

MANCHESTER ESSEX REGIONAL SCHOOL DISTRICT

MANAGEMENT LETTER

JUNE 30, 2013

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To the Honorable School Committee
Manchester Essex Regional School District
Manchester-by-the-Sea, Massachusetts 01944

In planning and performing our audit of the basic financial statements of the Manchester Essex Regional School District as of and for the fiscal year ended June 30, 2013, in accordance with auditing standards generally accepted in the United States of America, we considered the Manchester Essex Regional School District's internal control over financial reporting 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 Manchester Essex Regional School District's internal control. Accordingly, we do not express an opinion on the effectiveness of the Manchester Essex Regional School District's internal control.

However, during our audit we became aware of other matters that we believe represent opportunities for strengthening internal controls and operating efficiency. The memorandum that accompanies this letter summarized our comments and suggestions concerning 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 District 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.

The District's written response to the matters identified in our audit has not been subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

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.

A handwritten signature in black ink that reads "Powers & Sullivan, LLC". The signature is written in a cursive, flowing style.

March 14, 2014

MANCHESTER ESSEX REGIONAL SCHOOL DISTRICT

MANAGEMENT LETTER

JUNE 30, 2013

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Fraud Risk Assessment

Prior Year 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 recommended that the District 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 District'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 District 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 District, its environment, and its processes. The fraud risk assessment process should consider the District's vulnerability to misappropriation of assets.

Current Status

Over the past several years, the District has assessed risk in several key areas and has implemented changes to roles and responsibilities, systems, and processes and procedures to reduce the identified risks to what management believes is an acceptable level. We commend the District for the improvements that have been to address the identified risks. Some of the changes include improved segregation of duties for accounting and Treasury functions, improved segregation of duties and better control over changes to the payroll and vendor master files, more timely reconciliation of cash and bank accounts, and management is currently in the process of implementing an integrated cash management system.

Continuing Recommendation

We continue to recommend that the risk assessments and mitigating controls be documented and submitted to the school committee for review and approval. This will ensure that the school committee members are aware of the risks and are in agreement with the level of mitigating controls that are in place to reduce the risks to an acceptable level.

Management Response

Management's approach has been to identify key processes that individually pose the largest potential for fraud risk and to upgrade related procedures as needed to ensure that appropriate checks and balances are in place. In addition to improvements referenced above, management continues to invest considerable resources into ongoing improvement of Student Activity fund oversight. Improving documentation of incoming receipts is another area that is currently being revamped as noted below.

Written Job Descriptions

Prior Year Comment

In the prior year, we indicated that management has completed job descriptions for new employees and restructured positions; however job descriptions were not completed for all other financial positions.

Job descriptions will not only allow management to understand what is being performed by every person in the District, but will also serve as a guideline for anyone who subsequently replaces an existing position. Additionally, District policies and procedures will be further defined through this process. This process should also ensure segregation of duties so that the same employee is not initiating, recording, and approving transactions and handling related assets. Employees should then be assigned to the position best fitting their qualifications. Job descriptions provide a guideline to the employees of the responsibilities they are expected to perform. Without written guidelines, employees must assume what management desires. Having written, formal guidelines helps ensure appropriate communication of expectations.

Current Status

Management has completed job descriptions for new employees and restructured positions; however job descriptions have not been completed for all other financial positions.

Continuing Recommendation

We continue to recommend that the District complete the preparation and issuance of written job descriptions for all financial personnel. As part of this process, we also recommend that the District review the current positions to determine whether the appropriate tasks are being performed by the appropriate position. The District should then document the significant assignments of each position.

Management Response

The management team will develop a process for reviewing and developing job descriptions to be approved by School Committee.

Adopt a Cash and Investment Policy

Prior Year Comment

In the prior year, we indicated that new accounting standards have highlighted the need for governmental entities to consider adopting cash and investment policies that take into account custodial, credit and interest rate risk. Such policies establish guidelines for matters such as 1) the types of banks the District should have deposits with; 2) the maximum period that an investment can be held and; 3) the highest concentration the District can have in any one investment type or issuer.

Current Status

We are not aware of any action that was taken in fiscal 2013 to resolve this matter.

Continuing Recommendation

We continue to recommend that the District develop and formalize a cash and investment policy that includes both long and short-term objectives.

Management Response

The School Committee recently voted to establish a trust for funding Other Post Employment Benefits (OPEB) and has included an initial deposit into the fund in the fiscal 2015 budget. Management has discussed the need to create an investment policy to govern use of these and other funds with the School Committee and intends to formalize a policy in the coming months.

