

TOWN OF LUNENBURG, MASSACHUSETTS

MANAGEMENT LETTER

JUNE 30, 2008



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To the Honorable Board of Selectmen
Town of Lunenburg, 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 Town of Lunenburg, Massachusetts' (the Town) as of and for the year ended June 30, 2008, 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.

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. However, as discussed below, we identified certain deficiencies in internal control that we consider to be material weaknesses.

A control deficiency 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 misstatements on a timely basis. A significant deficiency is a control deficiency, or a combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or a combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control. We believe that certain deficiencies described in the memorandum that accompanies this letter constitute material weaknesses.

We also became aware of other matters that are opportunities for strengthening internal controls and enhancing operating efficiency. The memorandum that accompanies this letter summarizes our comments and suggestions concerning those matters.

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

October 24, 2008

TOWN OF LUNENBURG, MASSACHUSETTS

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JUNE 30, 2008

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Material Weakness

RECONCILE ACCOUNTS TO SUPPORTING DOCUMENTATION

Prior Year Comment

In order to make the financial reports generated by the accounting system as meaningful as possible, the Town should reconcile the general ledger accounts for cash, and accounts receivable to supporting documentation on a monthly basis. A benefit of monthly reconciliations is that errors do not accumulate but can be identified and attributed to a particular period, which makes it easier to perform future reconciliations.

A cash reconciliation that reconciles from the Treasurer's balance to the general ledger balance should be prepared on a monthly basis to determine that all cash transactions have been recorded properly and to discover bank errors. Bank statements were not reconciled to the appropriate general ledger controls subsequent to October, 2007, which was completed by a consultant. As of June 30, 2008, there was an unreconciled amount of approximately \$50,000 between the Treasurer's balance and the general ledger balance. Not reconciling the accounts on a monthly basis means that errors or other problems might not be recognized and resolved on a timely basis. Also, it is generally easier and less time-consuming to reconcile accounts while transactions are fresh in mind.

Monthly bank account reconciliations are the primary internal control procedure relating to the Town's cash accounts. There was an unreconciled amount of approximately \$8,000 in the accounts payable checking account and \$2,000 in the payroll checking account. The payroll outstanding checklist had not been completed for any months subsequent to April, 2008. For the accounts payable checking account, the Treasurer's cash book balance was overstated by approximately \$152,000 because the Treasurer does not consider outstanding checks to be a reduction of the cash book balance.

The Collector's subsidiary ledger of accounts receivable has not been reconciled to the general ledger since March 2008. Such reconciliation is a primary means of preventing or detecting an error or fraud in accounts receivable. For example, one way to conceal a misappropriation of cash is to record a fictitious entry in the accounts receivable subsidiary ledger. A reconciliation of accounts receivable from the general ledger to the accounts receivable detail ledger should be prepared to check that the recording of transactions is accurate and proper and that any adjustments to or write-offs of accounts receivable have been approved.

Action Taken

The Town hired a consultant to establish policies and procedures that would enable the Town Accountant and Treasurer/Collector to complete monthly cash and accounts receivable reconciliations. The consultant was also hired to bring the account reconciliations up-to-date and reduce the existing backlog.

Current Status - Unresolved

Recommendation

We continue to recommend that all bank accounts be reconciled to the Treasurer's cash book and the general ledger each month prior to preparation of the monthly financial statements.

We also continue to recommend that a reconciliation of the Collector's detail to the general ledger accounts receivable control be made at the end of each month and that any reconciling items be investigated and cleared promptly. The Town Accountant should then review the reconciliation and satisfy herself that it is proper.

Prior Year Comments and Recommendations

FORMALIZE CONTROLS OVER DEPARTMENTAL RECEIPTS

Prior Year Comment

In the prior year, it was recommended that the Town establish formal policies and procedures for handling departmental receipts. The development of formal uniform policies and procedures will provide increased controls over departmental receipts. Without formal policies and procedures, mishandling of receipts can occur and not be detected in a timely manner.

Action Taken

No action was taken in fiscal 2008 to resolve this matter.

Current Status – Unresolved

REMOVE OLD OUTSTANDING CHECKS

Prior Year Comment

In the prior year, it was recommended that the Treasurer remove checks that have been outstanding for more than one year from the bank reconciliations. Maintaining these outstanding checks increases the effort to reconcile cash and reduces the Town's available cash.

Action Taken

No action was taken in fiscal 2008 to resolve this matter.

Current Status - Unresolved

CONTRACT OUT IMPREST ACCOUNT RECONCILIATIONS

Prior Year Comment

In the prior year, it was recommended that the Treasurer outsource the compilation of outstanding checklists for the payroll and vendor disbursement accounts. Most local governments with similar size payroll and vendor checking accounts have privatized this function with banks that offer this service at minimal or no cost.

Action Taken

During fiscal 2008, the Town outsourced the compilation of outstanding checklists for the vendor disbursement account; however the payroll outstanding checklist is still being maintained internally.

