

**TOWN OF BLACKSTONE,  
MASSACHUSETTS**

MANAGEMENT LETTER

YEAR ENDED JUNE 30, 2016

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Table of Contents

Transmittal Letter.....1 – 2

Overview.....3

Informational Items.....4 – 5

Findings and Recommendations – General Government .....6 – 9

Findings and Recommendations – Enterprise Funds.....10 – 11



Board of Selectmen  
Town of Blackstone  
Blackstone, Massachusetts

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of Town of Blackstone, Massachusetts (the "Town"), as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise the Town's basic financial statements, and have issued our report thereon dated January 19, 2017.

### **Internal Control over Financial Reporting**

In planning and performing our audit of the financial statements, we considered the Town's internal control over financial reporting ("internal control") to determine the audit procedures that are appropriate in the circumstances 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.

A *deficiency in internal control* 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 and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or, significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

## **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the Town's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

## **Purpose of this Report**

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

*Roselli, Clark & Associates*

Roselli, Clark & Associates  
Certified Public Accountants  
Woburn, Massachusetts  
January 19, 2017

## OVERVIEW

Fiscal year 2016 proved to be another financially positive year for many Massachusetts municipalities. Employment rates throughout the Commonwealth steadied several years ago and unemployment rates are approaching records low. The June 2016 unemployment rates in Worcester county and the Commonwealth of Massachusetts were 4.6% and 4.3%, respectively. The June 2016 unemployment rate for the Town was 4.5%, which is relatively consistent with the county and statewide rates.

The housing market, particularly within the Town and many of its surrounding communities, has been robust over the past several years. Residential real estate valuations are at all-time highs in many of the Town's neighborhoods. Furthermore, the Town has seen an increase in new housing starts.

In its governmental funds financial statements, which most closely resembles the Town's statutory accounting records, the Town's unassigned fund balance in its general fund approached \$5.4 million at June 30, 2016. Included in the unassigned fund balance at June 30, 2016 was approximately \$3.4 million in stabilization funds.

Liquidity in the general fund is often measured by comparing both the unassigned fund balance to the current year's total fund expenditures. Credit rating bureaus often refer to this as a "reserve ratio." At June 30, 2016, the unassigned fund balance in the general funds approximated 29% of total general fund expenditures. Furthermore, the total fund balance in the general fund approximated 37% of that same amount. The Town's reserve ratio is very strong and provides the Town significant budgetary flexibility in the event of a downturn in the economy.

In fiscal year 2016, the Town established an OPEB trust and contributed \$250,000 into this trust in its first year. These funds are invested in the State Retirees Benefits Trust Fund, which is managed by the Pension Reserved Investment Management Board of the Commonwealth of Massachusetts, or PRIM. OPEB trusts are intended to assist the Town in funding its future postemployment health benefits to its employees. An additional \$250,000 was contributed into the OPEB trust in early fiscal year 2017. The establishment of an OPEB trust and continuing contributions, while not currently mandated by Massachusetts General Law, are prudent business decisions that are viewed very favorably by credit rating bureaus.

The Town's budgetary flexibility, strong reserve ratio and planning/funding for its future obligations has undoubtedly been seen as positive factors to S&P. In connection with a July 2015 general obligation bond offering, Standard & Poor's Rating Services, or S&P, assigned a credit rating of AA+, which is one step below S&P's highest rating of AAA. This high credit rating enables to Town to enjoy very favorable terms in the municipal bond market.

The remainder of the report reflects informational items and findings and recommendations. This discussion is intended to provide the Town and its management with recommendations for improvement in accounting and financial operations. The Town should review these recommendations and, if determined to be cost-effective, implement these improvements. Items that have been repeated from past letters to management are so indicated.

## **INFORMATIONAL ITEMS**

### ***New Accounting Principle – OPEB***

The Governmental Accounting Standards Board, or GASB, issued a new pronouncement related to other postemployment benefits, or OPEB, that is substantially similar to the pension standard implemented in fiscal year 2015. OPEB typically includes health and welfare plans and other similar benefits provided to Town retirees exclusive of pension benefits. The Town presently contributes 50% of the cost of retirees' comprehensive medical insurance offered through its health plan providers. This new accounting standard becomes effective in fiscal year 2018.

