

TOWN OF UPTON, MASSACHUSETTS

MANAGEMENT LETTER

YEAR ENDED JUNE 30, 2012

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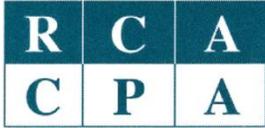
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TRANSMITTAL LETTER

The Honorable Members of the Board of Selectmen
Town of Upton
Upton, Massachusetts

In planning and performing our audit of the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Town of Upton, Massachusetts (the "Town"), as of and for the year ended June 30, 2012, in accordance with auditing standards generally accepted in the United States of America, we considered the Town'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 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.

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. However, material weaknesses could exist that have gone undetected.

This communication is intended solely for the information and use of management, the Board of Selectman, 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
January 23, 2013

I. OVERVIEW

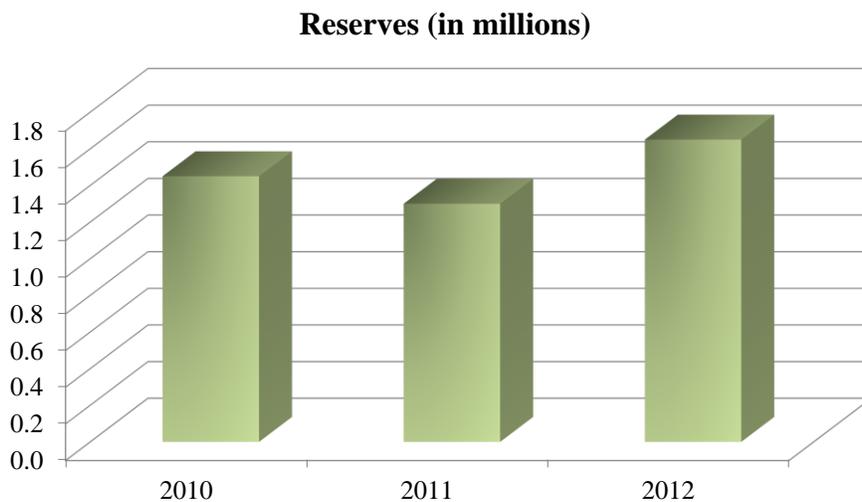
Financially speaking, 2012 was a year of mixed signals for the United States and Massachusetts' economies. Unemployment showed some improvement, but still remained near historic highs; and housing, construction and other indicators began to trend positive. Despite this, below forecast revenues for fiscal 2013 from the Commonwealth, the possible fiscal cliff and other available data show that the economy has yet to emerge from the recession that has plagued the area since 2009.

This is a signal that Towns must remain cautious while preparing their budgets. The fine balance of maintaining both reserves to satisfy rating metrics and an adequate level of services has become an increasingly complicated annual task.

Many towns have conceded to the pressure of maintaining services in lieu of building reserves and thus are facing the consequences of those decisions including downgrades to their credit ratings. The Town, however, has managed its financial operations well despite this prolonged challenge.

At June 30, 2012, the Town's unrestricted fund balance, or reserves, in its general fund increased nearly \$350,000 to approximately \$1,647,000 from the prior year. The Town has demonstrated its ability to implement an effective budget process without reliance on previously accumulated reserves.

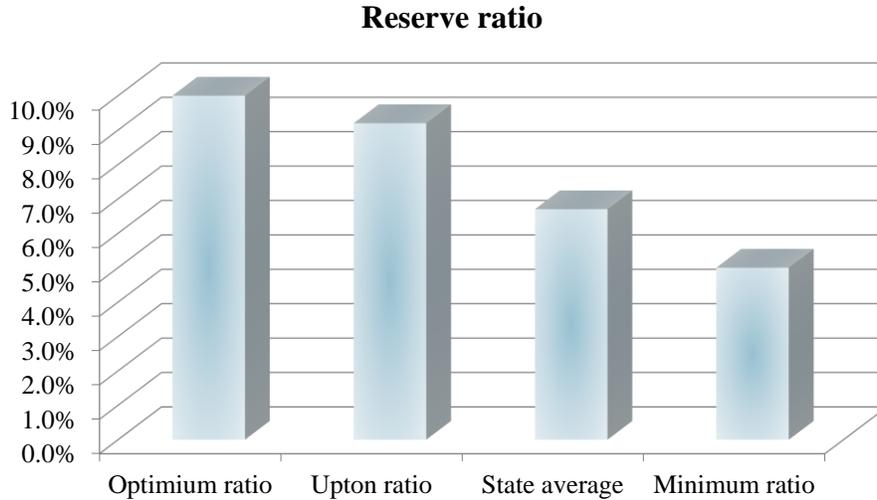
The following chart illustrates the recent trend in unassigned fund balance (calculated as undesignated fund balance plus stabilization under GASB 54):



