

TOWN OF BLANDFORD,
MASSACHUSETTS

Management Letter

For the Year Ended June 30, 2004

TABLE OF CONTENTS

	<u>PAGE</u>
<u>INTRODUCTORY LETTER</u>	1
<u>CURRENT YEAR ISSUES</u>	
1. Improve Procedures to Ensure Compliance With Procurement Act (Compliance Finding)	3
2. Comply with Rural Development Agency (RDA) Regulations (Compliance Finding)	4
3. Improve Controls Over Tax Collection and Reconciliation Procedures (Reportable Condition/Material Weakness)	4
4. Develop Budget Plan for Water Project Debt Service	5
5. Improve Controls Over Commitments	6
6. Comply with Grant Terms and Conditions	7
7. Include Short-Term Interest Costs in Water Budget	7
8. Improve Timeliness of Receipt Postings	7
9. Retain Documentation of Employee Pay Rates	8
10. Perform Periodic Inventory of Owned Equipment	8
11. Perform Periodic Audits of Gas Usage at the Highway Department	8
<u>PRIOR YEAR ISSUES</u>	
12. Include Outstanding Check Numbers in Bank Reconciliation	8
13. Establish More Aggressive Tax Collection Policy	9
14. Reconcile Allowance for Abatements (Overlay)	9
15. Review Procedures for Entering Executive Sessions	9
16. Implement Reconciliation Procedures for Key General Ledger Accounts	10
17. Improve Internal Controls in Certain Key Departments	10
18. Include Library Trust Fund Activity in Town's General Ledger	10
19. Establish Travel-Related Administrative Regulations	11

MH&Co

MELANSON HEATH & COMPANY, PC

CERTIFIED PUBLIC ACCOUNTANTS
MANAGEMENT ADVISORS

51 Davis Street • Suite 1
Greenfield, MA 01301-2422
Tel (413)773-5405 • Fax (413)773-7304
www.melansonheath.com

To The Board of Selectmen
Town of Blandford, Massachusetts

We have audited a portion of the basic financial statements of the Town of Blandford, Massachusetts as of and for the year ended June 30, 2004 and have issued our report thereon dated February 18, 2006. As part of our audit, we made a study and evaluation of the Town's system of internal accounting control to the extent we considered necessary to evaluate the system of internal accounting control in determining the nature, timing, and extent of other auditing procedures that are necessary for expressing an opinion on the financial statements.

The management of the Town of Blandford is responsible for establishing and maintaining a system of internal accounting control. In fulfilling this responsibility, estimates and judgments by them are required to assess the expected benefits and related costs of control procedures. The objectives of such a system are to provide reasonable but not absolute assurance that assets are safeguarded against loss from unauthorized use or disposition, that transactions are executed in accordance with required authorization and recorded properly to permit the preparation of financial statements in accordance with generally accepted accounting principles.

Because of inherent limitations in any system of internal accounting control, errors or irregularities may still occur without being detected. Also, projection of any evaluation of the system to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the degree of compliance with the procedures may deteriorate.

We noted a certain matter involving the internal control structure and its operation that we consider to be a reportable condition under standards established by the American Institute of Certified Public Accountants. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control structure that, in our judgment, could adversely affect the entity's ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements. This item is identified in the Table of Contents and comment headings.

Additional Offices:

Nashua, NH • Ellsworth, ME • Andover, MA

A material weakness is a reportable condition in which the design or operation of one or more of the specific internal control structure elements does not reduce, to a relatively low level, the risk that errors or irregularities in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control structure would not necessarily disclose all matters in the internal control structure that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses as defined above. However, we believe the reportable condition described above is a material weakness.

We are also submitting for your consideration a number of comments and recommendations which are not considered to be reportable conditions but are intended to improve operations and internal accounting control.

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

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

Melanson, Heath & Company, P.C.

