



Lefkowitz, Garfinkel, Champi & DeRienzo P.C.
Certified Public Accountants / Business Consultants

February 12, 2010

The Honorable President and
Members of the Town Council
Town of Lincoln, Rhode Island
Lincoln, Rhode Island

In planning and performing our audit of the financial statements of the Town of Lincoln, Rhode Island (the Town) as of and for the year ended June 30, 2009, in accordance with auditing standards generally accepted in the United States, we considered the Town'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 our 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.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. However, as discussed below, we have identified deficiencies in internal control that we consider to be significant deficiencies and other deficiencies that we consider to be material weaknesses.

A control deficiency 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 financial statement misstatements on a timely basis. A deficiency in design exists when a control necessary to meet the control objective is missing, or when an existing control is not properly designed so that even if the control operates as designed, the control objective is not always met. A deficiency in operation exists when a properly designed control does not operate as designed or when the person performing the control does not possess the necessary authority or qualifications to perform the control effectively.

A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the Town's ability to initiate, authorize, record, process or report financial data reliably in accordance with accounting principles generally accepted in the United States such that there is more than a remote likelihood that a misstatement of the Town's financial statements that is more than inconsequential will not be prevented or detected.

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We consider the following deficiencies to be significant deficiencies in internal control:

Pension Trust Fund (Town-wide):

Observation:

The Town maintains a Pension Trust Fund that covers substantially all Town and School Department employees not covered by other plans, as well as certain non-Town employees such as Fire District firefighters. The Plan's primary custodian is John Hancock Life Insurance Company, which provides the Town with quarterly statements of investment performance and activity. Contributions received from non-employee units of the Town and other Town Departments are deposited into the General Fund checking account. The Town has employed the services of the same actuary for the past seven years. The Town was unable to provide the auditors with a statement on the actuary's certifications, qualifications and licensure when requested to do so. The Town Finance Department records the pension fund investment and certain contribution activity only on an annual basis, even though contributions may be submitted on a bi-weekly basis. In addition, certain prior year contributions were incorrectly recorded, resulting in a prior period adjustment of an increase to the Pension Trust Fund's net assets of \$206,578.

Recommendation:

We recommend that the Town Finance Department review its procedures related to the Pension Trust Fund; record investment and contribution activity on a periodic (quarterly) basis; open a separate checking account for the Pension Trust Fund so as to avoid the commingling of Trust fund receipts with operating funds; and obtain, review and maintain on file the certification, qualifications and licensure of the Town's actuary and other service providers, as appropriate. In addition, the Town may want to seek proposals from qualified firms for actuarial services on a more periodic basis.

Response:

Recommendations received through the audit process will be implemented and the Town will be soliciting proposals for actuarial services during this fiscal year.

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Cash Procedures (Water Commission):

Observation:

The Town Charter specifically requires the Town Finance Director to 1) maintain “custody of all public funds belonging to or under the control of the Town, or any department, office and agency of the Town government, including the School Department and the Board of Water Commissioners,” 2) “receive all license fees, rents, funds, moneys receivable” and 3) “have custody of all invested funds of the Town.” During the course of our audit, we determined that the Water Commission maintains an actively used account where the Town Finance Director is not a signatory and the existence of which the Town Finance Director was unaware. The Water Commission deposits a substantial portion of its receipts into this account and then transfers funds, as needed, to the operating account to fund routine disbursements that are forwarded to the Town Finance Director. However, we also noted several direct disbursements from the account for minor purchases which were not reported to the Town Finance Director.

Recommendation:

We recommend that a review be made of the necessity for maintaining the separate account for depository purposes, as deposits can just as easily be recorded in the regular operating account, thereby eliminating the need to make transfers to fund payables. In the unlikely event that the separate account is determined to be necessary, the Town Finance Director should be included as a signatory on the account, and direct disbursements from the account (other than transfers to the operating account) should cease.

Response:

We agree and will implement procedures to comply with the recommendation.

