

Conor Baldwin
Chief Financial Officer

MEMORANDUM

TO: Eileen M. Donoghue, City Manager *EMD*

FROM: Conor Baldwin, Chief Financial Officer *CB*

CC: Bryan Perry, City Auditor
Finance Department

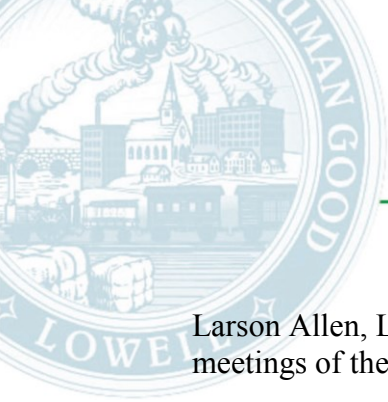
DATE: April 29, 2019

RE: FY2018 Audit – Management Letter response from Finance Department

The City Auditor, Superintendent of Schools, and I—on behalf of the finance department—have signed off on release of the final versions of Lowell’s outside audit of the FY2018 financials. The final versions of those documents: the FY2018 Basic Financial Statements, Reports on the FY2018 Federal Awards Programs, and the FY2018 Management Letter constitute the work product of our annual engagement with the outside audit firm, Powers & Sullivan. Each year, the city through the City Auditor’s office, regularly engages the services of a contracted outside audit firm to conduct testing of the city’s financial activity for the year, prepare the city’s basic financial statements, and provide commentary on the strength of the city’s internal controls over fiscal activities for the most recent year. The result of this year’s work is enclosed under the City Auditor’s portion of the Agenda. In keeping with the City Council’s key priority area of strong financial management, this memorandum is intended to serve as a supplemental, informational item from the finance department intended to respond to comments made by the audit firm and demonstrate the action plan for strengthening internal controls in the coming year.

Due to the various issues in the school department which occurred in FY2018, but came to light after the close of the fiscal year; the release of these reports was later than normal this year. Additionally, Powers & Sullivan noted a number of processes/ internal controls in the school department’s business office which have risen to the level of a “*material weakness*” on the management letter. A material weakness is a deficiency—or a combination of deficiencies—in internal controls such that there is a reasonable possibility that a material misstatement of the city’s financial statements will not be prevented or detected and corrected on a timely basis. The Management Letter, a standard component of each year’s annual audit process, typically highlights areas of improvement for management to strengthen internal controls over financial matters, but a material weakness is something which requires immediate attention.

The City Council and the School Committee were first made aware of these same issues through the publication of an additional, directed audit performed by the private audit firm, Clifton



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Larson Allen, LLP, and publicly released in December of FY2019. Through a series of joint meetings of the City Council's and School Committee's respective finance subcommittees, these

issues were discussed and the business office at the school has since submitted a corrective action plan to pay back the fund approximately \$2.1 million and resolve the matter. A copy of that plan is enclosed with this memorandum, for your records.

The implications of this material weakness on the city's financial standing primarily relate to future audit work necessary. The deficiency in internal controls and corrective action plan are noted on the audit of federal award programs ("SEFA") and will warrant more extensive audit work by our outside auditors in the future. As such, next year's SEFA will require an expanded scope of work and additional cost. Limitations on testing are directly affected by an audit firm's comfort level with the client and as a "high risk" client, additional testing will be necessary to produce an opinion by the audit firm.

Because this deficiency in the school department's financial controls has risen to the level of a material weakness, the finance department would advise that the matter be referred to a joint finance subcommittee of the School Committee and the City Council. The business office in school central administration has made progress in addressing many of the outstanding issues identified in this and the Clifton Larson Allen ("CLA") audit, and the Business Manager can update the body on further progress in resolving these deficiencies. The ability of the City Manager and the City Council to address these matters is limited by the authority granted to the School Committee over budgetary matters by Chapter 70 of the Massachusetts General Law, but as a practical matter, the city's finance department has an obligation to participate in ensuring their resolution, if only in an advisory role. Members of finance department stand ready to assist with whatever assistance may be required to address any and all issues in the school department.

The following comments were resolved during FY2018. Please refer to the June 30, 2017 Management Letter (FY2017) for the complete original comment.

1. Parking Ticket Receivables.
2. Treasurer's Cash Draw Over/ Under Policy
3. Tax Foreclosures

The following pages represent the finance department's response and corrective action plan for each of the comments listed on the FY2018 Management Letter as new and/or unresolved.



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Prior Year Comments

1. Cash Reconciliation Procedures

DEPARTMENT:

Office of the Treasurer/ Collector

CURRENT STATUS:

During 2018, the City's interim Treasurer resigned which resulted in incomplete cash reconciliation for 2018. Subsequent to June 30, 2018, the City has hired a Treasurer who began to reconcile the accounts with immaterial variances. Reconciliations are almost up to date, and remaining variances are being identified and corrected. The City expects that these procedures will be implemented in 2019 and that this comment will either be cleared entirely.