Current Status – Partially Resolved

ESTABLISH CASH AND INVESTMENT POLICES AND PROCEDURES

Prior Year Comment

In the prior year, it was recommended that the Treasurer establish written cash and investment policies that address investment objectives, types of investments permitted, length of investments, collateralization of funds, and monitoring cost versus market value. Formally documenting policies and procedures in written form will assist management with its fiscal goals, and define the Town's objectives to aid in assuring returns are maximized within the risk parameters established by the investment policies.

Action Taken

An investment policy was created during fiscal 2008; however it has not been formally adopted by the Board of Selectmen.

Current Status – Partially Resolved

IMPROVE CONTROLS OVER NON-TREASURER BANK ACCOUNT

Prior Year Comment

In the prior year, it was recommended that the Deputy Tax Collector fees be paid through the warrant process. Currently, the Deputy Tax Collector's fee and share of motor vehicle refunds are paid directly from a separate bank account and, therefore, bypass the warrant process.

Action Taken

No action was taken in fiscal 2008 to resolve this matter.

Current Status - Unresolved

ADOPT FORMAL STUDENT ACTIVITY POLICIES AND PROCEDURES

Prior Year Comment

In the prior year, we recommended that the School District address the following matters in its student activity fund policies and procedures:

- That all principals with check signing authority are required to provide bond to the Treasurer.
- That an annual audit of the funds is performed in accordance with the statute.
- That policies and procedures are developed for the recognition of student activities.
- That a requirement for periodic financial reports is formalized.
- That procedures are developed for fund raising events.
- That procedures are developed for the disposition of assets of inactive student activity organizations.
- That procedures are developed for the disposition of class accounts not closed out after graduation.

Action Taken

No action was taken in fiscal 2008 to implement these recommendations.

Current Status – Unresolved

IMPROVE TIMELINESS OF STATE CHAPTER 90 (HIGHWAY) REIMBURSEMENT REQUESTS

Prior Year Comment

In the prior year, it was recommended that the Town file for reimbursements of state Chapter 90 highway funds on a timely basis. During fiscal 2007, the Town incurred approximately \$40,000 of expenditures through October, 2006. The Town did not request reimbursement for these expenditures until May of 2007.

Action Taken

Reimbursement requests were submitted to the state on a timely basis during fiscal 2008.

Current Status - Resolved

WRITE-OFF UNCOLLECTIBLE AMBULANCE RECEIVABLES

Prior Year Comment

In the prior year, it was recommended that the Town actively pursue the collection of past-due ambulance billings or write them off. The existence of large past-due receivables impedes cash flow and, as time passes, increases the risk that these receivables will be uncollectible.

Action Taken

No action was taken in fiscal 2008 to resolve this matter.

Current Status – Unresolved

STATEMENT NO. 45 OF THE GOVERNMENTAL ACCOUNTING STANDARDS BOARD

Prior Year Comment

In July of 2004, the Governmental Accounting Standards Board (the GASB) issued Statement No. 45 *Accounting and Financial Reporting for Postemployment Benefits Other than Pensions*. This Statement improves the relevance and usefulness of financial reporting by (a) requiring a systematic, accrual-basis measurement and recognition of other postemployment benefits (OPEB) cost over a period that approximates employees' years of service and (b) providing information about actuarial accrued liabilities associated with OPEB and whether and to what extent progress is being made in funding the plan.

For financial reporting purposes, an actuarial valuation is required at least biennially for OPEB plans with a total membership (including employees in active service, terminated employees who have accumulated benefits but are not yet receiving them, and retired employees and beneficiaries currently receiving benefits) of 200 or more, or at least triennially for plans with a total membership of fewer than 200. The projection of benefits should include all benefits covered by the current substantive plan (the plan as understood by the employer and plan members) at the time of each valuation and should take into consideration the pattern of sharing of benefit costs between the employer and plan members to that point, as well as certain legal or contractual caps on benefits to be provided. The parameters require that the selection of actuarial assumptions, including the healthcare cost trend rate for postemployment healthcare plans, be guided by applicable actuarial standards. Failure to obtain an actuarial valuation will result in a qualification to the independent auditors' opinion on the basic financial statements.

Net OPEB obligations, if any, including amounts associated with under- or overcontributions from governmental funds, should be displayed as liabilities (or assets) in government-wide financial statements. Similarly, net OPEB obligations associated with proprietary or fiduciary funds from which contributions are made should be displayed as liabilities (or assets) in the financial statements of those funds.

An employer's net OPEB obligation is defined as the cumulative difference between annual OPEB cost and the employer's contributions to a plan, including the OPEB liability or asset at transition, if any. (Because retroactive application of the measurement requirements of this Statement is not required, for most employers the OPEB liability at the beginning of the transition year will be zero.) An employer with a net OPEB obligation is required to measure annual OPEB cost equal to (a) the annual required contribution (ARC), (b) one year's interest on the net OPEB obligation, and (c) an adjustment to the ARC to offset the effect of actuarial amortization of past under- or overcontributions.

