

***CITY OF SALEM, MASSACHUSETTS***

***MANAGEMENT LETTER***

***JUNE 30, 2006***



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To the Honorable Mayor  
and Members of the City Council  
City of Salem, Massachusetts

In planning and performing our audit of the basic financial statements of the City of Salem, Massachusetts, for the fiscal year ended June 30, 2006, we considered the City's internal control in order to determine our auditing procedures for the purpose of expressing our opinion on the City's basic financial statements and not to provide assurance on internal control.

However, 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 concerning those matters.

This letter does not affect our report dated September 29, 2006, on the basic financial statements of the City of Salem, Massachusetts.

The accompanying comments and recommendations are intended solely for the information and use of management of the City of Salem, Massachusetts, and are not intended to be and should not be used by anyone other than these specified parties.

We will review the status of these comments during our next engagement. We have already discussed these comments and recommendations with various City personnel, and we will be pleased to discuss them further at your convenience, to perform any additional studies of these matters, or to assist you in implementing the recommendations.

A handwritten signature in cursive script that reads 'Powers + Sullivan'.

September 29, 2006

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# ***Previous Year's Comments***

## **RESOLVED**

### **Budget Process**

We noted in last year's management letter that the City's practice for managing the general operating budget had been to budget less than the anticipated amounts required to operate the City and to adjust the budget once the fiscal year was underway as additional revenue sources (i.e. free cash) became available. This catch-up budgeting practice put undue pressure on management to find additional revenue sources to fund known recurring line item appropriations.

We recommended that the City establish an initial operating budget that encompassed all anticipated operating costs which could be funded with known recurring revenue sources. The only adjustments that should be made during the fiscal year would be in response to unforeseen variances or events and not as a part of the normal operating procedures. We also recommended that budgeting policies be adopted which would limit the use of non-recurring revenues to finance non-recurring expenditures and not to fund the general operating budget of the City.

### **Status**

*Resolved* - During the fiscal year 2007 budget process, the City implemented a budget which encompasses all anticipated operating costs to be funded with known recurring revenue sources.

### **Allocation of Sewer Costs to the Water Fund**

Last year's management letter noted that the City's water and sewer activities are maintained as individual enterprise funds, where the City charges rates to users to offset the cost of providing the corresponding services. The largest expense for each fund is the annual assessment from the Beverly-Salem Water District charged to the Water Enterprise Fund and the assessment from the South Essex Sewerage District (SESD) charged to the Sewer Enterprise Fund.

From fiscal year 1997 through fiscal year 2005, 11% of the SESD sewer charges were allocated to the Water Fund. Over this period of time \$6,375,990 of sewer assessments were charged to the Water Fund, for an average of \$638,000 per year. The SESD assessment is entirely related to sewer services. In fiscal year 2005, the City was unable to provide documentation to support this allocation of costs between funds.

The effect of this budgeting practice had overcharged water users and undercharged sewer users without apparent cause.

We recommended that the City document the rationale for charging sewer assessments to the water fund. If the charge was arbitrary, then they should have discontinued it immediately. We also recommended that the City evaluate the impact of past practices and determine if an adjustment was appropriate.

### **Status**

*Resolved* - The City discontinued this practice in fiscal year 2006 and the SESD assessment was entirely charged to the Sewer Fund.

## **Revenue Enhancements**

In the prior fiscal year, we noted that part of the solution to the City's structural deficit could come from increased revenues. Revenue enhancement could come in the form of increased collections of amounts already due, new fees, new grants and contributions, increased rates for fees and licenses, payment in lieu of tax agreements, internal control changes to current operations and other initiatives. The City did not have a policy that required the periodic review of collection procedures, timing of requests for reimbursements, rate structure for fees, loss of potential revenues due to policy or controls, or new revenues.

We suggested that the City could benefit through the evaluation of potential new or increased revenue sources and an expedited collection process as a means for addressing financial shortfalls.

### Status

*Resolved* - Several new policies were implemented during fiscal year 2006 to enhance revenues for the City. For example:

The City's unpaid tax lien account has decreased by approximately \$854,000 from the foreclosure of properties and an increased dedication to collection process.