Deferred Revenue (Water Commission):

Observation:

The Water Commission records estimates for the construction of new water services as an account receivable and deferred revenue on its general ledger. At the time of recording, no payments related to the new water service have been received, and no work performed relating to the installation of the new service has been performed. The Water Commission generally does not begin work on the service until 100% of the estimate is collected. As such, no receivable or deferred revenue exists; the recording of the estimates results in an overstatement of both accounts receivable and deferred revenue. Furthermore, when a customer chooses not to install the service, no entry is made to remove the recorded receivable or deferred revenue. We noted recorded “receivables” and “revenues” dating back several years recorded on the general ledger. As a result, we proposed an adjustment recording a contra receivable account, thereby reducing receivables and deferred revenue by \$95,753.

Deferred Revenue (Water Commission) (Continued):

Observation (continued):

Billings for residential water usage is done in two cycles for each district within the Town. The first billing is based upon a 20,000 gallon advanced minimum usage; the second billing is based upon meter readings, less the amount advance billed. We were informed that the advanced minimum billing is non-refundable and non-transferrable. For example, the advanced minimum billing done for District 1 in May 2009 covered the period October 2008 through September 2009. In prior years, the Water Commission included the initial minimum billing in deferred revenue rather than as revenue earned within the fiscal year. This resulted in a prior period adjustment in the current year's financial statements of \$160,875.

Recommendation:

We recommend that the Water Commission revise its procedure for recording the estimated charges due for new water services. General ledger entries should not be recorded until such time as a payment is received. Maintenance of proposals or estimates for future services should be maintained outside the general ledger system, as no transaction has occurred.

We further recommend that the Water Commission review its procedures for recording of advanced minimum billings based upon the period covered by the billing and the date of the advanced minimum billing. We also recommend that the Water Commission review its policy regarding the non-refundability and non-transferability of the residential advanced minimum billings.

Response:

We agree and will implement procedures to comply with the recommendations.

Activity Funds (School Department):

Observation:

The School Department maintains several Agency Funds, consisting of the High School Activity Fund(s), Camp Bournedale Activity Fund and Middle School Activity Fund. The balance within one of these Activity Funds exceeds \$100,000. We did not audit the activity within these funds; however, we observed that there appears to be insufficient oversight by the School Business Office on both expenditures and transfers within the funds. The oversight and responsibility over funds belonging to students or student organizations falls under the School Department's fiduciary responsibility umbrella.

We noted that the activity in the Middle School Activity Fund is reviewed and formally recorded only on an annual basis. The Middle School Activity Fund bank account reconciliation was not performed or reviewed on a monthly basis.

Activity Funds (School Department) (Continued):

Observation (continued):

We noted that activity in all agency accounts is reviewed and recorded only on an annual basis. We also noted that the review process is cursory, at best. For one high school Activity Fund, the custodian decided to open up a share account and two \$50,000 certificates of deposit by transferring monies under the custodian's control from one financial institution to a second institution, without the knowledge or authorization of the School Business Office. The High School principal was aware of and authorized the transfer in accordance with the Student Activity Fund Policy. The transfer was recorded as a disbursement in the Activity Fund, and the Business Manager inadvertently overlooked the transfer, summarizing the activity, resulting in an understatement of \$102,616 in the recorded Activity Fund cash balance at year-end.

Recommendation:

We recommend that the School Department adhere to the School Committee's written policies and procedures for control over the student activity funds at the schools, which include procedures for 1) performing monthly reconciliations, 2) requiring monthly review of reconciliations by the School Business Manager, 3) reviewing receipts and disbursements for propriety by persons that do not have custody or control of the funds, preferably the School Business Manager and 4) insuring that accounting records are updated on a monthly basis.

Response:

We agree that the School Committee's written policies and procedures for control over student activity funds must be followed. Currently, the School Business Manager reviews all of the activity funds on a monthly basis except for the Middle School Activity Fund. We are currently in the process of automating the accounting process for the Middle School Activity Fund and fully expect to have monthly expenditure reports, monthly bank reconciliations and transfer reviews for this fund completed shortly.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected.

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We consider the following significant deficiencies to be material weaknesses:

Financial Reporting and Close Process (Town-wide):

Observation:

The Town Charter vests responsibility for the Town's finances, including those of the School Department and the Water Commission, and financial reporting with the Town's Finance Director. Accounting principles generally accepted in the United States also mandate that management of the Town is responsible for the Town's financial statements and external financial reporting. Recently issued auditing standards require the independent auditors to assess the Town's capability to prepare financial statements in accordance with generally accepted accounting principles applicable to government entities and to communicate that evaluation to "those charged with governance" within the government, generally the Town Council. These standards also require Town personnel to be responsible for the selection and implementation of appropriate accounting policies and internal controls, and possess the ability to complete the financial statements and required disclosures.

