

CITY OF RUTLAND, VERMONT
SINGLE AUDIT
YEAR ENDED JUNE 30, 2008

Corrette & Associates, P. C.

CITY OF RUTLAND, VERMONT
TABLE OF CONTENTS

Report on Internal Control over Financial Reporting and On Compliance with Other Matters Based on an Audit of the Financial Statements Performed in Accordance with Government Auditing Standards	1 - 2
Report on Compliance with Requirements Applicable to Each Major Program and Internal Control Over Compliance in Accordance with OMB Circular A-133	3 - 4
Schedule of expenditures of federal awards	5
Notes to schedule of expenditures of federal awards	6
Schedule of findings	7 - 13
Summary Schedule of prior audit findings	14 - 33

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REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

To the Board of Aldermen
City of Rutland
Rutland, Vermont

We have audited the financial statements of the governmental activities, business-type activities, the aggregate discretely presented component unit, each major fund, and the aggregate remaining fund information of the City of Rutland, Vermont, as of and for the year ended June 30, 2008, which collectively comprise the City of Rutland, Vermont's basic financial statements and have issued our report thereon dated March 11, 2009. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in "Government Auditing Standards," issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the City of Rutland, Vermont'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 of Rutland, Vermont's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the City of Rutland's internal control over financial reporting.

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

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 functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the City of Rutland, Vermont's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the City of Rutland, Vermont's financial statements that is more than inconsequential will not be prevented or detected by the City of Rutland, Vermont's internal control. We consider the

deficiencies indicated in the accompanying schedule of findings and questioned costs to be significant deficiencies in internal control over financial reporting. Finding 08 – 01, 08 – 02, 08 – 03, 08 – 04, 08 – 05, 08 – 06, 08 – 07, 08 – 08, 08 – 09, 08 – 10, and 08-11.

A material weakness is a significant deficiency, or combination of significant deficiencies, that result in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the City of Rutland, Vermont's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies, and accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we believe that seven of the significant deficiencies described in the accompanying schedule are material weaknesses. Finding 08 – 01 through 08 – 07.

Compliance and Other Matters

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

We also noted other matters that we reported to management of the City of Rutland in a separate letter dated March 11, 2009.

The City of Rutland's response to the findings identified in our audit is described in the accompanying schedule of findings and questioned costs. We did not audit the City of Rutland's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of the Board of Alderman, management, federal awarding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Corrette & Associates, P.C.
March 11, 2009
State of Vermont
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REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM AND INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

To the Board of Aldermen
City of Rutland

Compliance

We have audited the compliance of the City of Rutland, Vermont, with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) "Circular A-133 Compliance Supplement" that are applicable to each of its major federal programs for the year ended June 30, 2008. The City of Rutland, Vermont's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of the City of Rutland, Vermont's management. Our responsibility is to express an opinion on the City of Rutland, Vermont's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in the Government Auditing Standards, issued by the Comptroller General of the United States; and OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the City of Rutland, Vermont's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the City of Rutland, Vermont's compliance with those requirements.

In our opinion, the City of Rutland, Vermont complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended December 31, 2008. However, the results of our auditing procedures disclosed instances of noncompliance with those requirements that are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings as items 08 – 03, 08 – 04, 08 – 05, 08 – 06, and 08 – 11.

Internal Control Over Compliance

The management of the City of Rutland, Vermont is responsible for establishing and maintaining effective internal control over compliance with requirement of laws, regulations, contracts, and

grants applicable to federal programs. In planning and performing our audit, we considered the City of Rutland, Vermont's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the City of Rutland, Vermont's internal control over compliance.

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in the entity's internal control that might be significant deficiencies or material weaknesses as defined below. However, as discussed in the accompanying schedule of findings and questioned costs, we identified certain deficiencies in internal control over compliance that we consider to be significant deficiencies and others that we consider to be material weaknesses.

A control deficiency in an entity's internal control over compliance 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 noncompliance with a type of compliance requirement of a federal program on a timely basis. A significant deficiency is a control deficiency, or combination of deficiencies, that adversely affects the entity's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs as items 08 – 01 through 08 – 11 to be significant deficiencies.

