

MANCHESTER ESSEX REGIONAL SCHOOL DISTRICT

MANAGEMENT LETTER

JUNE 30, 2012

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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, 2012, 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.

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.

Our consideration of internal control was for the limited purpose described in the first paragraph and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control that we consider to be material weaknesses, as defined above.

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 summarized 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.

March 22, 2013

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MATERIAL WEAKNESS (Resolved)

Reconcile The General Ledger Cash Balances To The Treasurer's Balances

In our previous management letter we addressed several matters related to internal controls over cash and the relationship between the accounting function and treasury function in assuring that adequate internal controls are in place. We specifically addressed concerns over:

- The reconciliation of the general ledger cash balances to the Treasurer's cash balances,
- The fact that for several years the payroll bank account has had significant and unsupported reconciling item,
- That the Treasurer's procedures for funding payroll warrants were inadequate and, in several instances, resulted in an estimated amount be used to fund the payroll warrant versus an actual amount,
- That a year's worth of transaction of the student activity bank account was not posted in a timely manner (it was done after year end).

Current Status

During FY2012 management implemented procedures to substantially improve all the material weaknesses noted above. Cash accounts were reconciled throughout the fiscal year in a timely manner, the payroll process was redesigned, reconciling items were identified and resolved, and transactions of the student activity account were posted in a timely manner. We deem the prior material weakness to be resolved.

PRIOR YEAR COMMENTS

Withholding Accounts

Prior Year Comment

In the prior year, we indicated that the payroll withholding liability accounts were not reconciled on a monthly or quarterly basis. The balance in each withholding liability account should represent amounts withheld from employees but not yet paid out. This is usually one week to one month worth of withholding, depending on the type of withholding. These accounts should be reconciled on a regular basis to ensure that all withholdings are being paid out and charged to the appropriate withholding account.

Current Status

The District has hired a human resource and financial data specialist who, in addition to processing payroll and working on other payroll related issues, has been auditing employee withholdings against plan enrollment to ensure that proper withholdings are being made. The District has also established procedures to reconcile the withholding accounts. We consider this comment to be resolved.

Reconcile Student Activity Funds

Prior Year Comment

In the prior year, we indicated that the District is required to maintain its student activity funds in a manner that is mandated by Massachusetts General Law, Chapter 71, Section 47 of the Acts of 1996. The student activity accounts should be used exclusively to account for student activity funds. The raising and expending of activity money by student bodies should have but one purpose: to promote the general welfare, education and morale of all students through the financing of the normal legitimate co-curricular activities of the student body operation.

In reviewing current policies and procedures we noted that the elementary student activity bank accounts are not reconciled with the elementary school student activity records.

Current Status

In FY2012, through the assistance of an outside consultant, the District implemented procedures to reconcile the student activity accounts. We consider this comment to be resolved.

Audit of Student Activity Funds

Prior Year Comment

In the prior year, we indicated that the Massachusetts Association of School Business Officials (MASBO) published a student activity accounts manual, in May of 2007, to assist school districts with the operation and management of student activity accounts under the provisions of Massachusetts General Law (MGL), Chapter 71, Section 47, as amended by Chapter 66 of the Acts of 1996. To comply with the MGL, the MASBO recommends that annual audits of the student activity funds be performed. The audit may be an internal audit conducted by the Director of Finance and Operations, if so approved by the School Committee. However, at least one time every three years, the audit should be performed by an independent audit firm.

Current Status

In FY2013 the District contracted with an independent accounting firm to have an agreed upon procedures engagement for student activity funds that is in compliance with MASBO guidelines. We consider this comment to be resolved.

Centralize Chapter 30B Compliance Information

Prior Comment

Chapter 30B compliance information for some purchases has been maintained by the Facilities Office and not centrally within the District Office. The Director of Finance and Operations monitors Chapter 30B compliance when approving purchase orders.

Current Status

The District has moved all compliance documentation to the central office account payable files. We consider this comment to be resolved.

Segregation of Duties

Prior Comment

During our audit of the District's cash balances, we noted that a segregation of duties within the payroll and accounts payable functions was lacking. It is crucial in a system of internal control for no one employee to be able to complete a transaction from start to finish. Currently, the payroll clerk is responsible for processing the biweekly payroll, has access to and issues manual checks, as well as has access to the Treasurers signature stamp which is loaded into the payroll system. The accounts payable clerk has the ability to enter new vendors into the master file, process invoices, and post transactions directly to the general ledger.

