

**CITY OF MALDEN, MASSACHUSETTS**

MANAGEMENT LETTER

YEAR ENDED JUNE 30, 2018

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Honorable Mayor and Members of the City Council  
City of Malden, Massachusetts  
Malden, Massachusetts 02148

In planning and performing our audit of the financial statements of the governmental activities, each major fund, its component units and the aggregate remaining fund information of the City of Malden, Massachusetts, (the "City") as of and for the year ended June 30, 2018, in accordance with auditing standards generally accepted in the United States of America, we considered the City's internal control over financial reporting ("internal control") 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.

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.

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

This communication is intended solely for the information and use of management, the City Council, and others within the organization, and is not intended to be and should not be used by anyone other than these specified parties.

*Roselli, Clark & Associates*

Roselli, Clark & Associates  
Certified Public Accountants  
Woburn, Massachusetts  
February 20, 2019

## **I. EVALUATION OF CITY OPERATIONS**

The City's unassigned fund balance increased from \$10.9 million at the end of fiscal year 2017 to \$12.5 million at the end of fiscal year 2018. This reversed two years of decreasing fund balances during fiscal years 2016 and 2017.

Contributing to this increase was the City's operating results, which exceeded estimated forecasts by almost \$3.0 million. This was leveraged by continued economic development and strong local receipts that were leveraged by a robust economy.

Despite the current year balances being less than the 2015 peak of about \$16 million they are still well above the 2011 levels of about \$6 million.

In the prior year we cautioned the City's strategy of using free cash during its budget process. This was a strategy that began in fiscal year 2015 and contributed to the decline we discussed in fiscal year 2016 and 2017. We continue to caution the City in that regard, as we observed that the City used an additional \$2.7 million in free cash for fiscal 2019.

At some point the economy will cool down and the City will find it difficult to recover free cash through positive operations. In addition, structural issues could emerge in the annual budget. This could create pressure on the City's bond rating which has enjoyed a three-step increase since fiscal 2012 from A to AA that allowed the City to achieve favorable bond rating status and become comparable to neighboring Greater Boston communities.

|            |     |
|------------|-----|
| Somerville | AA+ |
| Medford    | AA+ |
| Everett    | AA+ |
| Malden     | AA  |
| Chelsea    | AA  |
| Revere     | AA  |

The remainder of the report is dedicated to informational items, and recommendations for improvement in control and efficiencies in operations. We urge the City to implement recommendations where appropriate and cost/beneficial to do so.

## **II. INFORMATIONAL ITEMS**

### **OPEB Strategy**

The City implemented GASB 75 for the year ended June 30, 2018. This was the first year that the accounting standards required a true measurement of the unfunded net OPEB liability and its recording in the financial statements.

The actuary calculated the net OPEB liability at approximately \$235 million which has increased the City's net liabilities significantly. While the City established a formal OPEB trust fund, it has yet to dedicate any resources towards it. As a result, the actuary can not give the City credit for OPEB assets, future contributions or long-term investment rates. In such situations, the discount rate is calculated at the lowest possible rate which results in the higher liability.

The City manages its pension well, expecting to be fully funded by 2028 and currently almost 74% funded which places it ahead of most communities in Greater Boston, and the Commonwealth in general, however the City should create a strategy on how to address the OPEB liability. The process could begin by creating a committee with individuals educated in such liabilities.

### **New SEC regulation**

The Securities and Exchange Commission has approved two amendments to Rule 15c2-12. The amendments govern continuing disclosure requirements for issuers who are currently subject to Rule 15c2-12 with respect to annual disclosures and filings.

Due to these changes, effective February 27, 2019 any (1) "material" loan issued through the Department of Revenue (i.e. State House Notes), or (2) "material" leases issued or loans completed with the Massachusetts Clean Water Trust, MWRA, or USDA will require a disclosure to be filed no later than ten business days after the occurrence of the event.

In order to mitigate the consequences of a violation of these regulations, we suggest the following:

1. Send an email to all department heads asking them to report any possible leases (ambulances, fire apparatus, vehicles, technology, public works equipment, etc.) that may be entered into.
2. Call your financial advisor, and together make a determination if the financial obligation is material.
3. Disclose as deemed appropriate.

