

***CITY OF LOWELL, MASSACHUSETTS***

***MANAGEMENT LETTER***

***JUNE 30, 2017***

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

In planning and performing our audit of the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Lowell, Massachusetts as of and for the fiscal year ended June 30, 2017, 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 opinions 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.

However, during our audit we became aware of several matters that are opportunities for strengthening internal controls and operating efficiency. The memorandum that accompanies this letter summarizes our comments and suggestions regarding those matters.

We will review the status of these comments during our next audit engagement. We have already discussed these comments and suggestions with various City personnel, and will be pleased to discuss them in further detail at your convenience, to perform any additional study of these matters, or to assist you in implementing the recommendations.

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

*Powers + Sullivan, LLC*

February 15, 2018

CITY OF LOWELL, MASSACHUSETTS

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***Prior Year Comments - Resolved***

The following comments were resolved during the current year. Please see the June 30, 2016, Management Letter for the complete original comment.

**OLD OUTSTANDING RECEIVABLES**

**BUDGETED OPERATING TRANSFERS**

**CDBG LOANS RECEIVABLE**

**OTHER POSTEMPLOYMENT BENEFIT ACTUARIAL VALUATION**

**CHAPTER 90 FUND**

**GENERAL LEDGER MAINTENANCE**

**WATER AND SEWER USER CHARGES**

**FIXED ASSETS**

**PAYROLL WITHHOLDING ACCOUNTS**

**ACCOUNTING FOR LONG-TERM DEBT ACTIVITY**

**RELEASING FUNDS PRIOR TO AUTHORIZATION**

**SCHOOL INDIRECT CHARGES**

## ***Prior Year Comments - Unresolved***

## **CASH RECONCILIATION PROCEDURES**

### Prior Year Comment

In previous management letter we reported the following deficiencies surrounding the reconciliation of cash:

- Although the Treasurer's Office reconciled the bank statements to the Treasurer's book balance during the year, no monthly reconciliations occurred to reconcile Treasurer's cash to the general ledger.
- Many account reconciliations include reconciling items that are between 1 and 3 years old that have not been researched to determine its nature and final disposition.
- Vendor and payroll account reconciliations are completed by the bank but have not been reviewed and approved by the Treasurer's Office. These reconciliations include multiple items for over/under funding of warrants, stop payments and other miscellaneous items.
- An unreconciled cash variance has existed between the Treasurer's records and the general ledger for fiscal years 2014 and 2015 totaling \$245,000 and \$184,000, respectively.

Without monthly reconciliations there is a significant risk that errors or irregularities in amounts that would be material to the City's financial statements may occur and not be detected within a timely manner by City employees in the normal course of performing their assigned functions. Furthermore, the potential for errors to occur is significantly reduced with regular reconciliation procedures.

### Current Status

During 2017, the City's Treasurer resigned and the City has appointed an interim Treasurer who is working to determine the best way to account for and reconcile the City's cash accounts.

The City's interim Treasurer has reconciled cash with immaterial unknown variances as of June 30, 2017, and is working on updating the policies and procedures surrounding the cash reconciliation process. The City has also implemented the use of the general ledger cash module which is expected to facilitate the reconciliation process and should allow for both a more efficient and effective cash reconciliation process. The City expects that these procedures will be implemented in 2018 and that this comment will be cleared in 2018.

### Continuing Recommendation

- Although many old items have been removed, we recommend that old reconciling items be investigated and the proper disposition noted to assure that the amounts do not continue to carry over from month to month.
- We recommend that the Treasurer's Office include documentation of what reconciling items represent within the cashbook when items are identified.
- We recommend that the Treasurer formally reconcile the Treasurer's book balance to the reconciled bank balance on a monthly basis and properly account for any unknown variances.
- We recommend that the Treasurer work to close down the old vendor and payroll accounts. We also recommend that all reconciling items on the new accounts be reviewed and corrected in the following month.

## **TAX FORECLOSURES**

### Prior Year Comment

In previous management letters we noted, that the City did not have procedures in place to reconcile the general ledger balance for tax foreclosures to the Collector's records since 2014. Reconciling both the activity and the ending balance of tax foreclosures is an integral internal control procedure over an important revenue source of the City.

### Current Status

The balance on the general ledger still does not agree to the detailed balance maintained by the Collector at June 30, and a correcting entry was required. Activity to the foreclosure account should be recorded as it occurs throughout the year.

### Continuing Recommendation

We recommend that the City implement procedures to reconcile the foreclosure balances and activity from the general ledger to the Collector's records on at least a quarterly basis.