The Town currently reports a net OPEB obligation in its government-wide financial statements calculated under GASB 45, *Accounting and Financial Reporting by Employers for Postemployment Benefit Plans Other Than Pension Plans*. However, this new accounting standard will change the manner in which OPEB is accounted and reported in the Town's government-wide financial statements. GASB 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pension Plans*, will require that the net OPEB liability, which can be substantially larger than the net OPEB obligation, be reported in the government-wide financial statements beginning in fiscal year 2018.

While this new accounting standard will likely materially affect the Town's government-wide financial statements, the Commonwealth of Massachusetts has not passed legislation requiring municipalities to begin setting aside monies for this unfunded obligation like it has with pensions.

The Town currently reports a positive unrestricted net position in its governmental activities. It is likely that the adoption of this new accounting standard will require a one-time adjustment to the Town's government-wide financial statements in the form of a prior period restatement and cause its unrestricted net position to become a deficit.

### ***Municipal Modernization Act***

In August 2016, the Municipal Modernization Act was signed into law. This law streamlined many of the financial legislation used throughout the cities and towns in the Commonwealth. The two portions of this Act that will likely affect most (if not all) Massachusetts municipalities include:

1. Creating a single overlay reserve to cover the costs of potential abatements or exemptions granted by assessors or ordered by the ATB versus having to maintain individual overlay reserves by fiscal year. This portion of the Act became effective on November 7, 2016.
2. Changing the statutory treatment of premiums received when issuing debt. Prior to the Act, premiums (net of issuance costs) were general fund revenue. Effective November 7, 2016, premiums (net of issuance costs) are: (a) used to pay project costs and to reduce the amount of borrowings authorization by the same amount when the borrowing vote so authorizes; or
3. (b) reserved for appropriation for capital projects for which a loan has been, or may be, authorized for an equal or longer period of time than the loan for this the premiums were received.

The implementation of the changes to overlay accounts does not present much of an obstacle to most municipalities. However, future borrowings must contemplate the statutory changes to manner in which bond premiums are treated. Future bond issuances will require closer attention to these matters.

### ***New Financial Statement Disclosures – Tax Abatement Disclosures***

The GASB issued Statement No. 77, *Tax Abatement Disclosures*, to improve financial reporting by giving users of financial statements essential information regarding the nature and magnitude of tax abatement programs to assist in determining how tax abatements affect the Town's future ability to raise revenues and meet its financial obligations. This Statement is effective for the Town's fiscal year 2017 financial statements.

Tax abatements, as defined in the Statement, result from an agreement between the Town and an individual or entity in which the Town promises to forgo tax revenues and the individual or entity promises to subsequently take specific action that contributes to economic development or otherwise benefits the Town or its citizens. Tax abatement agreements may be in writing or may be implicitly understood by the Town and the entity.

This Statement requires Town's that enter into tax abatement agreements to disclose the following information about the agreements:

- Brief descriptive information, such as the tax being abated, the authority under which tax abatements are provided, eligibility criteria, the mechanism by which taxes are abated, provisions for recapturing abated taxes and the types of commitments made by tax abatement recipients.
- The gross dollar amount of taxes abated during the period.
- Commitments made by the Town, other than to abate taxes, as part of a tax abatement agreement.

The disclosures are organized by major tax abatement program and the Town may, but is not required, to disclose information for individual tax abatement agreements. It is important to note that tax abatements for valuation disputes or tax exemptions for qualified taxpayers are not covered by this Statement and no disclosure of these types of transactions is required.

While this new accounting standard does not pose a significant use of the Town's resources to comply, we recommend that the Town begin to compile the pertinent information above regarding all tax abatement agreements that may require disclosure so that the Statement may be efficiently implemented in fiscal year 2017.

## FINDINGS AND RECOMMENDATIONS – GENERAL GOVERNMENT

### *Fraud Prevention Measures*

There has been an alarming increase in municipal fraud throughout the United States. Many Massachusetts municipalities have been victims of fraud. For municipalities, the three most common ways to commit fraud:

1. ***Unauthorized Issuance of Vendor Checks*** – According to the Association of Certified Fraud Examiners, this type of fraud presents the greatest risk of theft of **material** amounts of municipal funds. Payments are made from municipal bank accounts to either fictitious vendors or to valid vendors for unauthorized or phantom goods or services. This type of fraud is generally perpetuated at higher levels within a municipality (i.e., department heads with purchasing capabilities, Accounting or Treasury personnel).