Credit rating agencies place strong value on reserve balances as a ratio of general fund expenditures. The optimal ratio credit rating agencies will use in evaluating a town is a minimum of 5% and a target of 10%. The Town's 2012 ratio is 9.2%, which is an improvement over its 8.1% ratio at June 30, 2011. This reserve ratio is significantly greater than the state-wide average and is approaching the optimal target ratio of 10%.

This is the type of consistency that has allowed the Town to earn and maintain an AA rating from the bond rating bureaus and should be proud of these efforts on the financial front.

As can be observed in the illustration that follows, this is a very positive development for the Town:



The Town's bond rating is important. Maximizing the Town's bond rating, will minimize the cost of future borrowing for the Town.

Therefore, the Town should continue to strive towards maintaining and/or obtaining a higher bond rating thereby enhancing investment appeal. We encourage the Town to include the following items as it plans this process:

1. Make efforts to conserve free cash. I.e. avoid using free cash in the operating budget.
2. Take aggressive efforts to increase free cash and stabilization balances.
 - a. Continue to forecast revenues conservatively.
 - b. Implement efforts to enhance revenue. More aggressive tax collections through tax title and review current fees and departmental charges.
 - c. Continue to monitor budget and aggressively turn back funds to surplus.
3. Prepare a 5 year financial projection and continuously update it.
4. Adopt financial policies that direct the use, conservation and establishment of minimum balances for free cash and stabilization.
5. Evaluate increased funding for OPEB as part of its management of long-term liabilities.

We were first engaged to audit the Town's basic financial statements in fiscal year 2011 and issued a comprehensive letter to management dated December 21, 2011. Many of the recommendations in that letter to management were expected to be multi-year action items. The Town and its leadership have aggressively addressed the recommendations in our December 21, 2011 letter to management. This letter to management is intended primarily to provide the Town with an update on the Town's corrective actions.

II. INFORMATIONAL ITEMS

Statement on Auditing Standards No. 115 – Audit Communications

The American Institute of Certified Public Accountants (“AICPA”) recently issued Statement on Auditing Standards No. 115, *Communicating Internal Control Related Matters Identified in an Audit* (“SAS 115”). SAS 115 establishes standards and provides guidance on communicating matters related to an entity’s internal control over financial reporting identified in an audit of financial statements. In particular, SAS 115 provides guidance on evaluating the severity of deficiencies in internal control identified in an audit of financial statements in the following order:

1. Deficiency in internal control
2. Significant deficiency
3. Material weakness

Deficiencies identified as *significant deficiencies* or *material weaknesses* are required to be communicated to those charged with governance. *Deficiencies in internal control* are not required to be communicated; however we have chosen to also report these types of deficiencies in this report.

We did not deem any of the findings in this report to be categorized as either a significant deficiency or a material weakness.

III. FINDINGS AND RECOMMENDATIONS

Part 1 – New Item

Departmental Turnover Policy

In our report to management dated December 21, 2011, we recommended that the Town begin the process of creating a financial policies and procedures manual. The development of an effective financial policies and procedures manual and its approval and communication is generally a long-term project, particularly for a town like Upton that utilizes a part-time accounting resource. However, there are important policies and procedures that can be developed, approved and communicated to all Town departments in relatively little time such as a cash receipts turnover policy.

In connection with our audits of the fiscal year 2012 and 2011 basic financial statements and reviews of the business operations of three Town departments, it is apparent that departmental turnover policy for cash receipts is needed. We have observed that Town departments may possess cash receipts (in the form of currency, bank checks or personal checks) for as much as a month before turning over these funds to the Town's Treasurer/Collector.