Greenfield, Massachusetts
February 18, 2006

CURRENT YEAR ISSUES

1. IMPROVE PROCEDURES TO ENSURE COMPLIANCE WITH PROCUREMENT ACT (COMPLIANCE FINDING)

Massachusetts General Laws Chapter 30B requires that purchases of \$ 5,000 to \$ 25,000 be supported by documentation that quotes were obtained by at least three vendors and that expenditures of \$ 25,000 or more be subject to a formal bidding process. Section 15 of Chapter 30B further establishes competitive, sealed bid procedures for the disposition of Town owned tangible property. In testing for compliance with MGL Chapter 30B, for fiscal years 2004 and 2003, we noted several instances of non-compliance with Chapter 30B, including:

- The Town could not provide evidence of a competitive bid process for excavation work done on the Kaolin Road project which was funded by a grant from the Massachusetts Turnpike Authority. During fiscal year 2004 approximately \$58,000 was paid to Northwood Excavating for the project. Based on the amount, this contract should have been subject to a formal bid process.
- The Town could not provide evidence of a competitive bid process on two purchases in fiscal year 2004 and three purchases in fiscal 2003 ranging from \$ 6,000 to \$ 38,000 each.
- The Town could not provide evidence of a competitive bid process for the lease of a Cat loader between fiscal year 2003 and 2004 with four payments totaling \$ 15,200.
- Multiple purchases from one vendor in fiscal year 2003 totaling \$ 37,000 where there was no evidence that procurement requirements were met.
- The former Highway Superintendent sold two Town trucks without evidence of compliance with Chapter 30B, Section 15. One of the trucks was purchased by the former Highway Superintendent himself for \$ 200. The second truck was sold to a private entity for \$ 2,000 although it had an assessed valued of \$ 7,000.

In order to these situations in the future, we recommend the Town's Chief Procurement Officer maintain all bid and quote files for the legally required amount of time. Additionally, as a method of checks and balances, we recommend that all bills submitted to the Town Accountant for payment contain a certification that all applicable bid requirements have been met in accordance with Massachusetts General Laws. Implementation of these recommendations will ensure that the appropriate bid procedures have been followed and that supporting documentation is properly retained and accessible.

2. COMPLY WITH RURAL DEVELOPMENT AGENCY (RDA) REGULATIONS (COMPLIANCE FINDING)

The Town is currently undergoing a significant water system improvement project federally funded through the Rural Development Authority (RDA) and administered for the Town by an independent engineering firm. According to Town officials, some of the bids for the project came in lower than anticipated and resulted in funds being available for "re-programming". The funds were re-programmed for the purpose of mapping the Town's water lines and identifying the current users and potential users of water. According to the independent engineering firm and Town officials, the "re-programming" of funds was done with the approval of the RDA; however, no documentation of this approval could be provided and we were unable to confirm the approval with the funding source. We also were unable to obtain a written project scope amendment with the engineering firm or other documentation to describe the scope of the task to be performed.

The Water Commissioners wanted to use Town employees to complete the mapping project since they would already have access to the necessary documentation as well as familiarity with the Town. According to Town officials, the RDA informed the Town the funds could not be used to pay Town employees. The engineering firm then agreed to hire two Town employees to perform the task and charge them to the project as the firm's employees. According to the engineering firm, the oversight and monitoring of the mapping project remained the responsibility of the Water Commissioners.

A total of 1,578.50 hours were charged to the mapping project. The maps produced by one of the employees cannot currently be located. The maps produced by the second employee were not, in the estimation of the Town, sufficient to justify the 1,279.50 hours the employee charged to the project. As a result, we have questioned the costs (\$ 39,462.50) related to the charges for the mapping project. (See also Single Audit Compliance Finding 04-3.)

We recommend the Town comply with grant regulations by ensuring grant expenditures are allowable and are a reasonable and efficient use of resources.

3. IMPROVE CONTROLS OVER TAX COLLECTION AND RECONCILIATION PROCEDURES (REPORTABLE CONDITION/MATERIAL WEAKNESS)

During fiscal year 2003, the Town opened a Collector's bank account. This bank account operates on an imprest basis, wherein tax collections are deposited weekly, biweekly or monthly (depending on frequency and amount of collections). At the end of the week, a check is issued for turnover to the Treasurer and deposited into the operating accounts of the Town. The balance in the account should reflect no more than one week's collections at any given time.

At June 30, 2004, the Collector's account had a reconciled bank balance of \$ 281,920. This balance represented \$ 243,949 in fiscal year 2004 receipts that were turned over to the Treasurer between October 2004 and June 2005. There were additional reconciling items totaling \$ 36,971 from fiscal years 2003 and 2004 that did not appear to have been turned over as of our fieldwork in February 2006.