There are a number of prevention methods that can be used to prevent or timely detect this type of fraud including:

- a. Timely review of budget to actual results by department heads, the Town Accountant and the Town Administrator;
- b. Regular periodic review of vendor master files within the MUNIS system and the deactivation of vendors who haven't served the Town for several years; and
- c. Timely reconciliation of bank accounts.

We are pleased to report that budget to actual reviews are prepared and distributed to all pertinent parties within the Town on a timely basis and that the Town Administrator carefully reviews these reports. In addition, the Town Treasurer's policy of reconciling all bank accounts within one week of month end is among the most timely bank reconciling cycles we've observed throughout the Commonwealth; based on our experience, most municipalities have their cash reconciled within three to four weeks of month end.

The Town does not have a formal schedule to periodically review (i.e., quarterly or semiannually) its vendor master files within MUNIS. We recommend that the Town Accountant or her designee review these vendor files for relevancy and validity and, if necessary, deactivate inactive vendors as needed.

2. ***Theft of Cash Receipts*** – According to the Association of Certified Fraud Examiners, this type of fraud is the **most frequent** type of fraud municipalities become victim to. Fraudulent schemes to steal municipal receipts prior to their recording in the accounting records represents the largest risk to a municipality and is the most common form of cash receipts fraud committed. For example, cash received at a departmental level are simply not turned over to the Town Treasurer. Generally, this type of fraud starts small and grows over time.

There are a number of prevention methods that can be used to prevent or timely detect this type of fraud including:

- a. Trend analysis of departmental revenues for multiple accounting periods by the Town Accountant and Town Administrator; and
- b. Performing periodic "audits" or business reviews of departmental turnover procedures.

The Town does not perform either of these activities.

Trend analysis of departmental revenues tracks monthly recorded revenues by department by revenue type (i.e., permits, user fees, fines, licenses) over several years. In doing so, patterns can generally be observed and deviations from these patterns may identify abnormalities, including the possibility of fraud. We recommend that the Town develop these reports and implement them beginning in fiscal year 2018.

Periodic “audits” or business reviews at departments by the Town Accountant can provide insights into a department’s operations that cannot be obtained by simply reviewing its periodic cash receipt turnovers to the Town Treasurer. We recommend that the Town Accountant adopt a schedule for these business reviews and perform these reviews on two to three departments each year.

3. ***Payroll Frauds*** – According to the Association of Certified Fraud Examiners, this type of fraud was present in a similar frequency as cash receipts fraud and its average loss was also comparable to cash receipts fraud. The most common types of payroll fraud applicable to municipalities pertains to (i) expense reimbursement and (ii) payments to “ghost” employees. Due to the nature of the Town’s operations, expense reimbursements are infrequent and generally carry a high degree of scrutiny. Furthermore, as there are less than 100 Town employees, payroll payments to ghost employees does not present a significant risk. The Town’s timely review of budget to actual performance serves as a key detective control with respect to this fraud risk area. Furthermore, there are multiple levels of review of payroll submissions to further prevent this type of fraud.

Although the Town’s profile mitigates the risk of this type of fraud, we recommend that regular periodic reviews of the payroll database be performed and terminated/retired employees be deactivated from the payroll master database.

### ***Town Treasurer/Collector is an Elected Position***

The Town elects its treasurer/collector every three years. Massachusetts municipalities operating with elected treasurer/collectors have been steadily declining. As a result, an elected treasurer/collector is becoming scarce. Recently, two much larger surrounding towns (Milford and Franklin) approved bylaw changes to appoint their treasurer/collectors versus having this critical position being elected. Furthermore, the Division of Local Services of the Massachusetts Department of Revenue has consistently recommended that this position be appointed versus elected.

As in any elected position, the Town’s treasurer/collector must be a resident of the Town. The Town has a population of approximately 9,000 residents, which limits the available talent pool capable of performing the critical Town functions of a treasurer/collector.

While the current elected treasurer/collector possesses the skills necessary to support this position, future elected Treasurer/Collectors may not. We recommend that the Town evaluate a referendum to amend its selection method of the Town treasurer/collector.