MANAGEMENT RESPONSE:

As the status from the management letter states, the former Treasurer has since resigned and the new Treasurer, who has a wealth of experience in private accounting and management as a Treasurer in a comparable sized Massachusetts municipality, has taken immediate steps to utilize the full newly implemented MUNIS module to its full capabilities, as well as make improvements to the process of monthly reconciliation, overall. The importance of resolving this comment has been stressed to the new Treasurer as the finance department's top priority for FY2019.

The treasury staff has become more comfortable with the new technological enhancements and using the MUNIS module as the cashbook. The Treasurer is currently reviewing and implementing the recommendations of the consultant. In addition, the following procedural enhancements have been proposed by the Collector's Office and approved to be implemented immediately. These improved procedures will also improve the handling of cash and the overall reconciliation process with the Treasury.

Revised cash handling policies are the central component of the Collector's contribution to the cash reconciliation process. On occasion, there are discrepancies with the tellers concerning the balance of cash received from customers for payments regarding Real Estate, Personal Property, Excise Tax, and Parking Tickets. While this issue is not affecting the customer's accounts, it is important to always adapt and improve in order to minimize any issue.



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2. School Grant Management

DEPARTMENT(S):

School Department Business Office

CURRENT STATUS:

During 2018, significantly fewer funds were sent back [than in FY2017]. A total of \$118,000 of grant proceeds was returned at the end of fiscal year 2018. Management should continue to review the grant programs and work to assure that the maximum benefits are being derived from all grant funds received and determine what the underlying reasons for needing to return funds each year are and if any changes are deemed necessary.

MANAGEMENT RESPONSE:

Early in FY2018, the city's finance department, including the City Auditor, communicated this issue with the School Business Office. Senior staff turnover in the school department's senior management delayed resolution to this issue, but the matter will again be communicated to the School Business Manager for resolution in FY2019.

3. SECTION 108 LOAN FUND

DEPARTMENT(S):

Department of Planning and Development ('DPD')

CURRENT STATUS:

Procedures were implemented to ensure when the debt payments are made the liability balance is adjusted accordingly. No determination of the nature of the cash balances maintained within these funds was determined during 2018.

We continue to recommend that management determine the nature of the cash balances in these funds and determine the proper disposition of these balances.



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MANAGEMENT RESPONSE:

The city's finance department has already begun to work with the Deputy Director of Planning and Development to identify the original source and intended use of these funds. It is anticipated that, after additional research, and ultimate disposition of the remaining funds will be determined. The city will either expend the funds on an eligible purpose or transfer the remaining balance to the general fund to close to free cash.

4. Purchase Order Dates

DEPARTMENT(S):

All Departments (Including Schools)

CURRENT STATUS:

We noted that there are still purchase orders with dates prior to the invoice date.

We continue to recommend that a policy regarding the approval of purchase orders prior to the purchase of goods or services by any Department be implemented.

MANAGEMENT RESPONSE:

The finance department takes this issue very seriously. Adherence to the city's existing financial policies and procedures is a critical component of good fiscal management. The city has a strong local, legal framework for procuring goods and services, found in the Code of Ordinances (Chapter §28-32), which requires Department Heads to wait for a purchase order award before procuring any goods or services.

Management will disseminate reminders to all department leadership and underscore the importance of following proper procedures. The finance department and, specifically the Purchasing Department, will also work with departmental project managers and finance staff to train them in the appropriate best practices. The city's MUNIS accounting system provides excellent workflow procedures to guarantee the process is followed to a certain extent, but it cannot eliminate human error.

Revised policy reminders and training schedules will be released in FY2019 to appropriate staff and the city anticipates this comment on the management letter will be resolved next year.



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5. Late Invoices

DEPARTMENT(S):

All Departments (Including Schools)

CURRENT STATUS:

During the current year review of invoices, we noted there are still several invoices that are months old being paid after fiscal year end. Also, please see the material weakness section at the beginning of this document regarding the School Department invoices.

MANAGEMENT RESPONSE:

While this response is partially directed at School Department operations and could be discussed further in a joint meeting of the City Council and School Committee finance subcommittees, the finance department has already reiterated to Department Heads the city's policies for year-end procedures and the need to adhere to existing ordinances and policies regarding timely submission of invoices to the City Auditor. This discussion will be followed up with additional written communication to Department Heads and periodic training for their financial staff throughout the end of FY2019 and into FY2020.



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CURRENT YEAR COMMENTS

1. Compensated Absences for the School Department

DEPARTMENT(S):

School Department

MANAGEMENT RESPONSE:

This matter will be referred to the School Central Administration to be addressed. The finance department and the Office of the City Auditor will work to ensure compliance.

2. Documentation of Internal Controls

DEPARTMENT(S):

Finance/ City Auditor

MANAGEMENT RESPONSE:

The City Auditor has already begun to compile a document of all internal controls and we expect this issue to be resolved by the next year's audit.