### **Process Manual**

In recent years, the City has experienced turnover in key financial positions. These include the City Treasurer and the Assistant City Controller who had worked for the City over 30 years. This sort of sharp transition makes it very difficult for successor employees to complete transactions in an efficient manner since much institutional memory is lost. This contributed to some of the issues you will read about later regarding reconciliations.

We suggest that the City create a process manual for each of the key financial departments; in effect a road map on how and when to complete transactions and where to retrieve the information necessary to complete those transactions.

### **Software System**

The City's current financial software system is about 10 years old and it has served the City well as a cost-efficient means of processing transactions. However, the vendor has undergone many transitions and two mergers since the software was first implemented in 2009. The latest news from the company is that at some point in the near future, as the company migrates three companies it has recently purchased into one software platform the City will have to convert its software.

Since the City has to complete this forced conversion of its software, it may make sense for the City to take this great opportunity and evaluate all software solutions available to it and make an informed decision in that regard.

### **III. FINDINGS AND RECOMMENDATIONS**

#### **Treasurer/Collector**

##### **A. Bank/Cash Reconciliation**

For the second consecutive year, the City was unable to reconcile its cash balances in a timely manner. This caused delays in completing the balance sheet, Schedule A, and the CAFR was placed on a 60-day extension. As a result, the DOR was unable to certify free cash in a timely manner.

The new Treasurer was appointed ½ way through fiscal 2018 and the prior Treasurer resigned before the end of fiscal 2017, thus the delay in this appointment impacted the completion of fiscal year 2017 records, which were not completed until March 2018. This caused a corresponding delay in closing the fiscal 2018 records. Compounding this was the retirement of the Assistant City Controller in March 2018.

The City was fortunate that it was able to reconcile the cash balances after this delay and the variances were not material.

Now that the new Treasurer and new Assistant City Controller each have a full-year under their belt, we will expect the fiscal 2019 records to be closed in a timely manner and that the two offices are communicating to each other monthly.

#### **City Response:**

There was a considerable delay in the fiscal year 2018 bank reconciliations due to the untimely resignation of the prior Treasurer as well as the length of time it took to fill the vacancy. Now that the current Treasurer has had time to get caught up it is expected that all fiscal 2019 reconciliations will be complete within 60 days of the end of the fiscal year.

##### **B. Interest Rate Reminder**

Over the past ten years, interest earned on bank deposits have not kept pace with inflation. Many bank depository accounts currently return far less than 1%. However, recent actions by the Federal Open Market Committee have had a positive impact on interest rates and there are a growing number of banks and financial institutions like the Massachusetts Municipal Depository Trust, or MMDT, that are financially stable and offer very liquid short-term investments with annual interest rates greater than 2% some approaching 3%. Many Treasurer's across the State have yet to react to these positive changes.

At year-end, the City's cash balances exceeded \$50 Million and most of these funds were invested in accounts that were still bearing low interest rates relative to current market. The lone outlier were 3 accounts with MMDT totaling about \$7 million.

The City generated about \$150,000 in interest income during fiscal year 2018; this could easily be increased to over \$500,000 and we suggest that efforts to create better returns are implemented.

City Response:

We have started to look at ways to increase interest earnings by opening accounts at new banks offering better rates. For fiscal year 2020, metrics will be established to track interest rate earnings with the goal to reach \$500,000 while preserving principal.

### **C. Withholding Accounts**

The City has yet to develop a reconciliation process for its Dental, Life insurance, short-term and long-term disability withholding accounts. These accounts continued to experience errors including the payment of July premiums in June. While these errors are not material to the overall financial status of the City it is still important to reconcile these on a timely basis.

City Response:

This is a policy that is discussed at length in a comprehensive financial policy manual that is scheduled to be completed during fiscal year 2019.

### **D. Abandoned Property**

Years ago, the City elected to treat abandoned property under *MGL Chapter 200 Section A*. This statute allows the City, through an advertising process, to revert abandoned property back to the City's Treasury if the abandoned property is not claimed within 1 year of advertisement.