The Parking Department increased its hours of operation for the parking garage and the Church Street lot to 8 P.M. They also implemented Saturday meter collection/enforcement and installed seasonal meters at Salem Willows Recreational Park. The annual revenue from the implementation of Saturday meter collections and the seasonal meters is estimated to be approximately \$100,000.

Effective September 2006, the City implemented a trash fee. The revenue generated from the trash fee is anticipated to be \$700,000 for the ten months of collections during fiscal year 2007 and \$840,000 a year for the twelve months of collections in future fiscal years. These amounts are based on the number of residential and commercial units that are currently being billed for trash. The fees collected are being used to offset the cost of collecting solid waste.

## **Recording Revenue on the Budgetary Basis of Accounting**

The Department of Revenue requires accounts receivable to be deferred at year end except for real and personal property taxes collected within 60 days of year-end and certain revenues specifically identified by them in a year-end closing memo. In the previous years management letter we noted several receivable balances that were not deferred on the City's general ledger at year end. This practice resulted in an overstated budgetary fund balance and could have lead to errors when free cash was certified.

We recommended that the City fully defer all receivables on the general ledger until the funds have been received.

### Status

*Resolved* - The City fully deferred all receivables on the general ledger in fiscal year 2006.

## **Timeliness of CDBG Drawdowns**

### Comment

The City operates a Community Development Block Grant (CDBG) from the U.S Department of Housing and Urban Development (HUD). The City's policy is to request grant funding from HUD on a weekly basis sufficient to cover expenditures made from the grant for that same week. Due to a staffing shortage in the Planning Department, the City was unable to request funds from HUD in a timely manner at various times throughout the fiscal year. This resulted in the CDBG fund operating in a significant cash deficit, which was subsidized by the City's general fund operating cash. Therefore, the City's general operating fund has less cash available to meet ongoing needs and the City is earning less investment income to support the City's operating budget.

We recommend that the City's Planning Department take steps to ensure that CDBG funds are requested on a timely basis.

### Status

*Resolved* – The City's Planning Department is now requesting funds on a weekly basis.

## **City Council Meeting Minutes**

Last year's management letter noted that the City was unable to produce approved, transcribed City Council meeting minutes for the period of July through December of 2004 and July through October of 2005. In lieu of actual certified minutes, we were provided with photocopies of notes from the time period specified. The Commonwealth of Massachusetts Public Records Law G.L.c.66 § 3-9, requires that a governmental body eventually put its minutes into a written form. Without establishing a strict policy regarding the timeliness of the preparation of "official" minutes, the Attorney General's Office has stated that a time frame of two to four weeks may be considered reasonable under most circumstances. City Council meeting minutes are important public documents that create a historical record of the events occurring at each meeting and the significant delay in preparing and approving these minutes increases the possibility that important details from any particular meeting could be lost or misinterpreted.

We recommended that the City implement procedures to ensure that City Council meeting minutes are transcribed and approved in a timely fashion.

### Status

*Resolved* – During fiscal year 2006, the City Council meeting minutes have been transcribed and approved in a timely manner.

## **Maintenance of Loan Balances on the General Ledger**

In the prior year's management letter we noted that the City had issued various economic development loans in conjunction with its Community Development Block Grant (CDBG). The loans were serviced by local banks and all records pertaining to loan activity were maintained in the Planning Department. The City maintained a balance for the principal portion of outstanding loans on the general ledger. However, the Finance Office was not provided with sufficient information to accurately account for new loans, uncollectible loans, and principal payments on loans outstanding. As a result the City's outstanding loan balance was incorrectly stated at the end of fiscal year 2005.

We recommended that the City implement procedures to report all loan activity to the Finance Office to provide additional internal controls over the City's assets and to ensure accurate financial reporting. To achieve this, the principal payments on loans should be reported to the Finance Office independently when receipts are turned over to the City Treasurer, new loans issued and old loans considered uncollectible should be reported to the Finance Office as they occur, and the outstanding loan balance on the general ledger should be reconciled to the detailed information in the Planning Department on a periodic basis.