After adjusting for the late turnovers, there remained several immaterial variances between the Collector's outstanding detailed receivable balances and the general ledger. As reported in previous year's management letter comments, the Collector does not maintain control totals, which would simplify this analysis and be used to identify the source of the remaining variances.

The lack of timely turnovers to the Treasurer significantly increases the risk of errors or irregularities occurring and going undetected. It also negatively impacts the cash flow of the Town and limits the Town's ability to monitor revenue collections in comparison to budget. The lack of a Collector's control schedule increases the difficulty in reconciling the detailed receivable balances to the general ledger.

We recommend the Town improve controls over tax collection and reconciliation procedures. This can be accomplished by requiring the following:

- Turnover of collections to the Treasurer on a weekly basis, and as of the last day of the month.
- Monthly reconciliation of the Collector's bank account to the Collector's records.
- Deposit receipts into the Collector's bank account at least weekly.
- Implement a receivable control log and ensure that is reconciled to the detailed list of outstanding receivables and general ledger balances monthly. Any variances should be identified specifically and appropriately corrected.

Implementation of these procedures will reduce the risk of errors or irregularities occurring and going undetected, as well as improve cash flow and provide timely revenue reporting.

4. DEVELOP BUDGET PLAN FOR WATER PROJECT DEBT SERVICE

The Town has approximately 200 water users. All water enterprise fund expenditures are distributed among the users based on an annual user charge. In fiscal year 2003, the Town began a major water project to improve its water system and construct a new filtration plant. The anticipated cost of the project is \$ 8,131,060 to be funded through USDA Rural Development Agency grants and loans totaling \$ 3,475,937 and \$ 4,655,123 respectively. The loans are anti-

pated to be payable over a period of 38 to 43 years. The project is scheduled in 3 phases. As each phase is completed, the loan for the respective phase closes and the annual payments of debt service are initiated. Once all of the loans close, the annual repayments will average approximately \$ 251,000. There are both fixed and variable payment water bonds; therefore, the repayment amount will vary from year to year. In certain years, the payment may be as high as \$ 300,000 annually.

The Town will need to fund the increase in water enterprise fund expenditures through a significant increase in user charges and/or a subsidy from the general fund. A significant increase in rates may cause a financial hardship for some users and result in an inability to collect the fees assessed. The Town is limited in its ability to subsidize the water enterprise fund because it is currently at it's maximum property tax levy capacity and the water debt is not excluded from the levy limit.

We recommend the Town begin to aggressively evaluate all potential options and develop a budget plan to fund the future increased expenditures of the water enterprise fund.

5. IMPROVE CONTROLS OVER COMMITMENTS

During various testing procedures, we noted the following areas of weakness over the commitment process:

- As reported in prior years, the Town usually bills on a semi-annual basis for usage by customers in the prior fiscal year. The water charges committed in fiscal year 2004 were for the period of July 1, 2002 to June 30, 2003. As a result, the Town's water enterprise fund is collecting fees for services provided several months in arrears. This results in diminished cash flows and can negatively impact certification of equity surplus.
- Approximately \$ 110,000 in Payments in Lieu of Taxes were not committed to accounts receivable for fiscal year 2004 until June 18, 2004. As a result, bills were not issued until near or after year end and payment was not received until August 2004. This further resulted in the revenue not being available for free cash.
- The Town could not locate a summary commitment warrant (original or copy) for water liens receivable in the amount of \$ 70,040.

We recommend the Town improve controls over commitments by ensuring commitments are processed in a timely manner and all original summary commitment warrants are retained. A copy of the commitment should also be maintained in the originating department's files when the original is submitted for collection.

6. COMPLY WITH GRANT TERMS AND CONDITIONS

The Town was awarded a Massachusetts Turnpike Authority (MTA) Tourism Grant in December 2002. The purpose of the grant, according to the "Work Plan Objectives" prepared by the Town, was to replace water mains from the pump house on North Street to the storage tank, installation of new pumps at the pump station, and installation of new hydrants in the vicinity of the MTA rest area on North Street. A review of the expenditures revealed the grant was actually used for the replacement of water lines on Kaolin Road, a residential street located approximately 1.5 miles from the pump house and MTA rest area. The Town contends that a grant amendment had been approved by the MTA; however, no written approval was provided.