Historically, the Town's Finance Director has not exercised significant review or taken responsibility for the accounting policies and internal control procedures within the School Department and Water Commission. Annually, the auditors would obtain information provided by the School Business Manager and the Water Commission's Administrative Assistant, without prior review for accuracy by the Finance Director. In addition, prior to 2009, the Town relied on the auditors to prepare the financial statements, including the disclosures required by accounting principles generally accepted in the United States.

Independent auditors are required to assess whether the Town has properly designed controls placed in operation to prepare financial statements in accordance with accounting principles generally accepted in the United States. As a result of that assessment, and the number of entries that were required to adjust the Town's financial statements to conform to those accounting principles, we believe that the Finance Director has not exercised the degree of control and responsibility required by both the Town Charter and accounting principles.

The inadequacy of the Town's financial close process was cited by the Town's predecessor auditors as a material weakness in internal control and has not been adequately addressed.

Recommendation:

We recommend that the Finance Director oversee the operations of the Water Commission and evaluate the capabilities of staff, the adequacy of the accounting system, the selection of accounting policies, and the preparation of monthly financial statements in accordance with accounting principles generally accepted in the United States. This appears to be required by both the Water Commission's Charter and the Town's Charter which was approved subsequent to the date of the Water Commission's Charter.

Financial Reporting and Close Process (Town-wide) (Continued):

Recommendation (continued):

Furthermore, in order to fulfill the requirements of monthly reporting of the Town's financial condition and revenue and expenditures required by the Town Charter, we recommend that the Finance Director revise procedures in collaboration with the School Business Manager for the timely submission of monthly financial information and reports "in sufficient detail to show the financial condition of the Town" prepared in accordance with both the budgetary basis of accounting or the government funds basis of accounting for all funds maintained by the School Business Office. In addition, the Finance Director and School Business Manager should develop an appropriate protocol to enable the Finance Director to exercise oversight over School Department purchases and expenditures, as required by the Town Charter.

Response:

The Water Commission and School Department have historically been granted certain levels of autonomy through state legislation. The Water Commission jurisdictional issue mentioned in the recommendation is acknowledged and should be addressed by the Town Council and the Water Commission. As these relationships are clarified, the oversight of the financial systems of the water department should be changed to allow for compliance with the recommendation.

The School Department does provide details of its payments due as approved by the school committee. Authority over purchasing decisions and processing remains under the control of the school department staff. Consistent with authority granted in state law, the responsibility of the finance office is a ministerial review in order to verify an overall compliance with the total appropriated budget for the fiscal year. Any changes to these current procedures will require changes in staffing within each department and a more direct participation of Town finance staff in the affairs of the School Department. There is no objection to such a change, but it will require a cooperative effort between the two governing bodies to be successfully accomplished.

The finance office is in agreement with the recommendation that the monthly financial reporting received from the School Department be forwarded to the finance office early enough to be included in the monthly report to the Town Council. Our previous request was unsuccessful.

Additional efforts to increase the amount of information coming to the finance office for review and oversight will be attempted.

Communications (Town-wide):

Observation:

The 1992 Integrated Framework on Internal Control issued by the Commission on Sponsoring Organizations (COSO), and adopted by the Government Accounting Office in 2004 as applicable to governments at all levels, lists the fundamental and essential objectives of any government as:

- Economy and efficiency of operations, including safeguarding of assets and achievement of desired outcomes;
- Reliability of financial and management reports; and
- Compliance with laws and regulations.

While most governments have implemented many of the recommended elements of the Control Environment and Control Activity components of the COSO report, an equally important component is Information and Communications. This component emphasizes both the **quality** of information generated within the government and the **effectiveness** of communications, whether written or oral in achieving the goals listed above, particularly as they relate to the government's ability to prepare accurate financial information on a timely basis. This requires an integrated accounting system and sufficient oral communications among those charged with the responsibility to maintain accounting records to ensure that the financial information being generated by the accounting system is accurate.

