

CITY OF WORCESTER, MASSACHUSETTS

MANAGEMENT LETTER

JUNE 30, 2011



Certified Public Accountants

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

In planning and performing our audit of the financial statements of the City of Worcester, Massachusetts (City) as of and for the year ended June 30, 2011 (except for the Worcester Contributory Retirement System, which is as of and for the fiscal year ended December 31, 2010), in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, 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 recommendations regarding those matters. This letter does not affect our report dated October 31, 2011, on the financial statements of the City.

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

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

Sullivan, Rogers & Company, LLC

October 31, 2011

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Comments and Recommendations

Green Hill Golf Course

Comment

The Green Hill Golf Course (the golf course) has a lease agreement (the agreement) with Kitsta Corporation (the tenant) to operate the golf course restaurant, bar, concessions and banquet services. As part of the agreement, the tenant pays the golf course monthly rent along with a percentage of gross monthly food and beverage sales.

We evaluated the systems of internal control related to the gross food and beverage sale payments (payments) and identified the following deficiencies:

1. According to the agreement, the payments are required monthly. We identified several instances in which the golf course's invoices for payments included amounts for partial portions of a month. From an administrative and consistency perspective, the golf course's invoices should be prepared monthly and cover an entire monthly period.
2. According to the agreement, beginning in January 2011, the tenant was required to pay the golf course eight (8) percent of gross monthly food and beverage sales. We identified that the January 2011 payment was for six (6) percent of monthly gross sales. While the payment difference was nominal, the payment was noncompliant with the agreement.

Recommendation

We recommend the golf course implement policies and procedures to:

1. Invoice gross food and beverage sale payments on a monthly basis for the entire monthly period
2. Verify that all payments are calculated in accordance with the terms of the agreement

Management's Response

Although the observation noted by the auditors appears to be an aberration, Administration & Finance (Treasurers Division) shall coordinate with the department of Public Works (Parks Division) to develop and document procedures to ensure monthly lease payments are remitted timely and accurately.

Department of Public Works and Parks Overtime

Comment

We evaluated the systems of internal control related to overtime payroll of the Department of Public Works and Parks (the department) and identified the following deficiency:

- One (1) of the 15 overtime timesheets tested did not have signatures indicating that supervisory personnel reviewed them. The department's "Payroll Procedures Manual" states that overtime timesheets require two (2) signature approvals of the employee's immediate supervisor and the divisional director.

Recommendation

We recommend the department implement procedures to ensure that all overtime timesheets contain two signature approvals prior to processing payroll.

Management's Response

The Department of Public Works and Parks is extremely diligent in the oversight of their internal procedures involving payroll processing, but recognizes exceptions do occur. The Department shall ensure that all payroll overtime slips are countersigned by the immediate supervisor and the divisional director.

Fire Department Overtime

Comment

We evaluated the systems of internal control related to overtime payroll of the Fire Department (the department) and identified the following deficiency:

- Twelve (12) of the 30 overtime timesheets tested were not signed by the employee. The department's policies (as stated at the top of the overtime timesheet) state that the employee submitting the overtime timesheet must personally sign the timesheet.

Recommendation

We recommend the department implement procedures to ensure that employees sign all overtime timesheets prior to processing payroll.

Management's Response

The Fire Department's policies relative to signing and countersigning has evolved over time to only requiring supervisory signatures on overtime slips, without amending their internal policies. After discussions with the Department of Administration and Finance, the Department shall return to enforcing the policy of obtaining both the employee and the commanding officers' signatures before processing overtime timesheets.

Marriage Counseling Special Revenue Fund

Comment

During fiscal year 2007, the City Clerk department (the department) increased the marriage license fee from \$40 per license to \$50 per license. The \$10 increase was implemented by the department to generate funds for donations to nonprofit agencies that provide marriage counseling to Worcester residents. During fiscal years 2007, 2008 and 2009, \$10 per marriage license revenue was posted to the Marriage Counseling special revenue fund (the fund). No revenues were posted to the fund during fiscal years 2010 and 2011. As of June 30, 2011, the fund's balance was \$43,130. This balance consisted entirely of revenues collected with the exception of a miscellaneous \$20 expenditure in fiscal year 2007.

According to Massachusetts General Laws (MGL) Chapter 40, Section 22F, the establishment of license fees by an officer who was appointed by an elected board shall be subject to the review and approval of such elected board. In this case, the City Clerk is an officer appointed by the City Council (i.e. an elected "board"). Therefore, if the City Council has accepted the provisions of MGL Chapter 40, Section 22F, the \$10 increase to the marriage license fee implemented in fiscal year 2007 had to be approved by the City Council. It is our understanding that the increase to the marriage license fee was not (and has not been) formally approved by the City Council.