Status

*Resolved* – The City's Finance and Planning Departments have created a quarterly report in which the Planning Department reports new loans, principal loan balances and loan write-offs. Each quarter, the finance department reconciles this report to the balance on the General Ledger.

**PARTIALLY RESOLVED**

**Financial Condition**

In last year's management letter we noted that the City's financial condition had significantly deteriorated and if the condition was not reversed that the City was at risk of not being able to provide essential core services.

At June 30, 2005 the City only had \$335,000 in undesignated fund balance in the general fund and the City had experienced general fund budgetary losses of approximately \$1 million per year over the preceding several years. Additionally, the City had been using other non-recurring revenue sources and reserve accounts to balance the general fund budget.

During the same time period, the health insurance internal service fund experienced a similar decline. At the end of fiscal year 2004 the fund deficit was (\$1.6 million) and increased to (\$3.0 million) at the end of fiscal year 2005. This deficit, for all essential purposes, is a hidden general fund deficit.

The short-term effect of the City's financial problems was highlighted by the fact that insufficient cash flows required the City to borrow in anticipation of tax revenues during fiscal year 2006 for the first time in several years.

We recommended that the City address the financial situation by:

- Monitoring the fiscal year 2006 budgetary results on an ongoing basis and making adjustments, as necessary.
- Preparing future budgets using reasonable expenditure projections which can be funded by conservative, recurring revenue streams.
- Considering permanently reducing staffing levels and other discretionary expenditures.
- Considering implementing a revenue enhancement program for either increased charges or new fees.
- Addressing the structural deficit in the health insurance trust fund.
- Planning to rebuild the City's stabilization fund and to rebuild and maintain the unreserved fund balance of the general fund. The plan should stipulate when reserves can be used, and a range of the minimum and the target level that fund balance will be maintained at.
- Adopting policies related to cash balances to eliminate the future need to borrow for cash flow shortfalls.

Status

*Partially Resolved* - During the last half of fiscal year 2006, the City took many steps to improve its financial condition for current and future fiscal years. The City monitored the fiscal year 2006 general fund budget and health insurance trust fund very closely to ensure the reduction of deficits in both funds. The City also

implemented spending freezes, increased parking rates, collection/foreclosure of tax liens, and implemented a staff-reorganization plan. Through this process, the City was able to end fiscal year 2006 with a general fund balance of approximately \$1.3 million. The City needs to continue on this path and set policies on desired levels of cash, reserves and fund balances.

The City's Health Insurance Trust Fund ended fiscal year 2006 with a positive cash balance of \$333,000 and a fund deficit related to IBNR of approximately (\$728,000). The decrease from prior years in the deficit balance is in part due to the adoption of M.G.L. chapter 32B, section 18, a Massachusetts statute requiring all Medicare-eligible retirees who are currently on self-insured plans to move from self-insured coverage to a fully insured Medicare supplement plan, which is estimated to save the City approximately \$700,000. The City also received reimbursements from grants for those employees paid by such grants which help to incur some of the health insurance costs.

### **Health Claims Internal Service Fund Deficit**

In the prior year management letter we noted the health claims internal service fund had been experiencing significant declines in its fund balance for the preceding several years. By the end of fiscal year 2005, the fund's cash deficit had grown to \$2.1 million with an additional deficit of \$900,000 from the liability for Incurred But Not Reported Claims (IBNR).

Consequently, during fiscal year 2005, the City was required to transfer \$2.1 million from the general fund to the health claims fund in order for the FY2006 tax rate to be set. The IBNR deficit is required to be funded and raised at a minimum of \$300,000 increments in fiscal years 2007, 2008 and 2009.

Contributing to these escalating deficits was the fact that the employer and employee contributions to the fund were not adequately adjusted to coincide with rising health care costs.

We recommended that the City and its insurance advisors immediately review the coverage offered to its employees and retirees and determine if there are more cost effective alternatives. Since this fund is legislatively required to be accounted for under the full accrual basis of accounting, similar to a business, we recommended that the City create a business model for this fund that consistently covers the cost of operations and creates a positive fund balance. We also recommend that the City implement a policy to create a minimum surplus to anticipate the normal fluctuations in a self-insured plan and to cover IBNR liabilities.