We also recommend that the Collector's Office provide the proper supporting documentation to the City Auditor's Office when amounts are added to the foreclosure account or foreclosed properties are sold.

## **SCHOOL GRANT MANAGEMENT**

### Prior Year Comment

In previous management letters we noted, the Lowell Public Schools receive significant federal education grant funds. We noted during 2016 that the City returned approximately \$508 thousand of federal funds that were not spent during the grant year to the Department of Elementary and Secondary Education.

Although these funds can generally be re-applied for in subsequent periods the City is at risk for having future funds under the programs reduced because current year funds have not been used.

We recommended that management evaluate these programs to determine the underlying reason for the return of funds and develop a plan to maximize the benefits that these programs provide.

### Current Status

During 2017, approximately \$807,000 of grant proceeds was returned.

## **PARKING TICKET RECEIVABLE**

### Prior Year Comment

In previous management letters we noted, the City uses a third party vendor to track the balance of outstanding parking tickets. Persons are able to pay their tickets either at the third party office or at City Hall. If the ticket becomes flagged at the registry they also have the ability to pay at the registry upon trying to register their vehicle. The third party vendor periodically sends a turnover of receipts collected at their office; however they are not providing the City with an outstanding receivable balance. Currently, City personnel in the Collector's Office have the ability to log into the third party system and print a receivable report themselves.

We noted that periodic receivable reports are not being reviewed and reconciled to the general ledger. The balance listed in the City's general ledger at year end is the same balance as recorded in the prior year.

We recommended that the City, on at least a quarterly basis, run the receivable report and reconcile the balance with the general ledger.

### Current Status

The detailed balance as maintained by the third party vendor was not generated and reconciled to the general ledger during 2017. An adjustment was required to properly state the balance as of June 30, 2017.

## **SECTION 108 LOAN FUND**

### Prior Year Comment

In previous management letters we noted, as part of the Federal Section 108 loan program, the City received federal funds in the form of loans from the Department of Housing and Urban Development (HUD) to then loan out to eligible companies for urban development. The City receives loan payments of principal and interest from the eligible companies and then pays HUD the required loan payments due. The activity related to this Section 108 loan program is accounted for in fund 2267 and the balance of the loans outstanding is recorded in fund 1134. Although fund 2267 correctly reports the debt service payments and revenues received under this program in the current year, fund 1134 has not been adjusted to reflect the actual loan balance at year end. Each year adjustments are required to appropriately report the Section 108 loans in the financial statements.

Also, fund 1134 has a cash balance of \$79 thousand that has not changed for multiple years and the City is maintaining fund 1135 as Section 108 also and is reporting a cash balance of \$126 thousand that has not changed for multiple years.

We recommended that procedures be implemented to assure that when debt payments on Section 108 loans are made that the liability balance maintained in fund 1134 be adjusted accordingly.

We also recommended that management determine the nature of the cash balances in funds 1134 and 1135 and determine the proper disposition of these balances.

### Current Status

The loan balances were properly adjusted during 2017. We continue to recommend that management determine the nature of the cash balances in these funds and determine the proper disposition of these balances.

# ***CURRENT YEAR COMMENTS***

## **PURCHASE ORDER DATES**

### Current Year Comment

During expenditure testing we noted that a number of purchase orders were dated past their corresponding invoice dates. Creating purchase orders after the invoice is received bypasses the City's purchasing policies and defeats the control that a purchase order system is intended to provide. Purchase orders play a primary role as they allow the City to ensure that budgetary funds are available and that the purchase has been properly approved before funds are expended.

### Recommendation

We recommended the City implement a process to ensure that purchase orders are initiated prior to the procurement of goods and services.

## **LATE INVOICES**

### Current Year Comment

Invoices paid after year end are reviewed to test for expenditures that may not have been recorded in the proper period. We noted several invoices related to Engineering, Wastewater, and the School Department from March and April 2017 being paid after year end. This situation occurs because the City does not have a well-defined policy outlining the timeliness of processing invoices. The lack of a policy over the timeliness of paying invoices can lead to inaccurate financial reporting and can mask overspending and deficit balances if invoices are intentionally held until the next year.

### Recommendation

We recommended that the City implement procedures to ensure the timely submission and payment of departmental invoices.

## **TREASURER'S CASH DRAW OVER/UNDER POLICY**

### Current Year Comment

When reviewing the general ledger we noted that there are many entries related to the Treasurer's Office having variances in their daily cash draw count. Although errors can occur, it is concerning that the entries in the general ledger are always for an even amount and similar amounts every time. This could indicate a situation in which irregularities are occurring at a level in which it is known that the discrepancies will not be reviewed.