In addition, we are not aware of any legal authority under which the Marriage Counseling fund was established, nor are we aware of the City Council formally approving the establishment of this fund.

Recommendation

We recommend the City determine whether there was legal authority to establish the Marriage Counseling fund. If not, the City must determine how the unauthorized funds should be accounted for and take appropriate action. We recommend the City consult with its Law Department and the Massachusetts Department of Revenue to assist in the matter.

Management's Response

The Department of Administration and Finance shall attempt to determine the legal authority in which the proceeds contained in the Marriage Counseling Special Revenue Fund were derived in consultation with the Law Department and the Department of Revenue. Upon this determination, the Treasurers Division shall take actions accordingly to either reclassify said proceeds to the appropriate fund or refund said proceeds.

Change Orders

Comment

In the prior year Management Letter, we identified change orders to a construction contract in which the change orders did not relate to a change in the scope of work to the original contract and were for amounts that far exceeded the original contract amount. City management's response to our findings contended that the change orders were appropriate since, among other reasons, they were issued less than six (6) months after the original contract was executed, thereby ensuring that the best available price was obtained.

During fiscal year 2011, we tested five change orders to construction contracts and identified that each change order was executed more than 6 months after the original contract was executed.

Two (2) change orders (both relating to the same original contract) were executed more than 2 years after the original contract. These two particular change orders represented the 15th and 16th change orders to the original contract, which was for \$2,528,769. After the execution of the 16th change order, the total change orders amounted to \$4,290,272, a 170% increase to the original contract amount.

By approving change orders greater than 6 months after the original contract was executed, as opposed to rebidding the contract(s), the City is at risk of not obtaining the best available price(s) for its construction projects.

Recommendation

We recommend the City evaluate its policies, procedures and practices related to procurement of construction projects and determine if they are in the best interests of the City and in compliance with Massachusetts Procurement Laws.

Management's Response

The City employs sound business practices in bidding and awarding Public Works (street resurfacing) projects. Although these activities are not subject to the provisions of Chapter 30B (limitation of a change order in excess of 25%), the City carefully considers the current construction market conditions, the cost and time associated with bidding of additional but similar work, (street resurfacing) prior to issuing change orders. Use of existing and recent contracts (for a period of up to 2 years as specified in the contract) for like work is often used to maximize the construction season to complete the extensive list of committed projects. The Department, in consultation with the Law Department, will develop a "Guidance Manual" to memorialize under what circumstances, administratively and financially, the utilization of change orders shall be utilized.

Health Department

Comment

In the prior year, we evaluated the systems of internal control related to the Health department (the department) and identified two (2) deficiencies. One (1) of the deficiencies was resolved in fiscal year 2011. However, the following deficiency remains unresolved:

- The department maintains an automated log of permits issued. However, the department does not perform daily reconciliations between cash collections and the number of permits issued as identified in the automated log. Performance of these reconciliations provides assurance that the proper amount of cash has been collected and recorded for the permits issued by the department.

Recommendation

We recommend the department utilize the automated log to reconcile cash receipts to the number of permits issued on a daily basis. The reconciliations should be reviewed and signed-off by the preparer and reviewer and maintained on file.

Management's Response

As noted in the comment, the administration has resolved the prior years comment. Unfortunately, with this resolution inadvertently omitted the implementation of a reconciliation of the automated permitting module. The Department of Administration and Finance shall develop a reconciliation template and incorporate this reconciliation into the Department's procedure manual.

Student Activity Funds

Comment

Subsequent to year-end, we completed an agreed upon procedures engagement related to the City's student activity funds and issued our report (RAUP) dated November 17, 2011. The RAUP contained various findings and recommendations related to internal control deficiencies we identified.

Implementation of some of the recommendations in the RAUP will require assistance from the City's finance team. In particular, we identified that student activity fund checking accounts are reimbursed through checks issued by the City. This process is administratively burdensome and inefficient. Checking account reimbursements should be processed through interbank transfers from the student activity agency account maintained by the City's Treasurer/Collector department.

Recommendation

We recommend the City's finance team assist the School Department with the recommendations identified in the student activity funds RAUP, including the implementation of procedures to process student activity checking account reimbursements through interbank transfers from the student activity agency account.

Management's Response

The Treasurer's Office has reviewed the independent auditors' suggestion, as well as its internal procedures, and shall commence depositing student activity account reimbursement checks on behalf of the School Department in lieu of processing said reimbursements through intra bank transfers.