The City's general ledger abandoned property account has not been updated in 5 years and has had the same balance in the general ledger account of approximately \$360,000.

We suggest the City update its abandoned property accounts by completing the following procedures:

1. Adjust the current outstanding balance of the abandoned property balances in the general ledger and record this as miscellaneous revenue in fiscal 2019.
2. Review items that meet the definition of abandoned that have yet to be advertised and apply the procedures required under *MGL Chapter 200 Section A*.

Once these procedures have been completed, the City will be up to date in its abandoned property accounts.

City Response:

The appropriate entries have been made in the general ledger and miscellaneous revenue has been credited with \$358,609.46 for fiscal year 2019.



### **E. Personal Property Receivable Balance**

Currently the City's general ledger includes a balance for personal property tax for fiscal year 2013 of about \$94,000 while the Collector's balance is approximately \$29,000. This variance has been maintained for a few years while the Collector investigated it. It was finally discovered that an error in the commitment process back in fiscal year 2013 was the major contributor to this error.

We suggest the amount is adjusted in the general ledger to equal the Collector's balance. All other variances in aggregate are not material.

This was reported in the prior year and has yet to be adjusted.

#### **City Response:**

The general ledger balance was adjusted during fiscal year 2019 to equal that of the Collector.

### **F. Collector/Controller Receivable reconciliation**

Currently, a reconciliation process between the Collector's subsidiary ledger and the Controller's control accounts in the general ledger is not completed. We reviewed both data sources and notwithstanding the adjustment required as discussed in section E. above, the variances are not material. However, a lack of reconciliation can lead to the issues that confronted the City a decade ago. We suggest such a process is implemented during fiscal 2019.

This is an item that can be included in the process manual previously discussed.

#### **City Response:**

This is a policy that is discussed in a comprehensive financial policy manual that is scheduled to be completed during fiscal year 2019. The Controller has implemented a monthly reconciliation process whereby he compares the general ledger control accounts to the Collector's subsidiary ledger and investigates any and all variances as they are identified on a monthly basis.

### **Fraud/Operational Risk Assessment (Update)**

As we have done in each of our last 9 management letters, we continue to advise Management to establish an internal audit process that would include risk assessment of all cash handling activities.

The most practical manner to accommodate such a process would be to establish a position within the Controller's Office that is dedicated to the design and implementation of internal control at the department level, as well as rotating risk assessment procedures of all cash handling activities. The MGL allows the Accountant or equivalent (Controller) this ability.

Currently, in lieu of an internal control function, the City continues to direct the Firm to audit departments from time to time.

The following audits were completed in the last three years:

1. Recreation Department
2. City Clerk
3. Police Details
4. Student Activities

The issues outlined in the **Recreation Department** review have been resolved.

With respect to the **City Clerk**; those cash handling processes were identified as the most severe and left the City exposed to high risk. Transition in both the City Clerk and Treasurer's department have made the recommendations challenging to implement, however we understand that a cash register process has been implemented and is currently in place.

The issues identified with **Police Details** are complex and will require planning amongst the Treasurer, Controller and Police Department. Those recommendations have yet to be implemented or addressed.

A separate report on **Student Activities** at each of the schools was issued to the school. This audit is required every three years. Corrective action plans are in place and the School Business Office has reached out to each of the schools to address the implementation of formal policies and procedures.

#### **Health Insurance Trust (Update)**

In the prior three years we alerted the City to a trend in its Health Insurance Trust Fund. The fund was established about 25 years ago and it allowed the City to self-manage its exposure to the risks associated with health insurance. For years it appeared this was the most affordable and efficient way the City could provide insurance to its employees.

The City began a practice in 2010 in which it reduced its health insurance appropriation in lieu of building reserves in the Health Insurance Trust. This practice worked well through fiscal year 2014 as the operating results for those years were positive and the funds used were replenished annually.

However, 2015 – 2017 proved challenging for the Health Insurance Trust as fiscal year 2017 ended with a deficit balance of approximately \$400,000.

The City responded to this comment aggressively and put in place a more conservative strategy with respect to the fund. The results were positive in fiscal 2018 as the fund ended the year with a balance over \$2.3 million. We encourage the City to continue these efforts.