### Recommendation

We recommend the Treasurer's Office develop a written policy that outlines the procedures to follow if a cash draw is under/over, and steps to take if it is consistently the same cash drawer having the irregularities.

# ***INFORMATIONAL COMMENTS***

## Future Government Accounting Standards Board (GASB) Statement for OPEB

### Current Year Comment

The GASB has issued a new pronouncement that will significantly affect the accounting and reporting requirements for Other Postemployment Benefits (OPEB). This new standard will be implemented during 2018 and will substantially impact the City's financial statements and will also affect the requirements for accumulating the necessary data to meet the reporting requirements.

The new standard that has been issued and the effective date is as follows:

- The GASB issued Statement #75, Accounting and Financial Postemployment Benefits Other Than Pensions, which is required to be implemented in 2018.

See below for a brief summary of this new standard:

- GASB #75 will substantially change the reporting for other postemployment benefit liabilities and expenses. Changes in other postemployment benefit liability will be immediately recognized as other postemployment benefit 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. Employers will report in their financial statements a net other postemployment benefit liability (asset) determined annually as of the measurement date. Net other postemployment benefit liability (asset) equals the total other postemployment benefit liability for the plan net of the plan net position. The other postemployment benefit liability is the actuarial present value of projected benefits attributed to past service. The plan 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. While this GASB does not go into effect until 2018, we wanted to make the City aware of the impact that this new standard will have on financial statement reporting and disclosures.

## Documentation of Internal Controls

### Current Year Comment

In December 2013, the U.S. Office of Management and Budget (OMB) issued *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) in an effort to (1) streamline guidance for federal awards while easing the administrative burden and (2) to strengthen oversight over the expenditure of federal funds and to reduce the risks of waste, fraud and abuse.

The Uniform Guidance supersedes and streamlines requirements from eight different federal grant circulars (including OMB Circular A-133) into one set of guidance. Local governments are required to implement the new administrative requirements and cost principles for all new federal awards and to additional funding to existing awards made after December 26, 2014 (fiscal year 2016).

In conformance with Uniform Guidance, the non-Federal entity must: (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in "Standards for Internal Control in the Federal Government" issued by the Comptroller General of the United States (the Green Book) and the "Internal

Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

The COSO internal control framework is generally accepted as a best practice within the industry including the best practices prescribed by the Government Finance Officers Association (GFOA). COSO is a joint initiative of 5 private sector organizations dedicated to providing thought leadership through the development of frameworks and guidance on enterprise risk management, internal control and fraud deterrence. The original COSO framework was published in 1992 and has been revised several times for changes in operations, technology, and audit risk. The most recent updates to the COSO Internal Control - Integrated Framework were issued in 2013 and are available at [www.coso.org](http://www.coso.org).

Management is responsible for internal control and to see that the entity is doing what needs to be done to meet its objectives. Governments have limited resources and constraints on how much can be spent on designing, implementing, and conducting systems of internal control. The COSO Framework can help management consider alternative approaches and decide what action it needs to take to meet its objectives. Depending on circumstances, these approaches and decisions can contribute to efficiencies in the design, implementation, and conduct of internal control. With the COSO Framework, management can more successfully diagnose issues and assert effectiveness regarding their internal controls and, for external financial reporting, help avoid material weaknesses or significant deficiencies.

The COSO internal control framework incorporates 5 major components of internal control, which are supported by 17 principles of internal control as follows:

1. CONTROL ENVIRONMENT
  - 1) Demonstrates commitment to integrity and ethical values
  - 2) Exercises oversight responsibility
  - 3) Establishes structure, authority, and responsibility
  - 4) Demonstrates commitment to competence
  - 5) Enforces accountability
2. RISK ASSESSMENT
  - 6) Specifies suitable objectives
  - 7) Identifies and analyzes risk
  - 8) Assesses fraud risk
  - 9) Identifies and analyzes significant change
3. CONTROL ACTIVITIES
  - 10) Selects and develops control activities
  - 11) Selects and develops general controls over technology
  - 12) Deploys through policies and procedures
4. INFORMATION & COMMUNICATION
  - 13) Uses relevant information
  - 14) Communicates internally
  - 15) Communicates externally

## 5. MONITORING

- 16) Conducts ongoing and/or separate evaluations
- 17) Evaluates and communicates deficiencies

Management should evaluate and assess the government's internal control system to determine whether: each of the five essential elements of a comprehensive framework of internal control is present throughout the organization; whether each element addresses all of the associated principles; and whether all five elements effectively function together.

### Recommendation

We recommend management follow the best practice for establishing and documenting their internal control system using the COSO Internal Control Framework.