This Statement generally provides for prospective implementation—that is, that employers set the beginning net OPEB obligation at zero as of the beginning of the initial year. The Town is required to implement this statement in fiscal 2009 although earlier implementation is encouraged.

We continue to recommend that management take a proactive approach to the planning and implementation of GASB Statement No.45. The most important consideration in the planning process is obtaining an actuarial valuation.

Action Taken

During fiscal 2008, the Town contracted with an actuary to perform the valuation. The report is expected to be completed during fiscal 2009.

Current Status – Partially Resolved

FRAUD RISK ASSESSMENT

Comment

In the prior year, we indicated that the opportunity to commit and conceal fraud exists where there are assets susceptible to misappropriation and inadequate controls to prevent or detect the fraud. To address this risk, we recommend that the Town perform a risk assessment to identify, analyze, and manage the risk of asset misappropriation. Risk assessment, including fraud risk assessment, is one element of internal control. Thus, ideally, the Town's internal control should include performance of this assessment, even though our annual financial statement audits include consideration of fraud.

The fraud risk assessment can be informal and performed by a management-level individual who has extensive knowledge of the Town that might be used in the assessment. Ordinarily, the management-level individual would conduct interviews or lead group discussions with personnel who have extensive knowledge of the Town, its environment, and its processes. The fraud risk assessment process should consider the Town's vulnerability to misappropriation of assets. When conducting the self-assessment, questions such as the following can be considered:

- What individuals have the opportunity to misappropriate assets? These are individuals who have access to assets susceptible to theft and to records that can be falsified or manipulated to conceal the theft.
- Are there any known pressures that would motivate employees with the opportunity to misappropriate assets? Pressures may relate to financial stress or dissatisfaction. In assessing whether these pressures may exist, the assessor should consider whether there is any information that indicates potential financial stress or dissatisfaction of employees with access to assets susceptible to misappropriation.
- What assets of the Town 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.

Action Taken

No action was taken to implement fraud risk assessment policies and procedures in fiscal 2008.

Current Status - Unresolved

FORMAL ACCOUNTING POLICIES AND PROCEDURES HANDBOOK

Comment

In the prior year, we noted that there are limited written policies and procedures for key administrative and financial functions of the Town. Because of the fact that there is a limited number of staff supporting key positions, a formal manual that identifies and documents key areas of administration and operations would reduce the risk to the Town in the event that personnel have extended absences.

Recommendation

We recommend that the Town document all key managerial functions in a manual that includes, among other items, 1) job descriptions; 2) daily, monthly, and yearly work procedures; and 3) other specific information relative to the function being documented.

Action Taken

No action was taken to develop a formal accounting policies and procedures handbook in fiscal 2008.

Current Status – Unresolved

IMPLEMENT A MONTH-END CLOSING SCHEDULE

Prior Year Comment

In the prior year, it was noted that the Town was unable to perform a monthly close out in a timely manner. The closing process can be delayed because some important procedures are not performed on time. As a result, there can be delays in producing closing entries, trial balances, schedules, reconciliations, account analysis, and other financial reports needed by management.

We believe that the month-end closing could proceed more quickly by developing a closing schedule that indicates who will perform each procedure and when completion of each procedure is due and accomplished. The timing of specific procedures could be coordinated with the timing of management's need for the information. The due dates could be monitored to determine that they are being met.

Action Taken

No action was taken to document a month-end closing schedule in fiscal 2008.

Current Status – Unresolved

RECONCILE THE GENERAL LEDGER BETTERMENTS BALANCE WITH THE SUBSIDIARY LEDGER

Prior Year Comment

In the prior year, it was noted that the Town's detailed accounts receivable records for sewer betterments did not agree with the general ledger control accounts by approximately \$636,000. As of June 30, 2008 the difference was \$662,000. The difference was due to adjustments to specific customer accounts that were not recorded in the general ledger but were reflected in the detailed customer accounts. It is important that management determine the underlying reason for the difference and take steps to correct current procedures as deemed necessary. In addition, management should develop procedures to ensure that differences are identified, researched, and resolved on a timely basis.

Action Taken

The Town Accountant completed an analysis identifying the majority of the discrepancies in the accounts as of June 30, 2007; however the corrections were not posted to the general ledger as of June 30, 2008.

Current Status – Partially Resolved

Current Year Comments and Recommendations

TRUST FUNDS

Comment

The Treasurer receives the trust fund bank statements on a quarterly basis. We noted a variance between the balance maintained by the Treasurer and the balance maintained by the bank at fiscal year-end totaling approximately \$9,200.

Additionally, the Treasurer is not making the necessary transfers between pooled cash and the trust funds for trust expenditures and income. The Town Accountant has reflected these amounts as due to/due from other funds on the general ledger. The Treasurer should initiate these transfers at the same time that the Town Accountant updates the general ledger so that both general ledger and cash book balances will be in agreement.

Recommendation

The Treasurer should implement policies and procedures for managing trust fund activity and begin to reconcile the activity with the general ledger and bank statements on a quarterly basis.