A material weakness is a significant deficiency or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the entity's internal control. We consider items 08 – 01 through 08 – 07 to be material weaknesses.

The City of Rutland, Vermont's responses to these findings identified in our audit are described in the accompanying schedule of findings and questioned costs. We did not audit the City of Rutland, Vermont's response and, accordingly, we express no opinion on it.

This report is intended for the information and use of the Board of Aldermen, management, federal awarding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Corrette & Associates, P.C.
March 11, 2009
State of Vermont
License #092-0000130

**CITY OF RUTLAND, VERMONT
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2008**

<u>Federal Agency/Program Title</u>	<u>Federal Contract#</u>	<u>Federal CFDA#</u>	
<u>Expenditures</u>			
U.S. Department of Homeland Security: pass-thru program from Vermont Dept of Public Safety:			
State Homeland Security	02140-11825-350	97.073	\$ 8,319
Fire Airport Training	02140-11875-013	97.067	7,763
Total U.S. Department of Homeland Security			<u>16,082</u>
U.S. Department of Justice - Direct programs			
Byrne Justice Assistance Grant	2006DJBX0086	16.738	5,721
Offender Reentry	2002RECX0022	16.202	20,000
Byrne Formula Grant	03480/03580-0026	16.579	12,500
Bureau of Justice Assistance		16.607	<u>2,882</u>
Total U.S. Department of Justice			<u>41,103</u>
U.S. Department of Transportation pass-through program from the State of VT Agency of Transportation:			
Routes 4 & 7 improvements	08126-CA0117	20.205	39,760
Recreational Trails	NRFT – 06-10	20.219	14,450
National Transportation Safety Administration			
Repeat offenders for DUI	02140-0808-9318	20.608	405
Highway Safety Program	02140-0808-2175	20.600	2,320
Highway Safety Program	02140-0808-2121	20.600	<u>18,056</u>
Total U.S. Department of Transportation			<u>74,991</u>
U. S. General Services Administration			
Elections Improvement Grant	071AFE065	39.011	<u>1,891</u>
U.S. Dept of HUD pass-thru program from from Vt Agency of Commerce and Comm. Develop Block Grants:			
State's Program:			
PACE – Elderly Care	0181/051G(22)	14.228	\$180,000
Western Gateway Project	0181/PG04(16)	14.228	4,733
Community Development Grant	0181/07MP	14.228	5,000
Master Plan Rewrite	0181/08MP	14.228	<u>6,000</u>
Total U.S. Department of Housing and Urban Development			<u>195,733</u>
U.S. Environment Protection Agency			
Water Roof Repair	RF3-146	66.468	<u>3,722,880</u>
Total expenditures of federal awards			<u>\$4,052,680</u>

See accompanying notes to schedule of expenditures of federal awards

CITY OF RUTLAND, VERMONT
NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR YEAR ENDED JUNE 30, 2008

NOTE 1. Basis of Presentation

A. Single Audit reporting entity – For purposes of complying with the Single Audit Act of 1984, as amended, the City includes all funds and programs that are considered part of the primary governmental unit, as described in the financial statements as of and for the year ended June 30, 2008.

B. Basis of presentation – The information in the accompanying schedule is presented in accordance with the Office of Management and Budget (OMB) Circular A-133.

1. Federal Award - Pursuant to the Single Audit Act and OMB Circular A-133, federal award means federal financial assistance and federal cost-reimbursement contracts that non-federal entities receive directly from federal awarding agencies or indirectly from pass-through entities. The City receives direct federal awards and awards passed through the State of Vermont.

2. Federal financial assistance – In the Single Audit Act and OMB Circular A-133, federal financial assistance is defined as assistance provided by a federal agency, either directly or indirectly, in the form of grants, contracts, cooperative agreements, loan guarantees, property, interest subsidies, insurance, or direct appropriations. Federal financial assistance does not include federal cash payments to individuals.

3. Major and nonmajor programs – OMB Circular A-133 establishes criteria for determining major programs and selecting these federal programs to be tested for compliance with program requirements. The major program for 2008 was the U. S. Environmental Protection Agency program Clean Water State Revolving Loan Fund, CFDA 66.468.