### ***Timing of Cash Processing***

In connection with our auditing procedures, we determined that the Town incorrectly accounted for approximately \$81,000 in state grant monies received in July 2016. These funds were recorded as cash receipts in the accounting records in fiscal year 2016. This cutoff error was significant to the Town and the audited financial statements were adjusted to correct for this error.

While incorrect, this method of accounting is not atypical in Massachusetts municipalities. Many communities will record intergovernmental receipts received subsequent to June 30<sup>th</sup>, but in close proximity to June 30<sup>th</sup>, as cash receipts in the closed fiscal year. By doing so, these communities may avoid reporting negative fund balances in their grant funds.

There are mechanisms available to the Town that would permit it to properly record its accounting transactions including recording an account receivable without an associated deferred revenue, which is permissible. We recommend that the Town employ these means of accounting in all future accounting periods.

### ***Reporting Fair Value of Investments***

In connection with our auditing procedures, we determined that the Town reported the carrying value of its stabilization and capital investment funds on an amortized cost basis versus at their fair value. As a result, the underlying accounting records understated these investment accounts by nearly \$118,000 in the aggregate.

While incorrect, this method of accounting is not atypical in Massachusetts municipalities. However, several years ago, the Massachusetts Department of Revenue included as part of its year-end closing procedures a requirement that investments should be recorded at their fair value.

We recommend that the Town Treasurer and Town Accountant record the appropriate increase in these accounts, which are the result of unrealized gains, in the Town's cash book and its underlying accounting records.

### ***Quality of Ambulance Receivables and Need for Write-off Policy***

The Town's fire department operates an ambulance service. Like the majority of Massachusetts municipalities, the Town outsources the billing, collections and account maintenance of its ambulance service to a third party.

It's been the Town's policy to write-off amounts unpaid by residents or their insurance companies. However, the Town has not been meeting with its third party billing company to identify and write off these amounts. As a result, the Town's ambulance receivable continues to grow and, at June 30, 2016, totaled nearly \$623,000. Furthermore, approximately \$468,000, or 75%, of this outstanding balance is aged more than 120 days past due.

The audited financial statements include a significant allowance for uncollectible accounts based on the poor quality of the receivables balance as well as the Town's policy to forgive write off resident balances.

We recommend that the Town implement a formal ambulance receivables and write off policy, which provides for the periodic review of receivable balances with the third party billing company. Furthermore, we recommend that this policy be written to authorize the Town Administrator to approve any and all ambulance receivable write offs.

### ***Capital Asset Tracking and Reporting***

The Town does not have a capital asset tracking and reporting system. In addition, the Town does not have a process in place to identify capital asset additions or disposals. Rather, it relies on its external accounting firm to track its capital assets.

Capital asset accounting systems have become increasingly affordable and it's likely that the Town could deploy a robust capital asset accounting system for a relatively minimum cost, which includes customization. The adoption of such a system would likely facilitate insurance reporting and provide a mechanism to safeguard the Town's capital assets.

We recommend that the Town investigate these solutions and include such a system in its fiscal year 2018 budget.

### ***Existence of Fully-Depreciated Capital Assets***

The fixed asset files used by the Town contain a significant number of fully-depreciated capital assets that, based on their description, are unlikely to be under the Town's ownership at this time. For example, there are a number of vehicles aged over twenty-five years that were likely disposed of many years ago. These should have been disposed of in the capital asset records.

Disposal of fully-depreciated capital assets does not affect the net carrying value of the Town's reported net capital assets. However, including these values artificially grosses up both capital assets and accumulated depreciation.

In connection with the transition of audit firms in fiscal year 2016, the fixed asset records required a significant amount of modification and enhancements. The records are now in a format that would more easily permit the Town to conduct an analysis of its capital assets.

We recommend that the Town evaluate its capital asset records and, where needed, dispose of capital assets that are no longer owned by or used by the Town before the conclusion of fiscal year 2017.

### ***Foreclosure Receivables***

The Town is unable to produce an accurate detail of foreclosed properties that have been transferred from tax title to foreclosures. The Town Accountant and Treasurer work together to ensure that current foreclosures are properly accounted for, however those that were recorded by previous personnel require additional attention.