We observed a lack of timely communication among the Town's Finance Department personnel, the School Business Office personnel and the Water Commission personnel. While information may be provided among departments on a periodic basis, it is unclear whether any significant use of that information is made. For example, the interfund account balances between the accounts maintained by the School Department and those maintained by the Finance Department as of June 30, 2009 were not reconciled until January 5, 2010, a full six months after the closing of the Town's fiscal year-end, and the differences were material to the Town's financial statements. Furthermore, the Town's capitalization policy had apparently not been communicated adequately to the Water Commission, as numerous small dollar items below the capitalization threshold were recorded as capital assets. Furthermore, the information that is provided does not meet the basic requirements of financial reporting. The School Business Office does not prepare monthly financial information in sufficient detail (for example, a balance sheet) or submit the information sufficiently timely to the Town Finance Department for its review and inclusion in the reporting packages provided to the Town Council, and the Water Commission does not prepare complete financial statements, but simply a monthly budget variance report without significant explanation of variances.

Communications (Town-wide) (Continued):

Observation (continued):

At year-end, when the Town must prepare the government-wide financial statements, information for capital asset additions must be provided in sufficient detail to be entered into the capital asset management software for control and depreciation purposes. For example, if the School Department acquires assets that are at several locations, that information needs to be communicated to the Town Finance Department in order to be appropriately classified and sited. Such information was not communicated on a timely basis in 2009.

The Town's failure to timely reconcile interfund accounts was cited by the Town's predecessor auditors as a material weakness in internal control and remained uncorrected throughout the year.

Recommendation:

We recommend that the Town develop a system of communication that includes an integrated accounting system and enhanced oral communications among departments of the Town in order to facilitate the timely preparation of monthly and annual financial statements and adherence to the provisions of the Town Charter.

Response:

The finance office will continue to strive to obtain complete information from the School Department in order that the inter-fund balance that was finally reconciled as of June 30, 2009 can be maintained and reconciled at least quarterly. This endeavor will require the assistance and cooperation of the governing bodies and chief administrators of each department in order to be successful.

Future requests for the information necessary for the successful and timely completion of monthly and annual reports, as well as a more timely completion of the annual audit, will be undertaken.

Capital Assets (Water Commission):

Observation:

We noted that the Water Commission maintains a listing of its capital assets and related depreciation utilizing Microsoft Excel spreadsheets. However, during our audit we noted that the information included on the spreadsheets (cost, accumulated depreciation and depreciation expense) was not reconciled to the Water Commission's general ledger. Summary analyses of capital assets by general ledger classification submitted to the auditors as being derived from the spreadsheets were revised multiple times, and did not include all assets acquired during the current fiscal year. The spreadsheets do not show beginning of year accumulated depreciation, current year depreciation and end of year accumulated depreciation for each individual asset; as a result, assets previously disposed of continue to be depreciated under the system utilized by the Water Commission.

Capital Assets (Water Commission) (Continued):

Observation (continued):

We also noted that revenues collected by the Water Commission were recorded as reductions in the cost of capital asset additions. This resulted in an increase in capital assets of \$214,063, an increase in the infrastructure rehabilitation revenue account of \$366,239, with the difference increasing expenses.

As discussed under the caption ***Loan Payable***, below, capital asset additions acquired with proceeds from certain loans were unrecorded on the general ledger of the Water Commission.

Journal entries provided to us by the Water Commission's Administrative Assistant to reconcile capital asset records to the general ledger were clearly in error and were revised multiple times. It became clear to us that the Administrative Assistant did not have a clear understanding of capital asset recording procedures. Similar material weaknesses concerning capital asset recording were noted in prior years by the Town's former independent auditors.

As noted previously under ***Communications***, above, the Water Commission failed to follow the Town's capitalization policy (minimum item cost of \$5,000 **and** a minimum useful life of at least 2 years) with respect to many purchased small dollar items, such as valves, meters and services. While purchased small dollar items should be inventoried and kept under physical control, perpetual recordkeeping, including calculation of depreciation and ultimate disposal, is unnecessary and contrary to the Town's capitalization policy.

Substantially all of the above conditions were cited by the Town's predecessor auditors as material weaknesses in internal control and remained uncorrected throughout the year.