C. Basis of accounting – The accompanying schedule of expenditures of federal awards includes the federal grant activity of the City and is presented on the basis of accounting used for reports submitted to grantor agencies. The information in the schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Therefore, some amounts presented in this schedule may differ from amounts presented in the financial statements.

NOTE 2. Subrecipients

The City of Rutland, Vermont provided federal awards to subrecipients as follows:

<u>Program Title</u>	<u>CFDA Number</u>	<u>Amount Provided</u>
Community Development Block Grant	14.228	\$180,000
Serious & Violent Offender Reentry Initiative	16.202	20,000
Byrne Formula Grant	16.579	<u>12,500</u>
		<u>\$212,500</u>

**CITY OF RUTLAND, VERMONT
SCHEDULE OF FINDINGS
FOR THE YEAR ENDED JUNE 30, 2008**

A. Summary of Auditor's Results

OMB Circular A-133 requires the following summary of auditor's results be included in the Schedule of Findings.

1. The auditor's report expresses an adverse opinion on the financial statements of the City of Rutland, Vermont.
2. Eleven significant deficiencies disclosed during the audit of the financial statements are reported in the Report on Internal Control over Financial Reporting and On Compliance with Other Matters Based on an Audit of the Financial Statements Performed in Accordance with Government Auditing Standards. Seven of these are reported as material weaknesses.
3. No instances of noncompliance material to the financial statements of the City of Rutland, Vermont, which would be required to be reported in accordance with *Government Auditing Standards*, were disclosed during the audit.
4. Five significant deficiencies in internal control of major federal programs disclosed during the audit is reported in the Report on Compliance with Requirements Applicable to Each Major Program and Internal Control Over Compliance in Accordance with OMB Circular A-133.
5. The auditor's report on compliance for the major federal programs for the City of Rutland, Vermont expresses an unqualified opinion on all major federal programs.
6. Audit findings that are required to be reported in accordance with OMB Circular A-133 are reported in the accompanying schedule.
7. The programs tested as major programs is the State Drinking Water Revolving Loan fund, CFDA 66.468.
8. The threshold used for distinguishing between Type A and B programs was \$300,000.
9. The City of Rutland, Vermont did not qualify as a low-risk auditee.

**CITY OF RUTLAND, VERMONT
SCHEDULE OF FINDINGS
FOR THE YEAR ENDED JUNE 30, 2008**

B. Findings – Financial Statement Audit

Material Weaknesses

08 – 01: Internal Control Risk Assessment

Condition: The City has not conducted a complete internal risk assessment necessary to identify weaknesses in internal control that should be designed to prevent or detect material misstatement due to error or malfeasance.

Recommendation: The City should conduct a government-wide review of fraud and internal control risk that assesses these risks and develops a plan to mitigate these risks.

Management Response: The City acknowledges that a complete risk assessment is needed on a government-wide basis. The City has worked with Castleton State College to understand what internal control means and develop policies to address this concern. A current project to document procedures in the Treasurer’s Office is a start to review procedures against internal control standards to assure mitigation of risk.

08 – 02: Balance Sheet Reconciliations – The City has not developed procedures to reconcile balance sheet accounts such as cash, interfund receivables and payables, deferred revenue, accounts receivables, and equity balances, nor does the City have supporting documentation for these accounts.

Recommendation: The City Treasurer should develop regular reconciliations of all balance sheet accounts and maintain supporting documentation for each of these reconciliations.

Management Response: The City did not have an accurate balance sheet in FY 2008 or in the prior year. While reconciliation of bank statements was being done during FY 2008, after adjusting starting balances were established from the FY 2007 audit, problems inherent in the MUNIS accounting system thwarted the City’s efforts to reconcile the bank statements to the balance sheet. Conversion of the accounting system to NEMRC has demonstrated in subsequent reconciliation activity to solve this problem and provide supporting documentation. The City has developed forms and procedures to accomplish monthly reconciliation based on the new system. Bank reconciliation after year end has proven exactly against the general ledger balances.