We recommend that the Town develop a cash receipts turnover policy and communicate this policy to all departments that receive cash (in all forms) for services.

Part 2 – Previously Reported Items

Consideration of Fraud and Theft

In our letter to management dated December 21, 2011, we informed the Town of the heightened risk of fraud and theft Massachusetts municipalities now face by their employees, vendors, contractors and tax payers. We recommended that the Town (i) implement a written fraud policy and (ii) establish a limited internal audit process.

In its August 28, 2012 Town Meeting, the Board of Selectmen adopted the *Town of Upton Fraud Policy*, which addresses specific fraud risks the Town faces and action plans the Town will take in event that fraud is encountered, including whistleblower protections.

As we noted in our previous letter to management, the Town does not have sufficient resources to establish an internal audit function or engage a third party to perform these services. The Town has implemented a monthly budget to actual review process for not only expenditures, but also revenues, to assist the Town Manager in evaluating the operating effectiveness of Town departments and continually monitor the Town's budget. Furthermore, we observed that many departments regularly submit to the Town Manager operating metrics for analysis and benchmarking. This process is in its early stages; however valuable fiscal management objectives are being met with this new process. Furthermore, if used correctly, these analytical review procedures can provide effective oversight of the fiscal management of the Town's departments.

Policies and Procedures Manual

We recommended that the Town develop and communicate a formal set of financial policies and procedures that focus on (i) purchasing, (ii) cash receipts, (iii) human resources, (iv) investment management, (v) fraud and (vi) fixed assets. As expected, this is a long-term project that the Town has informed us is underway. To that end, a fraud policy has been implemented (see above). In addition, the Town adopted policies with respect to human resources that are very comprehensive and satisfy the human resource objectives of such a manual.

Regionalization

We recommended that the Town continue to seek out regionalization of certain of its municipal services as it had with its conservation agent, who is shared with Ashland. The Town has been diligently seeking ways to share costs with other area communities. To that end, effective January 1, 2013, the Town will enter into a regionalization program with Hopedale for dispatch services. This arrangement is expected to produce annual revenues of approximately \$50,000 for the term of the arrangement. We commend the Town on its regionalization efforts and encourage the Town's leadership to continue to seek additional regionalization relationships.

New Health Insurance Legislation

In our previous letter to management, we informed the Town of a newly enacted state health insurance law that requires the Town to conduct an enrollment audit not less than once every two years. The Town performed this analysis in the fiscal year 2012 and as a result, effective July 1, 2013 its health insurance premiums decreased over 5%.

Monthly Cash Reconciliation Process

We observed in the prior year that the results of the Town Treasurer's monthly bank reconciliation were not timely communicated to the Town Accountant. We were informed that these two offices have worked together to share this information on a more timely manner.

Check Stock

We noted that the Town's check stock was maintained by the Office of the Town Treasurer in a locked safe in their office together with a valid signature stamp. We recommended that blank check stock be stored in a secured location outside the Office of the Town Treasurer and that a check log be maintained that accounts for the sequence of check stock issued by warrant number and warrant date. The Town now stores blank check stock in another secured location and has implemented a check log.

Town Treasurer is an Elected Position

In our December 21, 2011 letter to management, we recommended that the Town consider a referendum to amend the selection method of its Treasurer/Collector to an appointment by the Town's Board of Selectmen or its Town Manager. While the current elected Treasurer/Collector possesses the skills necessary to support this position, future elected

Treasurer/Collectors may not. The Town indicated that it continues to evaluate this recommendation, however no decisions have been made by the Town's leadership in this area.

Short-term Disability Self Insurance

We reported in our previous letter to management that the Town self-insures its short-term disability, which exposes it to a variety of risks. We recommended that the Town investigate the cost effectiveness of implementing a short-term disability insurance policy in place of the current system used. The Town indicated that, effective July 1, 2012 it had secured short-term disability insurance with a third party insurer.

Master Payroll Database

We noted that the Town did not have a master payroll database in our prior year audit. This tool is instrumental in evaluating the weekly payroll vouchers presented to the Town for payment by the individual department heads and thereby functions as a key control element in the Town's payroll cycle. The Town has taken actions with its outside payroll processor to implement improvements in its payroll processes, which will provide Town leadership with easier and timelier reporting tools with respect to payroll.