Recommendation:

We recommend that the Water Commission upgrade its capital asset subsidiary ledger to include an item by item listing of capital assets that agrees, by classification, to the Water Commission's general ledger. Furthermore, the Water Commission should invest in a capital asset management program that identifies the depreciation and accumulated depreciation by individual asset and reconciles to the Water Commission's general ledger. Revenue collected should rarely, if ever, be recorded as a reduction to capital asset additions, except in the case of insurance proceeds from an involuntary conversion. Finally, the maintenance of capital asset records should be delegated to an individual with sufficient understanding of capital asset transactions and recording procedures so that future errors can be eliminated.

Response:

We agree and will implement procedures to comply with the recommendation.

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Loan Payable (Water Commission):

Observation:

The Water Commission has a loan payable to the Rhode Island Clean Water Finance Agency (RICWFA). The general ledger recorded balance of this loan is not adjusted on a monthly basis in accordance with the terms of drawdown and/or repayment; for example, loan disbursements of \$68,776 from RICWFA to the Water Commission were not recorded. We confirmed the loan payable balance with RICWFA, noting that the June 30, 2009 balance did not agree with the confirmation that was received. This resulted in audit adjustments amounting to a net increase in loans payable of \$140,999 and an increase in capital assets of \$68,776, amounts which are significant to the Water Commission's financial statements.

This situation was cited as a material weakness in internal control by the Town's predecessor auditors, and remained uncorrected throughout the year.

Recommendation:

We recommend the Water Commission update its procedures relative to its transactions with RICWFA and reconcile the loan payable balance on its general ledger against the loan statements provided by RICWFA on a monthly basis. Furthermore, any capital asset additions resulting from drawdowns of RICWFA funds should be recorded and depreciated once placed in service.

Response:

We agree and will implement procedures to comply with the recommendation.

Transfer Recording Errors (School Department):

Observation:

The COSO report noted previously cites one of the components of internal control as monitoring of routine transactions through a series of control procedures, review of unusual or nonrecurring transactions by persons separate from the initiator of the transaction, and assessing the risk of error and/or management override in the preparation of financial statements.

Transfer Recording Errors (School Department) (Continued):

Observation (continued):

In fiscal 2008, the School Committee authorized the transfer of \$150,000 of excess funds from the School Unrestricted Fund to the School Capital Reserve Fund maintained by the Town. On June 27, 2008, the School Business Manager drew a check for \$150,000 payable to the Town, charging seven fuel accounts, in error, in amounts ranging from \$25,000 to \$50,000. For some reason, the School Business Manager failed to deliver the check to the Town until October 24, 2008. Since the check was long-outstanding and “held” at June 30, 2008, the prior Town auditors proposed that the check be “reversed” as of June 30, 2008 and proposed an entry to reverse the check (also made in error), recording a liability, rather than reducing (the incorrectly charged) fuel expenditures. When the check was received by the Finance Director in October, without instruction, it was “held” by the Finance Director and not deposited into the Capital Reserve Account. On June 25, 2009, the Town Administrator authorized the use of the money toward renovation of the band room at Lincoln High School, and the Finance Director and Business Manager determined that the long-outstanding check should be voided and reissued. The Finance Director then deposited the check into the Town’s Capital Reserve Account before the close of the 2009 fiscal year. In the meantime, InSight reports were filed with erroneous fuel expense amounts, budgetary based financial statements were issued which showed over-expenditures in several fuel accounts, the subsequent year’s budget for fuel was based upon erroneous and inflated “actual” data and the prior year’s audited financial statements contained a significant error.

While we view the series of events as unintentional errors that led to significant errors in the prior year’s financial statements, with diverse effects on the current year, the primary cause of the errors appears to be a lack of understanding of how to record fund transfers and the lack of communication between the School Business Department and the Town Finance Department.

Recommendation:

We recommend that the School Business Manager and the Town Finance Director increase communication between the two offices, refamiliarize themselves with the principles of fund transfer accounting and utilize those principles where appropriate when transfers are made. We also recommend that an individual, other than the person assigning charge codes and recording transactions at the School Business Department review and monitor the original assignments and recording for accuracy and appropriateness. Finally, we recommend that the Town Finance Director prescribe and maintain accounting processes and procedures in collaboration with the School Business Manager as contemplated by the Town Charter.