Motor Vehicle Excise Tax Exemptions

Comment

In prior years, we evaluated the systems of internal control related to tax exemptions and abatements and identified two (2) deficiencies. One (1) of the deficiencies was resolved in fiscal year 2011. However, the following deficiency remains unresolved:

- Exemptions excluded from each motor vehicle excise tax commitment were reviewed and reconciled to the Assessor's database. However, the review and reconciliation process was not formally documented. Documented reviews of motor vehicle excise tax exemptions would provide evidence that the exemptions are appropriate and in compliance with MGL.

Recommendation

We recommend the City implement policies and procedures requiring documentation of the reconciliation and approval process for motor vehicle excise tax exemptions.

Management's Response

Commencing with the 1st Commitment of calendar 2012, the Assessing Division shall perform reconciliations of the exemptions granted for motor vehicle excise taxes issued by the City.

Accounts Receivable Reconciliations

Comment

At June 30, 2011, the following accounts receivable variances exist between the general ledger and Collector and departmental balances:

<u>Accounts Receivable</u>	<u>Variance</u>
Real estate taxes	\$ 44,976
Police off-duty details	40,849
Sewer user charges	23,666
Water user charges	11,622
Water liens	9,555
Sewer liens	4,323
Parking tickets	4,065
Tax liens	3,158
Special assessments	826
Fire off-duty details	257
Water backflow	246
Motor vehicle excise taxes	174
Personal property taxes	148

The City made significant improvements from fiscal year 2010 to fiscal year 2011 in reducing the variances in several accounts receivable balances.

While the variances identified above were immaterial to the City's audited financial statements, proper internal controls require accounts receivable to be reconciled timely to provide assurance that transactions have been properly recorded.

Recommendation

We recommend the City implement policies and procedures to investigate and resolve all variances between accounts receivable balances of the general ledger and Collector (and other departments) monthly.

Management's Response

As noted in the comment, the variances identified are immaterial in amount (four-tenths (4/10) of one percent) in relation to the City's financial statements. These variances are predominantly from prior fiscal years. During fiscal year 2011, the Treasurer's Office reduced the receivable variance by 16% from the previous fiscal year. In fiscal year 2012, the Treasurer's Office shall continue to identify the residual variances and adjust the City's records accordingly.

Authorized and Unissued Debt

Comment

At June 30, 2011, the City has several old borrowing authorizations for which debt has not been issued and the authorizations have not been rescinded. This matter was also reported in prior years' Management Letters.

As a frame of reference, the following table summarizes authorized and unissued borrowing authorizations greater than two (2) years old as of June 30, 2011:

<u>Fiscal Year of Loan Authorization</u>	<u>Authorized and Unissued Debt Balance</u>
1987	\$ 400
1994	230,000
1995	78,000
1996	330,500
1998	4,041,500
1999	2,000
2000	125,000
2001	1,060,000
2002	11,817,000
2003	885,688
2004	2,290,000
2005	6,115,000
2006	66,369,405
2007	99,605,000
2008	6,300,000
2009	12,570,000
Sub-total - Greater than 2 years old	\$ <u>211,819,493</u>
Total at June 30, 2011	\$ <u>325,336,993</u>
Percentage of total greater than 2 years old	<u>65.1%</u>

While some of the authorized and unissued debt identified above relates to projects the City is still planning to undertake (for example, a majority of the fiscal year 2006 authorized and unissued debt relates to the CitySquare project), there may be authorized and unissued balances for projects the City no longer intends to borrow money for. As an example, the authorized and unissued balances from fiscal year 1987 through 1999 (as identified above) remained unchanged from fiscal year 2010.

While the City is allowed to use old borrowing authorizations to fund new projects similar to the original purpose of the authorizations, the new projects might not meet the intent of the original authorizations.

Recommendation

We recommend the City implement policies and procedures to periodically review unissued borrowing authorizations and to rescind authorizations for projects the City no longer intends to borrow money for.

Management's Response

Loan orders and capital projects are not like general fund appropriations, which expire annually. Capital projects generally span multiple fiscal years and thus loan orders can generally be older than two years old. Although carrying authorized and unissued loans on the City's financial statements does not have adverse effects to the City's overall financial statements, the administration shall review all outstanding loan orders annually with the submission of the five year capital improvement program and will recommend rescissions of any loan order which it determines not be required.

City Clerk Financial Policies and Procedures

Comment

As identified in previous Management Letters, we identified that the City Clerk department (the department) does not maintain formal financial policies and procedure manual that detailed the financial operations of the department.

During fiscal year 2011, the department developed a draft financial policies and procedures manual. Subsequent to year-end, the department completed the manual.

Recommendation

We recommend the City's finance team review the department's manual for completeness and work with the department to finalize the manual for full implementation.

Management's Response

The Department of Administration and Finance has received, and will review the City Clerk's Procedure manual. Administration and Finance shall work with the City Clerk's Office and finalize the manual and place any recommendations into operation.