

CITY OF SPRINGFIELD, MASSACHUSETTS

MANAGEMENT LETTER

JUNE 30, 2012

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To the Honorable Mayor, the City Council, and Management
City of Springfield, Massachusetts:

In planning and performing our audit of the financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the City of Springfield, Massachusetts as of and for the fiscal year ended June 30, 2012 (except for the Springfield Contributory Retirement System which is as of and for the year ended December 31, 2011), in accordance with auditing standards generally accepted in the United States of America, we considered the City'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 City's internal control. Accordingly, we do not express an opinion on the effectiveness of the City's internal control. Our opinions on the financial statements and this report, insofar as they relate to the Springfield Redevelopment Authority and the Springfield Library and Museums Association, are based solely on the report of other auditors.

However, during our audit we became aware of several matters that we believe represent opportunities for strengthening internal controls and operating efficiency. The memorandum that accompanies this letter summarizes our comments and suggestions regarding 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 City 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 City's written responses to the matters identified in our audit have not been subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on them.

This communication is intended solely for the information and use of management of the City of Springfield, Massachusetts, and is not intended to be and should not be used by anyone other than these specified parties

Powers & Sullivan, LLC

December 27, 2012

CITY OF SPRINGFIELD, MASSACHUSETTS

MANAGEMENT LETTER

JUNE 30, 2012

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Current Year Comments

RETIREMENT SYSTEM FUNDING STATUS

Comment

To comply with current Massachusetts General Laws, the Springfield Contributory Retirement System (System) must be fully funded by 2040. As reflected in the most recent actuarial valuation (January 1, 2012), the funded ratio for the System decreased to 29%, down from 35% in the previous valuation (January 1, 2010). The funded ratio is the percentage of the accrued liabilities that are covered by assets accumulated to satisfy the liability. The unfunded actuarial liability is approximately \$657 million.

The System's ratio ranks among the lowest percentages in the nation. The current funding level places the System in a precarious position which could require future borrowing or drastic cuts to other budget areas to properly fully fund the plan.

Recommendation

We recommend the System should work closely with its Actuaries and Financial Advisors to put plans in place to address and monitor this situation over the next several years.

City's Response

Management agrees with this recommendation. The Springfield Retirement Board has adopted an aggressive funding schedule with increases of 5% in the appropriation for FY 2014 & 2015 and a 6% increase per year until FY 2036 with final payment of the unfunded actuarial liability in FY 2037.

FUTURE GOVERNMENT ACCOUNTING STANDARDS BOARD (GASB) STATEMENTS FOR PENSIONS AND OPEB

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. To briefly summarize these new standards –

- GASB #63 and 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 outflows – liabilities – deferred inflows = net position. These new requirements will affect certain aspects of the financial statements currently and they 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 City should expect to record significant pension and OPEB liabilities in the future.

Recommendation

We recommend that management begin to study and evaluate these changes for financial statement reporting and disclosure purposes, and to formulate plans 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 your constituents and other financial statement users.

City's Response

Management agrees with this comment and will be prepared to implement these financial reporting standards as they become effective.

Prior Year Comments - Unresolved

PRIOR YEAR COMMENTS – UNRESOLVED

The following comments and recommendations were reported in prior Management Letters and we have only included the comments that we believe to be unresolved.

TREASURER’S OFFICE OPERATIONS

Updated Previous Comment

This finding related to the lack of resolution of items identified during the reconciliation of the bank accounts. Old outstanding checks dating back decades were not transferred to tailings and other reconciling items were never corrected on the bank reconciliations or on the City’s ledgers.

Continuing Recommendation

We found the finding to still be valid. We continue to recommend a new reconciliation process be formalized that utilizes the capabilities of the new management and accounting software being installed. Any outstanding reconciling items other than the normal deposits in transit, current outstanding checks and other timing differences must be adjusted before implementation.

Updated City Response

The City agrees with the auditor’s recommendations and is currently using the MUNIS treasury management system to reconcile its bank accounts. Utilizing a new format recommended by the Department of Revenue, the City has continued to research, identify and make any adjustments to the reconciliations and on the City’s ledgers. Outstanding checks older than 90 days are now transferred to the Tailings account on a monthly basis and reconciled to the general ledger. The Treasurer is continuing to work with the Comptroller’s Department to research, identify and resolve all reconciling items.

INFORMATION TECHNOLOGY AUDITOR

Updated Previous Comment

We believe that an IT auditor could play a vital role in ensuring that appropriate financial and operational controls are included in the City’s IT systems, such as MUNIS. The IT auditor could provide a valuable internal control function by periodically testing systems controls to determine that they are effective and have not been circumvented.

Continuing Recommendation

We continue to recommend that the City consider establishing an IT auditor position within the internal audit division or outsource this function to a qualified independent consultant. The role and responsibilities of the IT auditor should be formally defined and communicated to IT management as well as other affected user departments. The IT auditor should meet regularly with IT department representatives, user personnel, and relevant contractors during developmental projects to ensure that proper financial controls and audit trails are included in each new or modified system. These meetings would allow the IT auditor to ensure that applicable, cost beneficial controls are included in each system. The meetings would also help the IT auditor develop auditing approaches by increasing his or her understanding of the controls being adopted. We recommend that the IT auditor establish a formal, ongoing program of tests to be conducted.

Updated City Response

The City's Acting Director of Internal Audit plans to initially outsource this function as funding becomes available. The Acting Director of Internal Audit will work directly with the IT Auditor in developing and performing an audit plan and in communications with IT management.

City management has established an IT Steering Committee to perform strategic planning for all IT operations. This matter has been prioritized by the Committee to address areas of risk that potentially could be detrimental to the City.

Outsourced IT audit services are expected to begin during the first quarter of fiscal year 2014 and will initially encompass a review of controls of IT functions at Springfield City Hall. Additional areas will be reviewed as part of an ongoing comprehensive review.

UNCLAIMED CHECKS

Updated Previous Comment

The City has a substantial number of unclaimed checks (tailings) within the bank accounts maintained by the Treasurer. A large portion of these checks are more than several years old and we are not aware of any established procedures that have attempted to resolve the reason for these checks to remain outstanding. The lack of controls and procedures places the City at risk that funds could be misappropriated.

Within Chapter 46, Section 108 of the Acts of 2003 "An Act Providing Relief and Flexibility to Municipal Officials" is a section that improved the law regulating abandoned property. This section was written with the intention to make it easier for Treasurer's to process uncashed checks which have been deemed abandoned to either return the funds to the owner or to the City's general fund.

Continuing Recommendation

We continue to recommend that the Treasurer's office implement Chapter 46, Section 108 of the Acts of 2003 for tailings. As part of the implementation plan, the Treasurer should continually monitor and investigate all outstanding checks greater than three months old. These balances must be periodically reconciled to the general ledger.

Updated City Response

The City continues to research the tailings account and continues to apply any overpayments to outstanding balances due the City, where applicable. Checks older than 90 days that are not utilized to pay outstanding balances due the City are now transferred monthly to the Tailings account and reconciled to the City's ledger. Per the rules and conditions of Chapter 46, Section 108 of the Acts of 2003 "An Act Providing Relief and Flexibility to Municipal Officials", these checks will be advertised as of March 1, in order to either refund the checks to the owner or the City's General Fund.