Response:

We agree that communication between the Town Finance Director and the School Business Manager must increase not only in frequency but in quality. Collaborating to formulate accounting processes and procedures is a good way to begin enhanced communications.

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We identified the following control deficiencies that we determined do not constitute significant deficiencies or material weaknesses:

Water Purchases (Water Commission):

Observation:

We noted certain surcharge fees paid to the Providence Water Board and the Rhode Island Resources Water Board were recorded as reductions of fees revenue collected from Water Commission customers. This resulted in an understatement of revenue and an audit adjustment amounting to a net increase in fees expense and fees revenue of \$169,800.

Recommendation:

We recommend that the Water Commission revise its procedures to ensure that surcharge fees collected from customers are recorded appropriately as revenue, rather than as a contra expense.

Response:

We agree and will implement procedures to comply with the recommendation.

Accrued Compensated Absences (Water Commission):

Observation:

The Water Commission incorrectly recorded accrued compensated absences by not including FICA taxes and pension contributions payable for those compensated absences. This resulted in audit adjustments amounting to a net increase in accrued compensated absences of \$25,199.

Recommendation:

We recommend that the Lincoln Water Commission revise its calculation of accrued compensated absences to include the associated FICA taxes and pension contributions.

Response:

We agree and will implement procedures to comply with the recommendation.

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Police Detail Revenue and Expenditures (Town):

The Town provides police details for various events and projects throughout the Town and bills the appropriate parties for the cost, including an allocation of benefits, for the police detail services. The Town maintains control over unpaid amounts and has been very successful in both billing and collecting amounts for such services.

Because the Town maintains its books on a budgetary basis of accounting, and police detail revenue and expenditures are not budgeted, the Town records both the expenditure and the billing to accounts receivable (a balance sheet account). Neither the payroll cost nor the related billing is presented as expenditures or revenues throughout the year, other than the net revenue effect. As a result, an adjustment to revenue and expenditures in the amount of \$569,444 was required.

Recommendation:

We recommend that the police detail billings and expenditures be recorded in the revenue and expenditure accounts on a monthly basis. Such revenue and expenditures can be grouped so as not to distort budget to actual comparisons that are presented to the Town Council on a monthly basis.

Response:

We agree with the recommendation and have implemented the change.

Management of Federal Funds (School Department):

Observation:

In requisitioning federal funds as reimbursement for various programs, the School Department utilized an incorrect pension contribution rate, resulting in an over-requisitioned amount of approximately \$42,000. It should be noted that there were unprecedented changes in the pension rate for federal programs in July 2009 retroactive to fiscal 2008.

The School Department participates in the National School Lunch Program. That program requires that the School Department determine participation based upon specified eligibility requirements. We noted several instances of incorrect level of eligibility determination at two schools and the use of outdated eligibility applications at several schools. These errors resulted from the failure of the School Department to adequately review eligibility calculations at the individual school sites. This condition was cited by the Town's predecessor auditors as a significant deficiency in internal control and was addressed throughout the year, resulting in significantly fewer errors occurring in the current year.

Management of Federal Funds (School Department) (Continued):

Observation (continued):

The School Lunch Program service provider failed to monitor and adequately inventory commodities received under the National School Lunch Program. While utilization of such commodities reduces the overall cost of the lunch program, the federal government requires that requisitioning and usage of commodities be monitored and a perpetual inventory of usage and unused commodities be maintained.

The School Lunch Program service provider submits a monthly operating report to the School Department. That operating report details cash sales by type (breakfast, lunch, adult, etc.). Daily, a deposit slip is prepared and brought to the bank by the service provider; the receipted deposit slip is given to the School Department Business Office and used as the basis for recording School Lunch Program revenue. The School Department does not attempt to reconcile the daily cash receipts with the monthly operating report of sales revenue provided by the service provider to determine that all sales are recorded as revenue on the School Department's general ledger.

Recommendation:

We recommend that the School Department review its policies and procedures to ensure that compliance requirements for charging of fringe benefit costs to federal programs are being met.

We recommend that the School Department monitor expenditures under federal programs and requisition funds from the federal government on a periodic basis to facilitate cash flow.