### **Status**

*Partially Resolved* - Through a combination of increased rates, increased oversight, adjustments to billing and collection procedures, and decreased claims, the City ended fiscal year 2006 with a positive cash balance of \$333,000 and an IBNR deficit of \$728,000. The City must fund the remaining deficit to be in compliance with the new law. During fiscal year 2007, the City has converted most health insurance plans to premium based which shifts the risk of insurance to a third party. The premium based plan goes into effect on February 1, 2007. The City will still be liable for the IBNR claims incurred through January 31, 2007 under the self-insured health insurance fund.

### **Fixed Asset Maintenance**

In last year's management letter we noted that the City did not have formal policies and procedures established concerning the maintenance of the City's database or to account for the acquisition and disposal of capital assets. In order to continue to meet reporting requirements, the City needs to maintain a fixed asset sub-system to track

all additions, disposals and depreciation of capital assets on an ongoing basis.

We also noted that the City had elected to postpone the accumulation of its infrastructure assets until fiscal year 2006, as allowed by GASB #34.

We recommended that the City implement policies and procedures to insure the proper accounting for capital assets and that the City maintain a fixed asset management sub-system to account for all capital assets and to ensure proper financial reporting.

#### Status

*Partially resolved* – In fiscal year 2006, the City recorded all major general infrastructure assets acquired prior to July 1, 2001, as required by GASB Statement No. 34. However, the City has not yet developed or implemented policies and procedures to insure the proper accounting for capital assets and the City has not yet implemented a sub-system to account for all capital assets.

### **UNRESOLVED**

#### **Budgeting for Snow and Ice Removal**

In last year's management letter we noted that the City is allowed, under MGL, Chapter 44, Section 31D, to over-expend the budget for the removal of snow and ice, as long as the appropriation for each fiscal year was at least equal to the prior year's appropriation and that any deficits created from this were to be raised in the subsequent fiscal year. During fiscal year 2005 the City incurred expenditures of \$1,181,208, leaving a deficit of \$831,208 to be raised on the fiscal year 2006 tax rate. The FY2006 budget for snow and ice was set at only \$355,000. Less than half way through the fiscal year 2006, the budget was already overspent.

The policy of budgeting the minimum amount for snow and ice removal had become part of the ongoing structural deficit facing the City. Although the practice of under-budgeting for snow and ice removal is legal, it does not demonstrate prudent budgeting practices.

We recommended that the City establish budget policies to incorporate realistic estimates for the removal of snow and ice in the initial City Budget. The amount budgeted does not have to be the worst case but could be the rolling average of the last three or five years of actual expenses.

#### Status

*Unresolved* - The City has not established a new budget policy for budgeting snow and ice removal. The fiscal year 2006 deficit for snow and ice removal totaled \$256,592.

#### **Indirect Cost Allocation**

The prior year's management letter noted that the methodologies used to charge overhead costs and fringe benefits to enterprise funds were not adequately supported. The overhead and fringe costs used for allocations may not include the proper amounts. The charge is based on estimated expenses and a final analysis of the actual expenses for the year is not reconciled and adjusted.

The general fund provides services and pays for certain fringe benefits for its enterprise operations. It is sound business policy to complete a cost allocation plan to charge the enterprise funds for their share of these costs. If

a properly approved and supported cost allocation plan is not used to calculate these charges, then the City is at risk that the general fund and enterprise funds are not being charged their fair share of expenses.

These shared costs should be apportioned by a systematic and rational allocation methodology that is documented in a cost allocation plan and approved each year.

We recommended that the City document a plan which identified all fringe benefits and overhead departments that support each enterprise fund. The plan should include documentation of:

- Direct and indirect charges used to calculate the allocable cost of the overhead department.
- The appropriate base to allocate the specific cost.
- Identifying costs that can use actual direct charges for specific expenses.
- A required year-end reconciliation of the estimate budgeted allocation to the actual results of operations.

The benefit of implementing these recommendations would be the assurance that the general and enterprise funds are not subsidizing each others operations and that the City has a documented sound policy that can be used to balance future budgets.