Information Security

We observed instances in our previous audit in which information security needed improvement. To that end, the Town Treasurer/Collector has implemented a department information security policy to address these issues. We continue to reiterate the need for diligent information security for the Town's electronic and paper documentation, particularly with respects to personal information of its employees, contractors and tax payers.

Ambulance Billings

We noted in our December 21, 2011 letter to management that the Town had recently engaged a third party service provider to process its ambulance billings and collections. We recommended that the Town develop a formal policy with respect to the write off of contractual allowances and uncollectible accounts as soon as possible.

In its August 28, 2012 Town Meeting, the Board of Selectmen adopted the *Town of Upton Ambulance Write Off Policy*, which addresses the processes and controls placed in service to address ambulance billings, collections, adjustments and write offs.

Accounting System

We reported in our previous letter to management that the Town's integrated accounting system is cumbersome to operate at the Town Accountant level and that the existing software manufacturer is better known for its Assessing and Collecting capabilities. We recommended that the Town evaluate accounting software applications that integrate with their current vendor's Assessing and Collecting modules to determine whether another solution is both cost effective and efficient to use. The Town indicated that it continues to investigate alternative accounting applications, however it has not made a decision at this time and does not expect to make a decision on an alternative accounting system in the near future.

Water and Sewer Enterprise Funds

In our December 21, 2011 letter to management, we reported that the majority of the transactions of the Town's water and sewer enterprise funds were accounted for in the Town's general fund. As a result, a significant amount of additional work was needed to properly report the results of operations and financial position for these two enterprise funds. The Town indicated that, effective July 1, 2012, all of the operations of these two enterprise funds are being accounted for in separate enterprise funds within the Town's accounting records.

In addition, we recommended that the Town develop an indirect cost methodology for these two enterprise funds. The Town continues to evaluate indirect costs for its enterprise funds, however a formal indirect cost study/methodology has not yet been completed.

IV. DEPARTMENTAL REVIEWS

In connection with the financial statement audit, we performed certain procedures surrounding the cash management and recordkeeping for the Code Enforcement department. In addition, the Town requested that we visit with the two departments subject to similar reviews in the prior year to evaluate their progress in our recommendations. Departmental reviews are limited to areas of accounting and financial significance and therefore do not focus on operational effectiveness or efficiency.

As we reported in our letter to management dated December 21, 2011, we continue to observe the absence of formal policies and procedures relating to departmental finances (refer to our general recommendations in Section III). Effective policies clearly communicate what is expected of employees along with the intent and purpose behind the expectations. The use of this control mechanism would better ensure that transactions are authorized and assets are adequately safeguarded. Furthermore, in the event of personnel turnover, effective policies and procedures facilitate the transition of new personnel. We continue to recommend that the Town endeavor on a process over the next two fiscal years to have each department analyze their operations, assess the business and operating risks inherent within their operations and outline their key processes and internal controls. Policies and procedures should then be developed that are easy to understand and follow.

Part 1 – Current Year Departmental Review

CODE ENFORCEMENT

Code Enforcement generates revenues from permitting activities for (i) building, (ii) plumbing/gas and (iii) electrical/wiring. In fiscal year 2012, the Town reported \$109,160 in revenues. Expenses are primarily related to salaries and wages. The following revenues and expenses were reported in the 2012 accounting records:

	Fiscal Year 2012		Variance	
	<u>Actual</u>	<u>Budget</u>	<u>Dollars</u>	<u>Percent</u>
Building permits	\$ 76,845			
Plumbing/gas permits	13,500			
Electrical/wiring permits	<u>18,815</u>			
Total revenues	<u>109,160</u>	\$ 92,000	\$ 17,160	19%
Salaries and wages	126,033			
Other expenses	<u>14,404</u>			
Total expenses	<u>140,437</u>	<u>164,533</u>	<u>24,096</u>	15%
Funded through tax base	<u>\$ 31,277</u>	<u>\$ 72,533</u>	<u>\$ 41,256</u>	

The Department has a single full-time employee; six part-time employees are paid via a combination of stipends or stipends and a fee per inspection. There is no elected or appointed board to oversee Code Enforcement; the department head reports directly to

the Town Manager and meets with the Town Manager approximately twice a month for departmental updates.