08 – 03: Pooled Cash Accounts – The City has not developed procedures to allocate cash to appropriate funds when cash is pooled for those funds into a single banking account. This creates effective operating transfers from one fund to another when expenditures are made from the pooled cash account without consideration of the availability of cash in that account attributable to each fund.

**CITY OF RUTLAND, VERMONT
SCHEDULE OF FINDINGS
FOR THE YEAR ENDED JUNE 30, 2008**

B. Findings – Financial Statement Audit (continued)

Material Weaknesses: (continued)

Recommendation: The City should develop a tracking system, preferably within its general ledger system, to allocate cash in a pooled cash account between the funds that possess ownership over that cash.

Management Response: The City will strive to develop a tracking system to separate cash from the general fund from proprietary funds. In our conversations with NEMRC, our software supplier, this appears possible due to way NEMRC handles cash receipts and upload of data to the modules representing tax, utility bill and accounts receivable data. We will work with NEMRC to develop a procedure to properly allocate cash with a process at month-end.

08 – 04: Basis of Accounting – The City maintains funds on inconsistent bases of accounting. Some governmental funds recognize full accrual accounting, some recognize the cash basis of accounting, and the remaining funds use a mixed basis of accounting.

Recommendation: Establish a clear basis of accounting for each type of fund within the City’s Chart of Accounts and develop procedures to ensure consistent recording and reporting in consonance with the fund’s basis of accounting.

Management Response: The City had inconsistencies in accounting representation in MUNIS. The intention of the City is to avoid a “mixed” basis of accounting and reflect full accrual for proprietary funds and modified accrual for the general fund in FY 09.

Changes to be implemented within the chart of accounts to be consistent with fund definitions consistent with government accounting standards (GAAFR, or GFOA Blue Book) will help to provide clarity for the City in this regard.

08 – 05: Grant Management – The City has not established adequate procedures for monitoring, recording and reporting grant revenue and expenditures throughout the fiscal year.

Recommendation: Conduct training that instructs all City employees regarding the requirement to monitor and document compliance with grant documents and establish procedures that allow for consolidated grant management throughout the year.

Management Response: The City did not have adequate procedures for monitoring, reporting or recording grant revenue primarily due to a disorganized chart of accounts. A clean up of the chart of accounts occurred in the conversion to a new accounting system and further refinement during FY 2009 to define funds will provide better clarity for the board and the departments. This will be an area of focus and process improvement for the remainder of 2009.

**CITY OF RUTLAND, VERMONT
SCHEDULE OF FINDINGS
FOR THE YEAR ENDED JUNE 30, 2008**

B. Findings – Financial Statement Audit (continued)

08 – 06: Revenue recording – The City has not developed adequate procedures for accurately recognizing revenue by source. Approximately \$1,332,814 of grant and reimbursement activity was posted to miscellaneous revenue.

Recommendation: Develop procedures that require management to identify revenue by source prior to recording that revenue in the general ledger system of accounts.

Management Response: Miscellaneous revenue accounts are a legacy problem in MUNIS as the City did not correctly identify separate grant sources. More definition will be provided to grant revenues and other non-tax or fee revenues in the modified chart of accounts in NEMRC. Funds will be established according to accounting standards with approval by the Board of Finance.

08 – 07: General Ledger System and Fund Accounting – The City has failed to accurately identify all fund types and individual funds in compliance with government accounting standards and funds as established by legal requirements.

Recommendation: Conduct a thorough review of all legal and operational requirements for establishing funds throughout the government. Modify the general ledger chart of accounts to reflect those identified funds and establish procedures that allow for recording activity in the appropriate fund.

Management Response: Miscellaneous revenue accounts are a legacy problem in MUNIS as the City did not correctly identify separate grant sources. More definition will be provided to grant revenues and other non-tax or fee revenues in the modified chart of accounts in NEMRC. Funds will be established according to government accounting standards with approval by the Board of Finance.

Significant Deficiencies

08 – 08: Reimbursement recognition – The City independently recognizes expenditures on behalf of employees as expenses, and the reimbursement of those disbursements from employees as revenues, with the result that both are overstated in governmental funds.

Recommendation: Monitor those expenditures made by the City on behalf of employees and ensure that employees provide these reimbursements timely to the City and that these expenditures and reimbursements are netted against one another to avoid overstatement of either revenues or expenditures.