#### Status

*Unresolved* - The City is in the process of documenting a systematic and rational allocation for charging future indirect costs.

#### **Compensated Absences**

We noted in the prior year's management letter that the City maintains separate systems to monitor available sick and vacation balances for police, fire, school, and other city employees. The School Department utilizes a manual system to monitor these balances. None of these systems allow for an automated and perpetual balance of the City's liability for compensated absences at any point in time. The process for determining the City's liability at year-end for financial reporting purposes is time consuming and inefficient. The systems do not provide the City with a tool for managing the accumulated liability.

We noted that the City's payroll system has a function for tracking sick, vacation and compensatory time that is not utilized. The automation and centralization of this process would strengthen controls to ensure that compensated absences practices, within all departments, are in compliance with union contracts and it would provide management with a tool for monitoring and managing the City's growing liability in this area.

This growing liability is the result of contracts and policies which allow employees to carry-over unused sick, vacation and compensatory time and to be paid for that time upon the termination of their employment with the City. Allowing such liabilities to continue to accumulate puts the City at risk of having to pay on the liabilities at a time when available budgets have already been stretched, further impairing the City's financial condition.

Each year employees leave or retire and the accumulated liability must be paid out of current budgeted funds. In order to manage the budget, and eliminate another area that can add to the structural deficit, it would be useful if the finance director and department heads could access information on employees who are likely to retire based on years of service and age. With the associated accumulation of the liability the City could ensure that all departments include these added expenses within their budget projections.

There is increased accountability along with better management information and improved employee reporting if the City's liability for compensated absences is monitored through the payroll system. The City should consider

using the payroll function to control this information.

We also recommend the City consider the existing policies related to the accumulation of compensated absences as a means of managing its future budgets and potential liabilities.

Status

*Unresolved* - The City plans to fully automate the process for monitoring compensated absences through the MUNIS system during fiscal year 2007.

**Require Employees to Take Vacations**

Last year we noted that the City employees are not required to take an annual, uninterrupted, one-week or longer vacations. Requiring annual vacations is an important internal control function designed to help an employer to detect errors, inefficiencies, and irregularities; to provide management with a means of cross-training employees; and to help prevent employee burnout and the resulting inefficiencies. Additionally, it is important to require another person to perform the absent employee's duties while he or she is on vacation.

We recommend that the City consider implementing a policy requiring all employees to take an annual, uninterrupted vacation and that the policy be enforced.

Status

*Unresolved* - The City is actively encouraging employees to take vacations; however, there is no policy requiring all employees to take an annual, uninterrupted vacation.

**Statement No. 45 of the Governmental Accounting Standards Board**

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 over contributions 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 over contributions.

This Statement generally provides for prospective implementation. This means that employers set the beginning net OPEB obligation at zero as of the beginning of the initial year. The City is required to implement this statement in fiscal 2008 although earlier implementation is encouraged.

We 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.

#### Status

*Unresolved* - The City is in the planning phase of implementing GASB 45. An actuarial has not been performed as of June 30, 2006; however, the City does plan to obtain an actuarial valuation.

#### **Reconciliation of Trust Fund Investments**

Last year's management letter noted that the City's Board of Trust Fund Commissioners oversee a substantial portfolio of investments related to the City's trust funds. The City was periodically provided with a spreadsheet prepared by the Board's investment advisor that detailed the activity of the individual trusts that made up the investment pool and the City used the spreadsheet to record the cumulative activity of the trusts to the general ledger. However, the City was not provided with an investment statement from the bank detailing the fair market value of the pool's individual investments to support the total amount of cash and investments reported on the spreadsheet. The reconciliation of the investment spreadsheet prepared by the advisor to the actual cash or investments supporting those balances is an important internal control over significant City assets. The lack of reconciliation procedures increases the possibility that errors or irregularities could occur and would not be detected.

We recommended that the Board of Trust Fund Commissioners complete a quarterly reconciliation of the amounts and activity reported on the investment advisor's spreadsheet to the investment statement received from the bank. This reconciliation should then be forwarded to the City's Finance Office and the activity should be reported on the City's general ledger and the balances should be reconciled to the supporting documentation.