Code Enforcement reports its operations each year in the Town's Annual Report. The information presented in the Town's Annual Report is based on the calendar year versus the Town's fiscal year. Code Enforcement receives a budget-to-actual report each month that details year-to-date activity in both revenues and expenses.

The Town Manager implemented an internal reporting requirement for Code Enforcement whereby Code Enforcement reports the monthly and fiscal year-to-date permit fees and numbers of permits issued (by type).

Based on our review of this department's operations, we are presenting the following recommendations to the Town:

Receipt Turnover

Receipts are turned over to the Town Treasurer/Collector approximately twice each month. Between turnovers, Code Enforcement regularly receives cash (in all forms) from permit applicants. Receipts are stored overnight in an unlocked drawer in a locked office that is monitored with up-to-date video surveillance equipment. We recommend that the Department (i) implement a policy to turn over receipts on a weekly basis, regardless of the amount of the turnover and (ii) purchase a safe for storage of its receipts prior to turnover to the Town Treasurer/Collector.

Use of a Signature Stamp on Payroll Warrants

We observed that the Department has used a signature stamp of its department head to authorize payroll warrant vouchers. Although there are a number of other mitigating controls in place, the use of a signature stamp on warrant vouchers should be avoided. We recommend that all warrant vouchers be signed in person versus through a signature stamp.

Manual Permitting

Code Enforcement's permitting process is entirely manual. We understand that the Town is currently investigating a computerized permitting application, which would facilitate the issuance, tracking and monitoring of permits issued by the Department and serve as a valuable reporting tool for both the Department and the Town. We recommend that the Town continue this process and select an appropriate application that is cost beneficial.

Pricing Update

Code Enforcement indicated that it last updated its pricing for plumbing, gas and electrical work permits over four years ago. We recommend that the Department perform a market analysis of permit fees from area towns and, if appropriate, implement a rate increase.

Part 2 – Update on 2011 Departmental Reviews

BOARD OF HEALTH

In our December 21, 2011 letter to management, we made a number of recommendations with respects to the Board of Health's financial operations. The following represents an update on these recommendations based on our inquiry and interview with an authorized representative from the Board of Health.

Cost Gap – Annual revenues generated from the solid waste program do not cover its expenses. We presented three alternatives to remedy this cost gap that included: (i) increase the revenues for solid waste trash bags, (ii) reduce costs of (iii) abandon this process entirely and provide solid waste trash disposal services to its residents as part of its general Town services. The Town continues to evaluate these alternatives; however a decision has not yet been made in this area.

Turnover Frequency – The Board of Health's turnover of its cash collections is, often times, not done in a timely manner. We recommend that the department turn over all cash and checks in its possession to the Town Treasurer on a timelier manner (at a minimum weekly). We reviewed the turnover frequency as reported in the Town's accounting records noting a slight improvement, however the timing of turnovers can still be improved. We recommended in Section III that the Town implement a departmental turnover policy for the entire Town.

Reconciliations and Recordkeeping – In our previous letter to management, we observed that the Board of Health maintains a manual system to account for trash bag sales on consignment. We recommended that the Board of Health implement improvements to its manual system. The Board of Health indicated that it continues to use its manual system in concert with a newly implemented off-the-shelf accounting application (QuickBooks), which tracks cash collections and inventory.

Operating Metrics

Based on our prior year review, the Board of Health accumulates operating data from third party haulers in an untimely manner. We recommended that the department diligently collect and record all key operating metrics and regularly compare this data to its revenue collections. We observed that the Board of Health's operating metrics data was timelier completed and that the department had performed analytic review procedures on this data versus monies turned over to the Town for collection fees.

Inventory Controls

Physical Inventory Counts – We recommended that the department perform periodic physical inventory counts of trash bags available for sale in our prior year review. The Board of Health indicated that it performs many informal physical inventory counts throughout the course of the fiscal year and compares these results with those in its records. Furthermore, the manual process in place appears to be sufficient in tracking trash bags delivered to outside convenience stores.