The grant conditions also specifically state, "The Authority does not reimburse for staff salaries"; however, four employees were paid salaries from grant proceeds. The grant agreement also requires the submission of separate fiscal and narrative reports on programmatic activity to the MTA. Based on inquiry of the Town, these reports were not submitted.

We recommend the Town comply with all grant terms and conditions and retain documentation of any changes in grant agreement or conditions. Expenditures should be evaluated to ensure they are consistent with allowable grant activities before they are paid. Improvements in these procedures will minimize the risk of disallowed costs that would be subject to recoupment by the funding source.

7. INCLUDE SHORT-TERM INTEREST COSTS IN WATER BUDGET

The Town did not include the interest costs resulting from short-term borrowing for the water project in the fiscal year 2004 water enterprise fund budget. This resulted in approximately \$ 29,000 that was required to be raised on the fiscal year 2005 recap and, in effect, created a general fund subsidy to the water enterprise fund.

We recommend the Town budget the interest costs related to short-term borrowing for the water project in the water enterprise fund.

8. IMPROVE TIMELINESS OF RECEIPT POSTINGS

Receipts are not posted to the Treasurer's receipt subsidiary journal until well after month end. This results in untimely postings to the general ledger which can hinder reconciliation procedures and budget monitoring. It also increases the risk of errors or irregularities occurring and going undetected.

We recommend the Town improve the timeliness of receipt postings by ensuring the Treasurer's receipts are posted to the subsidiary journal within 30 days of month end.

9. RETAIN DOCUMENTATION OF EMPLOYEE PAY RATES

The Town's Board of Selectmen and Water Commissioners approve employee pay rates. As reported in the prior year, controls over documentation of pay rates should be improved. During our testing of eight payroll expenditures for fiscal year 2004 we identified one employee file that did not contain documentation of the Board of Selectmen's approved pay rate in effect at the time. A second individual (a Water Department employee) was paid at \$ 20.00 per hour instead of the Water Commissioner approved rate of \$ 14.00 per hour. We recommend the Town retain documentation of each approved rate in the employee's file. This documentation could include either an individual salary agreement or a Town-wide salary scale, as approved by the Board of Selectmen or Water Commissioners. We further recommend the Town compare approved rates to rates processed through payroll to ensure they are consistent with authorized and budgeted amounts.

10. PERFORM PERIODIC INVENTORY OF OWNED EQUIPMENT

The Town does not have a listing for, or perform a periodic inventory of, Town owned equipment. This can result in the loss or misappropriation of assets occurring and going undetected.

We recommend the Town develop a list of equipment owned by the Town and perform periodic inventories ensure that Town assets are appropriately safeguarded.

11. PERFORM PERIODIC AUDITS OF GAS USAGE AT THE HIGHWAY DEPT.

The Highway Department has its own gas pump to provide fuel for highway vehicles. Gas cards (similar to credit cards) are issued to each Highway Department employee in order to access the pump. The pumps can produce an audit report which indicates the employee accessing the pump and the date accessed. Currently, there are no formal procedures in place to monitor the consumption of gas. Lack of monitoring procedures can result in irregularities occurring and going undetected.

We recommend the Town perform periodic audits of the gas consumption at the Highway Department to ensure usage is reasonable based on Highway Department activity.

PRIOR YEAR ISSUES

12. INCLUDE OUTSTANDING CHECK NUMBERS IN BANK RECONCILIATION

While the Town Treasurer reconciles the bank statements monthly, we noted that two of the bank account reconciliations do not include the individual check

numbers for some of the outstanding checks. This complicates the reconciliation process and can result in errors.

We recommend the Town Treasurer include the check numbers for all outstanding checks on the bank reconciliations. This will help simplify the reconciliation process, provide a clear trail of the status of checks issued, and minimize the risk of errors.

13. ESTABLISH MORE AGGRESSIVE TAX COLLECTION POLICY

The Town does not follow an aggressive policy for collecting delinquent taxes. Massachusetts General Laws provide specific timetables for the liening and foreclosing of properties for non-payment. The Town has not been performing these procedures as aggressively as permitted by statute. The Town has delinquent taxes dating back to fiscal year 1989. The existence of old receivables results in the loss of revenue from the increased interest rates of lienied properties. Also, the Town risks losing a secured interest in the property in the event the property is sold or the taxpayer files for bankruptcy.