Current Status

The District has made process modifications to prevent individual employees from completing transactions from start to finish. New employees and vendors may no longer be added into the software systems without approval from the Director of Finance & Operations. We consider this comment to be resolved.

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

The District conducted an outside-party review of various Business Office functions and practices, which included some feedback on fraud prevention measures.

Continuing Recommendation

We continue to recommend that management develop and implement a fraud risk assessment program to identify, analyze, and manage the risk of asset misappropriation.

Management Response

As noted previously, management has contracted with an independent accounting firm to have an agreed upon procedures engagement for student activity funds. As part of this review, the accounting firm will be examining procedures for safeguarding cash receipts and monitoring appropriateness of disbursements. Management has also requested that a similar analysis of cash management be conducted as part of its fiscal 2013 audit for the athletics and food service program, which also process significant incoming receipts each year. Through these steps, management hopes to make significant progress towards completing a fraud risk assessment in fiscal year 2013.

Establish a Program for Evaluating Employee Performance

Prior Year Comment

In the prior year, we indicated that the District does not have a prescribed standard or written record for measuring, evaluating, and reporting employee performance. It has been demonstrated that individuals generally accomplish more and work better as a team when they fully understand their responsibilities and have a common agreement with their superiors about the job objectives and performance standards on which they will be evaluated.

Current Status

The District's management has completed the implementation of performance reviews. Job descriptions have been created for new employees and restructured positions.

Continuing Recommendation

We continue to recommend that the District complete the preparation and issuance of written job responsibilities for all personnel.

Management Response

Responsibility for creation of additional job descriptions has been assumed by the School Committee of the Regional School District.

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 - No significant progress was made in fiscal 2012 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

Management has begun research into policies developed by other government entities and will endeavor to complete work on this item in fiscal 2013.

Assess Organizational Structure/Roles and Responsibilities

Prior Year Comment

In the prior year, we indicated that the Director of Finance and Operations duties include, among other things, general ledger account reconciliations, recording and posting journal entries to record payroll on the general ledger, recording and posting monthly adjusting entries to the general ledger, reviewing vendor warrants prior to the posting to the general ledger, completing monthly and year-end closing procedures and account reconciliations. In our experience, many of these accounting functions are typically performed by an accountant and are not part of the Director of Finance and Operations primary roles and responsibilities.

We believe that the District should assess the role and responsibilities being performed by the Director of Finance and Operations and consider adding an accountant's position to the organizational structure. The accountant would perform the accounting functions that are currently assigned to the Director of Finance and Operations. This organizational structure would bring the accounting staff inline with similar sized school Districts, would increase the controls over the District's accounting functions, and would be an additional resource for management by providing them with budgets, analyses, and other reports that could be useful in making decisions.

Current Status

The District has hired a human resource and financial data specialist to assist with Business Office responsibilities, including account reconciliations. This position was subsequently modified to include processing payroll and drafting payroll-related general ledger entries for the Director of Finance & Operations.

Continuing Recommendation

We continue to recommend that the District further assess the current roles and responsibilities being performed by the Director of Finance and Operations and consider reassigning them to other positions within the business office while being mindful of proper segregation of duties.

Management Response

Organizational needs continue to evolve in the business office as a result of ongoing upgrades to financial management and internal control procedures. As new procedures become routine, it is expected that greater clarity will emerge with regard to the most efficient way to divide tasks between various office staff. Management will endeavor to resolve this matter in fiscal 2013.

CURRENT YEAR COMMENTS

Financial Policies and Procedures Manual

Comment

The District does not currently 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 E&D, 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.

Recommendation

We 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.

Cash Receipt Postings

Comment

There are certain departments of the District who are currently responsible for depositing their own cash receipts in the bank, an example being the school lunch program. Once deposited the department is responsible for providing the central office with adequate documentation to support the receipts.

Often times there have been instances in which the departments have not been providing the central office with supporting documentation in a timely manner, which has resulted in receipt postings to the general ledger being based on the amounts deposited per the bank statement.

Recommendation

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

INFORMATIONAL COMMENTS

Other Postemployment Benefit Actuarial

Informational Comment

For financial reporting purpose, 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 total membership of fewer than 200.

For the District to remain compliant with GASB Statement #45, the District must obtain an updated actuarial valuation that would be dated July 1, 2012, and will be used for the fiscal 2013 and 2014 audits.

Recommendation

We recommend that the District work with their actuarial firm to assure that any updated information they may need to update the report is provided in ample time for the fiscal year 2013 audit.

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 your 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 #63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, which is required to be implemented in fiscal year 2013.
- 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.