Inventory Security – We recommend that the Board of Health change the physical security of its storage shed for trash bags as it was easily susceptible to theft. The department corrected this security flaw.

Permitting

We recommended that the Board of Health implement the use of pre-numbered permits or implement an automated permitting system if deemed cost effective. The Town is currently in the process of evaluating an automated permitting system that can be used throughout all Town departments that issue permits.

RECREATION COMMISSION

In our December 21, 2011 letter to management, we made a number of recommendations with respect to the Recreation Commission's financial operations. The following represents an update on these recommendations based on our inquiry and interview with an authorized representative from the Recreation Commission.

Recordkeeping and Operating Metrics

We recommend that the recreation department consider implementing an off-the-shelf accounting package such as QuickBooks or Quicken to track its selling transactions as well as implement an Internet-based activity registration system that is capable of accepting payment via credit and debit cards.

The department indicated that it continues to use Excel to account for its finances; however it had recently implemented an online activity registration system with ecommerce capabilities. This system was rolled out in the summer of 2012 and the department expects to fully adopt it for the majority of its activities in fiscal year 2013. This system can also track operating metrics like numbers of paid participants per program, which can provide valuable information to the department's management.

Reconciliations

In our December 21, 2011 letter to management, we noted that the recreation department does not reconcile its activity with the activity recorded by the Town Accountant in the Town's accounting records. We recommend that, once our recordkeeping recommendations are implemented, that the recreation department review the monthly activity posted in the Town's accounting system to its own records. The department indicated that, effective July 1, 2012, it receives monthly reports from the Town Accountant and will begin meeting with the Town Accountant monthly to review its financial results.

Inappropriate Accounting Practices

In our December 21, 2011 letter to management, we noted that the department engaged in two activities that were inappropriate accounting practices according to Massachusetts General Law. The department indicated that it had ceased all activities related to the sale of ice cream concessions to the public. Furthermore, the manner in which the department

organized its basketball program has been redesigned and all payments to referees now run through the Town's warrant process.

Safeguarding Assets

Cash – In our prior year review, we noted cash received by recreation department personnel may, at times, be taken home at the end of a day as opposed to having been counted, recorded and stored in a safe. We recommend that the recreation department implement a policy requiring that all cash collections be counted, recorded and deposited into a safe at the end of each day. The department indicated that through the implementation of its online activity registration system, this issue has been significantly mitigated as most department collections are now made through a credit or debit card.

Fidelity Bonds – We recommend that the Town evaluate this risk and determine if fidelity bonds are cost effective. Furthermore, we recommend that the Town evaluate its current insurance policies to determine if employee fidelity is covered as well as evaluate its other tort coverages in light of kinds of activity performed within this department. We were informed that this is still under review by the department and the Town.

Personnel Matters

The recreation department has year-long employees and many seasonal employees. Personnel management is therefore a key business cycle for the recreation department.

Information Security – We recommended that the recreation department review its internal information security procedures, particularly with respects to sensitive employee personal data. The department indicated that it takes greater caution with this type of data, changed many of its forms to remove the association of names with social security numbers and, where needed, secures personnel data in a locked file cabinet.

Timesheets – We suggest that the department transition to a more technologically efficient and accurate manner of tracking time, through either a punch clock or biometric (thumb push) means the use of timesheets serves as a key control in the personnel management business cycle. We were informed that a biometric time clock was implemented in the summer of 2012 and was used in concert with the department's manual time sheet system. The department is working with the Town to fully adopt the biometric clock system into its payroll warrant process.

Long-term Capital Improvement Program

We recommend that the recreation department develop a long-term capital improvement plan. Investments in infrastructure may create additional revenue-generating programs for the recreation department. The department and the Town continue to work on this area.

Internet Access

The recreation department facility does not have access to the Internet. There were several recommendations in our December 21, 2011 letter to management that could be facilitated with Internet-based applications. Furthermore, without Internet access,

recreation department personnel cannot access email, which is a principal means of communication in today's world. We recommended that the recreation department investigate the cost benefit of securing wireless Internet access for itself. The department indicated that, effective late fiscal year 2013, it will have Internet access.