We recommend that the School Department review the operation of the National School Lunch Program to ensure that: 1) a sufficient review of eligibility determination is performed by someone other than the individuals making the initial determination, 2) its service provider adheres to compliance requirements of the program, 3) a monthly reconciliation of cash sales and cash deposited is performed to ensure that all receipts are accounted for; and 4) controls surrounding the collection and deposit of cash by the service provider are properly designed and placed in operation to ensure that all cash collected by the service provider is deposited.

Response:

We agree. The compliance requirements for charging of fringe benefit costs to federal programs must be met and we will be diligent in insuring that fringe benefit rates are charged correctly even if there is additional statutory change at the end of any fiscal year. Federal funds will be requisitioned on a quarterly basis. Finally, the School Lunch application process was centralized for the 2009-10 school year and we believe that issues surrounding eligibility were addressed. We will begin the process of a monthly reconciliation of cash sales and cash deposits and will review the procedures regarding the collection and deposit of cash by the service provider to insure that chain of custody is strictly adhered to so that all the cash collected is deposited.

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The following items are brought to your attention, not as control deficiencies or immaterial instances of non-compliance, but rather as items for your consideration.

Federal Program Reimbursements (School Department):

The School Department provides services to students under a variety of federal programs (such as Title I, IDEA Part B and Title II, etc.) utilizing, in part, federal financial assistance in combination, in certain cases, with a local share. The federal financial assistance carries with it eligibility requirements and restrictions as to the use of funds and the timing, calculation and method(s) of requisitioning of those funds. The School Department did not request reimbursement from the federal government for both Title I and IDEA until after the close of the year, even though salaries and other expenditures had been made throughout the year. The programs permit requisitioning of funds on a periodic basis in order to facilitate cash flow.

In 2009, the School Department was successful in securing ARRA funds to partially fund salaries for aides in the IDEA program for the period April through June. The ARRA funds were required to be deposited in a separate restricted fund bank account. A portion of the aide salaries were funded through the operating account prior to the receipt of the ARRA funds in July, and the School Department deposited the ARRA funds into the operating account because the funds had been expended and guidance received from the Rhode Island Department of Education did not specify that a separate fund should have been used. In the future, ARRA monies received PRIOR to expenditure should be accounted for through a separate fund.

Response:

The Rhode Island Department of Education's Uniform Chart of Accounts (mandatory for all Rhode Island District's beginning July 1, 2009) requires separate funds for all ARRA receipts and expenditures. For fiscal 2009, Lincoln was not subject to the rules of the Uniform Chart of Accounts and followed RIDE's guidance that required only the ability to separately account for the expenditures.

Reduction in Number of Funds and Impact of GASB Opinion 54 (Town-wide):

The Town and School maintain their books using a series of more than 70 "funds" besides the General Fund and the School Unrestricted Special Revenue Fund. Substantially all of these funds are "special revenue" funds. Recently issued Governmental Accounting Standards Board Opinion No. 54 (GASB 54), which becomes effective for fiscal 2011, eliminates the use of "special revenue" funds except in certain specific instances, such as restricted Federal funds or if required by grantors outside of the Town government. As a result, a substantial number of "special revenue" funds will need to be collapsed into the General Fund, and to a lesser extent, the School Unrestricted Special Revenue Fund. Management should begin the process of reviewing its special revenue funds to determine which ones meet the criteria for continued classification as "special revenue" funds, and consolidating those that do not into the General or School Unrestricted Fund during the 2010 fiscal year.

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Reduction in Number of Funds and Impact of GASB Opinion 54 (Town-wide) (Continued):

In addition, GASB 54 revises the classifications of fund balance, eliminating terms such as “reserved” and “designated” and replacing them with a series of other classifications requiring review of all fund balances to determine the appropriate classification. This review should be conducted during 2010 because the ending fiscal year 2010 fund balances will need to be reclassified for purposes of completion of the 2011 financial statements. Early review also provides management with the opportunity to have the appropriate resolutions prepared and acted upon by the Town Council to meet certain of the classifications.

The Town’s written responses to the deficiencies 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 and members of the Town Council and is not intended to be and should not be used by anyone other than these specified parties.

DeFazio, J. J. Finkel, Campi & DeGuzo, P. C.