Financial Policies and Procedures Manual

Prior Year Comment

In the prior year, we indicated that the District does not maintain a written policy and procedures manual documenting the District's financial goals and objectives. A formal policy and procedures manual will establish benchmarks for excess and deficiency, fund balance levels, a long-term capital and debt plan, and other important financial indicators. Other policies that should be included in this manual include purchase order requirements, and allowable use of District credit cards.

These policies and procedures will provide a framework for management to utilize when making important financial decisions.

Current Status

We are not aware of any action that was taken in fiscal 2013 to resolve this matter.

Continuing Recommendation

We continue to recommend that the District develop a written financial policies and procedures manual. This document should be updated for any new policy changes that are put into effect. A master manual of all procedures should be maintained and stored in a secure location.

Management Response

The District has documented policies and procedures for many key areas of its financial operations, but has not yet formally gathered such documents into a published master manual.

Cash Receipt Postings

Prior Year Comment

In the prior year we indicated that there are certain departments of the District who are currently responsible for depositing their own cash receipts in the bank, such as the school lunch program. Once deposited the department is responsible for providing the central office with documentation to support the deposit.

Often times there have been instances in which the departments have not provided the central office with supporting documentation in a timely manner, which has resulted in the central office posting the receipt to the general ledger based on the amount deposited in the bank. Using bank information to post amounts to the general ledger is not a good internal control as it does not provide a “check and balance”, or corroboration, of information from two different sources.

Current Status

We are not aware of any action that was taken in fiscal 2013 to resolve this matter. However, it is our understanding that significant actions were taken subsequent to year-end to address this comment and recommendation. Please see management’s response below for further discussion of the procedures that have been put in place.

Continuing Recommendation

We continue to recommend that the District develop procedures to ensure that the turnover of adequate receipt documentation by the departments occurs in a timely manner. We also recommend that receipts not be posted to the general ledger until the supporting documentation has been received.

Management Response

The District has recently upgraded documentation considerably for cash receipts. Turnover sheets are now collected for 100% of Student Activity deposits and retiree payments for health insurance. In addition, the Athletics department now photocopies all checks received and shares its tracking sheet of these receipts with the central office for reconciliation to the General Ledger. Management is now in the process of creating a similar system of documentation for the Food Service department.

Future Government Accounting Standards Board (GASB) Statements for Pensions and OPEB

Informational Comment

The GASB has issued new pronouncements that will significantly affect the accounting and reporting requirements for Pensions and Other Postemployment Benefits (OPEB). These new standards will start to phase in during fiscal year 2013 and will substantially impact the District’s financial statements and will also affect the requirements for accumulating the necessary data to meet the reporting requirements.

The new standards that have been issued and their effective dates are as follows:

- The GASB issued Statement #65, Items Previously Reported as Assets and Liabilities, which is required to be implemented in fiscal year 2014.

- The GASB issued Statement #67, *Financial Reporting for Pension Plans*, an amendment of GASB Statement No. 25, which is required to be implemented in fiscal year 2014.
- The GASB issued Statement #68, *Accounting and Financial Reporting for Pensions*, an amendment of GASB Statement No. 27, which is required to be implemented in fiscal year 2015.

The GASB is expected to issue additional standards following #67 & #68 for Pensions, which will similarly affect accounting and financial reporting for OPEB Plans. The GASB is encouraging earlier application of these standards. See below for a brief summary of these new standards:

- GASB #65 will require reporting each of the financial position elements in a separate section in the statements of financial position. These elements are Assets, Deferred Outflows, Liabilities, Deferred Inflows, and Net Position; where assets + deferred inflows – liabilities – deferred outflows = net position. This new requirement will affect certain aspects of the financial statements currently and will pave the way for the new reporting requirements of the new Pension and OPEB standards.
- GASB #67 and #68 will substantially change the reporting for pension liabilities and expenses. Changes in pension liability will be immediately recognized as pension 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. Current actuarial methods may continue to be used to determine funding amounts. Employers will report in their financial statements a *net pension liability (asset)* determined annually as of the fiscal year end. *Net pension liability (asset)* equals the total pension liability for the plan net of the plan net position. Pension liability is the actuarial present value of projected benefits attributed to past service, and plan net position is the accumulated plan assets net of any financial statement liabilities of the plan.

The District should expect to record significant pension and OPEB liabilities in the future.

Recommendation

While the most significant changes from these GASB's go into effect in FY2014 and FY2015, we wanted to make the District aware of the magnitude that these changes will have on financial statement reporting and disclosures. The District should plan to meet with your actuaries and financial advisers as more information becomes available. You may also want to consider how and when this information should be communicated to financial statement users.