We recommend the Town establish a policy to be more aggressive in pursuing delinquent accounts. This will result in an improved financial condition of the Town.

14. RECONCILE ALLOWANCE FOR ABATEMENTS (OVERLAY)

The Assessors' Office does not maintain an independent balance of the allowance for abatements (overlay) accounts but instead relies on the general ledger. A good internal control system dictates that the Assessors' Office maintain a balance of allowance for abatements and that this balance be periodically reconciled to the general ledger. As a result, there is assurance that all abatements granted are properly recorded in the general ledger and in a timely manner.

We recommend the Assessors' Office maintain a continuous record of all abatements and reconcile the balance of this record with the general ledger on a regular basis.

15. REVIEW PROCEDURES FOR ENTERING EXECUTIVE SESSIONS

As in the prior years our review of the Board of Selectmen's meeting minutes, for fiscal year 2004 found several instances in which the Selectmen entered into executive sessions without following the appropriate procedures as dictated by Massachusetts General Laws (MGL) Chapter 39, Section 23. We noted that in several instances a roll call vote was not taken, the purpose for an executive session was not stated, and there were no statements as to whether or not the Board would reconvene after the executive session.

We recommend the Board of Selectmen follow the applicable MGL when entering into executive sessions.

16. IMPLEMENT RECONCILIATION PROCEDURES FOR KEY GENERAL LEDGER ACCOUNTS

Our inquiries found that several key general ledger accounts (including accounts receivable, payroll withholding and debt) are not reconciled on a regular (monthly/quarterly) basis.

Reconciliation of general ledger balances to supporting documentation and adjustments of activity and records is integral in ensuring the accuracy of the Town's accounting records.

We recommend the Town establish formal procedures to reconcile these key general ledger accounts on a monthly basis. This will provide additional assurance that accurate information is provided to Town management and will reduce the likelihood that errors or irregularities could occur and go undetected. This will also reduce the effort required to close the books at year end.

17. IMPROVE INTERNAL CONTROLS IN CERTAIN KEY DEPARTMENTS

A key component of any financial statement audit is the evaluation of internal controls. This evaluation is accomplished through inquiry, observation and testing. In addition to the weaknesses in the collector's office noted in a separate comment, the following weaknesses were noted as a result of our evaluation of controls in the following key Town departments:

Treasurer's Office:

- Certain departments do not remit receipts in a timely or consistent manner.

Town Accountant:

- The Town's general ledger is accessible to the Town Accountant and Treasurer, thereby weakening the separation of duties between the accounting function and the treasury function.

We recommend the Town review, in conjunction with the above-noted deficiencies, the Town's overall internal controls in order to create an environment where the risk to Town assets is acceptably minimized.

18. INCLUDE LIBRARY TRUST FUND ACTIVITY IN TOWN'S GENERAL LEDGER

The Town has traditionally reported balances for various library trust funds in its general ledger as well as including them in the Treasurer's quarterly cash reconciliation reported to the State. The balances are recorded based on information provided at year end by the library Board of Trustees. Balances are adjusted from year to year through general entries as no activity is recorded in

the Town's general ledger. In fiscal years 2002 through 2004, the balances were not updated, resulting in erroneous general ledger and Treasurer cash balances.

Because the Town is assuming a fiduciary duty over the library Trust Funds, we recommend the activity and resulting balances for the library Trust Funds be recorded in the Town's general ledger. This activity can be recorded on a periodic basis based on supportable information provided by the library Board of Trustees. Implementation of this recommendation will provide assurance that the balances reported by the Town for the library Trust Funds are accurate and supportable, and that sufficiently detailed activity is recorded in the Town's general ledger.

19. ESTABLISH TRAVEL-RELATED ADMINISTRATIVE REGULATIONS

The Town does not maintain formalized regulations to provide departments with documented guidance over travel-related administrative policies and procedures. As a result, inconsistencies may exist between departments with respect to such issues as:

- Prior approval of travel and conference attendance
- Travel and expense reimbursement limits
- Approval of travel and expense reimbursement
- Establish standard rate of mileage reimbursement

We recommend the Town develop formal regulations to provide current guidance over travel-related administrative policies and procedures. This should result in improved Town-wide consistency over travel-related expenditures.

* * *

All other prior year issues have been satisfactorily resolved or repeated in current year issues.