transfer varies each year, ranging from \$48,000 to \$71,000. All budgeted transfers should be recorded at the beginning of the fiscal year.
- While tax title commitments were recorded in the general ledger, there was only one other adjustment posted (after year-end) to reflect all other transactions. Like all other receivable accounts, tax title activity (commitments and receipts) should be recorded as they occur and the balances reconciled with the Treasurer's records on a quarterly or semi-annual basis.
- Student activity funds of approximately \$56,000 were included in the general ledger but were not reflected in the Treasurer's records. Since the Town is ultimately responsible for these funds, they should be reflected in the Treasurer's balances.
- The Treasurer's Office does not have a current supportable list of non-expendable trust fund balances.

Town's Response:

- The student activity funds were added to the Treasurer's records in fiscal year 2016.
- The Treasurer's Office will research and attempt to compile a list of non-expendable trust fund balances.

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All other prior year management letter comments have been satisfactorily resolved or repeated as current year issues.