#### Status

*Unresolved* – The Board of Trust Fund Commissioners has not provided the City with quarterly reconciliations of the activity and balances reported on the investment advisor's spreadsheet to the investment statement received from the bank.

## **School Lunch Deficit**

The previous year's management letter noted that the City's School Lunch Program was in deficit. The deficit was required to be funded through available funds or taxation in fiscal year 2006. School lunch deficits typically occur when the fees charged for the services provided are insufficient to cover the costs of operating the program.

We recommended that management implement procedures to identify the reasons for continued deficits and to better manage the fund. To do this, management could benefit by preparing a budget for the school lunch program and by comparing projected and actual results of operations throughout the year. We noted that this would allow management to better plan for potential shortfalls and to take action, as necessary, to reduce any future impact it might have on the City's general fund. We further recommend that the budget be prepared with the input of the individuals who will be responsible for meeting budgetary goals. With the cause of significant variations from the budget being determined and documented to be used as a management tool so that corrective action can be taken if necessary in a timely fashion.

### Status

*Unresolved* – Although financial controls and account changes have been implemented in fiscal year 2006, the School Lunch Program's deficit increased from \$89,000 to \$195,000.

## **Personal Use of City Vehicles**

In last year's management letter we noted that the City does not report, as employee compensation, the value of the personal use of City owned vehicles for those employees that utilize a City vehicle to commute to and from work. Internal Revenue Service (IRS) regulations require that the value of noncash fringe benefits be reported as income to the recipient. Thus the commuting value of a vehicle owned or leased by a public entity usually represents taxable income to the employee.

We recommended that the City review the IRS guidelines relating to employees' personal use of City owned vehicles and establish policies and procedures to ensure compliance with all applicable laws and regulations.

### Status

*Unresolved* – There has been no change in the above comment.

## ***Current Year's Comments***

## **Accounting for Cherry Sheet Receipts and Assessments**

### Comment

We noted that the finance department recorded the Cherry Sheet receipts net of assessments on the City's general ledger. The City is required to report all revenues and expenditures gross, rather than net. Consequently, several adjustments were required to the general ledger for state reporting, budget to actual comparisons, and for the City's financial statements.

### Recommendation

We recommend that the City record both budget and actual Cherry Sheet receipts and assessments gross, rather than net, as revenues and expenditures on the general ledger.

## **Recording Activity Directly to Fund Balance**

### Comment

The City records a significant amount of activity directly to equity accounts in the general ledger. All revenue, expenditures, and other financing sources/uses should be posted to subsidiary accounts of its respective fund. By doing so, interim reporting of budget to actual results to management will be accurate and more easily generated (i.e. system generated reports versus reports requiring a manual calculation).

### Recommendation

We recommend that transaction that effect fund balance be processed using revenue and expenditure accounts.

## **Disaster Recovery Plan**

### Comment

The City does not have a well-defined written disaster recovery procedure. The time to make contingency plans is before disaster strikes, so that all personnel will be aware of their responsibilities in the event of an emergency situation that precludes the use of existing IT facilities.

### Recommendation

We recommend that management develop a disaster recovery plan that includes, but is not limited to, the following matters:

- Location of, and access to, off-site storage.
- A listing of all data files that would have to be obtained from the off-site storage location.
- Identification of a backup location (name and telephone number) with similar or compatible equipment for emergency processing. (Management should make arrangements for such backup with another company, a computer vendor, or service center. The agreement should be in writing.)
- Responsibilities of various personnel in an emergency.
- Priority of critical applications and reporting requirements during the emergency period.

## **Internal Policy and Procedures**

### Comment

We noted that most departments do not have written policies and procedures for its administrative and financial functions. This manual should include all areas of activities, including administration and operations. A policy and procedures manual will document how the Department operates and will support cross-training and employee turnover when necessary.

### Recommendation

We recommend that each Department Head develop an internal procedure manual. The document should be written in sufficient detail to provide a person with the ability to understand the procedures required to complete daily tasks. Once completed, this document should be updated as system changes occur. A master should be maintained and stored in a secure location.