We recommend that the Town Accountant, Treasurer and assessing personnel determine all properties owned by the Town that were taken through foreclosure and determine the correct amount that should be recorded in the underlying accounting records.

## FINDINGS AND RECOMMENDATIONS – ENTERPRISE FUNDS

### *Overview*

Since July 2000, the Town operates its water and sewer operations as an enterprise fund. An appointed water and sewer commission oversees these operations. In fiscal year 2016, the Town began reporting separately the operations of its sewer and water operations in its annual audited financial statements in an effort to provide more transparency to its residents and rate payers.

The sewer and water funds reported positive results of operations in the proprietary funds financial statements included in the Town’s audited financial statements for the year ended June 30, 2016 in the amounts of \$425,802 and \$61,718, respectively. The proprietary funds financial statements report balances using full accrual accounting, which differs materially from the statutory basis of accounting, which is the manner in which the Town reports the results of operations for these operations to the Massachusetts Department of Revenue and to the taxpayers of the Town. Included in these positive results of operations were transfers from the general fund of \$725,431 and \$226,279 to the sewer and water funds, respectively, for debt service costs paid by the general fund on their behalf. These transfers are funded from the PILOT agreement monies with ANP Blackstone Energy Company LLC, a power generator.

As stated above, the Town manages its operations using a statutory basis of accounting. The following is a summary of the fiscal year 2016 financial activity on a statutory basis for these two operations inclusive of sewer and water capital projects funds:

	Sewer	Water	Total
<b>Receipts:</b>			
User charges	\$ 679,604	\$ 964,555	\$ 1,644,159
Proceeds from bond offerings	-	882,000	882,000
Total receipts	679,604	1,846,555	2,526,159
<b>Expenditures:</b>			
Personnel related	166,159	233,310	399,469
Operations	343,134	380,774	723,908
Debt service	-	67,611	67,611
Indirect costs	30,000	30,000	60,000
Capital	-	205,769	205,769
Total expenditures	539,293	917,464	1,456,757
Change in fund balance - statutory basis	140,311	929,091	1,069,402
Statutory fund balances - July 1, 2015	545,116	194,651	739,767
Statutory fund balances - June 30, 2016	\$ 685,427	\$ 1,123,742	\$ 1,809,169

The Town recently increased its sewer and water user rates approximately 20% and 23%, respectively. On an annualized basis, this is will generate an additional \$150,000 and \$190,000 for the sewer and water operations, respectively.

### ***Semi-Annual Billings at Water/Sewer Enterprise***

The Town bills its water and sewer usage charges in semi-annual installments, unlike the majority of Massachusetts municipalities who generally bill quarterly. The vast majority of the Town's meters have been converted to radio-frequency meters, which greatly improves the billing process and lends itself to more frequent billings. Of the remaining manual reads, the Town estimates that it can accomplish all needed readings in approximately one day.

The use of quarterly billings provides more steady cash flows to these enterprise funds. We recommend that the Town evaluate its current billing processes to determine whether quarterly billings are feasible.

### ***Indirect Costs***

The water and sewer enterprises do not have dedicated employees. Rather, the Town allocates portions of its DPW, assistant Town Accountant and Assistant Collector personnel costs to these enterprise funds based on their job duties as salaries and wages. In addition, some personnel benefits are also allocated to these enterprises. However, the water and sewer enterprises consume larger amounts of Town resources, which are not being properly assessed to these enterprise funds. The following significant costs are being incurred by the water and sewer operations, but are not being assessed to these operations:

- Regional pension system's retirement assessment;
- Unemployment insurance and Town's matching share of Medicare insurance;
- Shared services for information technology, legal and audit; and
- Shared personnel services for Town Administrator, Town Accountant and Town Treasurer/Collector.

As a result, the Town's tax payers are absorbing these costs in their property taxes as opposed to the water and sewer users in their usage rates. Furthermore, as a result of the current accounting, the Town is unable to accurately determine the exact costs necessary to operate and administer its water and sewer enterprises.

The Commonwealth of Massachusetts has guidance on indirect costs for enterprise funds. We recommend that the Town evaluate the impact that assessing reasonable indirect costs would have on these operations and their users and begin the process of assessing indirect costs in fiscal year 2018 (2019 at the latest).

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