Management Response: The City recognized certain reimbursements as revenue based on advice previously provided. The City has instituted this change in FY 2009 and made adjustments to reflect a policy to consider these reimbursements as a reduction of expense to avoid overstating revenue and expenses.

**CITY OF RUTLAND, VERMONT
SCHEDULE OF FINDINGS
FOR THE YEAR ENDED JUNE 30, 2008**

B. Findings – Financial Statement Audit (continued)

08 – 09: Segregation of duties – The City has established an internal control of segregation of duties over expenditures by requiring three independent passwords on its check creation software; however, single individuals possess and enter these passwords undermining the intent of the internal control.

Recommendation: Require that system passwords not be shared with others and that individuals enter their own passwords into a check control system.

Management Response: The password system for check generation has been re-configured to require the City Clerk utilize a separate password. The Treasurer will continue to apply the two signatures of the majority of the Board of Finance based upon the signatures on the warrant.

08 – 10: Timely Recording of Financial Activity – The City has not developed procedures to ensure that all financial activity for all funds is recognized and recorded in a timely manner.

Recommendation: Develop the requirement that all financial activity is posted timely to the general ledger accounting system by fund.

Management Response: The City's conversion to NEMRC has vastly improved management's ability to record financial activity in a timely manner as activity on the several sub ledgers are batched and posted daily to the general ledger. The Treasurer's Office has developed a series of standardized adjustment forms which facilitate the timely and accurate recording of activity and adjustments. The Treasurer's Office will continue to develop standard procedures to identify and record all financial activity as well as monthly reconciliation procedures to ensure full and accurate accounting for all activity.

08 – 11: Monitoring by Management – The Board of Aldermen is responsible for oversight of the financial assets, liabilities and activities of the City. The Board is presented only with cash and debt balances and with current budget to actual revenues and expenditures.

Recommendation: Management of the City should be presented with a complete set of financial statements at each review of the City's finances. This should include a complete balance sheet as well as budget-to-actual results from operations.

Management Response: The City agrees that the management should have a full set of financials—including budget to actual results and a balance sheet. By the last quarter of FY 2009, after audit adjustments have been entered for FY 2008 and the balance sheet established in the new accounting system, this will be provided to the Board and management of the City on a quarterly basis. This has been a goal of the Treasurer's office since 2007 but system configuration in MUNIS and data issues relating the previous accounting system negated that goal.

**CITY OF RUTLAND, VERMONT
SCHEDULE OF FINDINGS
FOR THE YEAR ENDED JUNE 30, 2008**

C. Findings and questioned costs - major federal award programs

08 – 03: Pooled Cash Accounts – The City has not developed procedures to allocate cash to appropriate funds when cash is pooled for those funds into a single banking account. This creates effective operating transfers from one fund to another when expenditures are made from the pooled cash account without consideration of the availability of cash in that account attributable to each fund.

Recommendation: The City should develop a tracking system, preferably within its general ledger system, to allocate cash in a pooled cash account between the funds that possess ownership over that cash.

Management Response: The City will strive to develop a tracking system to separate cash from the general fund from proprietary funds. In our conversations with NEMRC, our software supplier, this appears possible due to way NEMRC handles cash receipts and upload of data to the modules representing tax, utility bill and accounts receivable data. We will work with NEMRC to develop a procedure to properly allocate cash with a process at month-end.

08 – 04: Basis of Accounting – The City maintains funds on inconsistent bases of accounting. Some governmental funds recognize full accrual accounting, some recognize the cash basis of accounting, and the remaining funds use a mixed basis of accounting.

Recommendation: Establish a clear basis of accounting for each type of fund within the City's Chart of Accounts and develop procedures to ensure consistent recording and reporting in consonance with the fund's basis of accounting.

Management Response: The City had inconsistencies in accounting representation in MUNIS. The intention of the City is to avoid a "mixed" basis of accounting and reflect full accrual for proprietary funds and modified accrual for the general fund in FY 09.

08 – 05: Grant Management – The City has not established adequate procedures for monitoring, recording and reporting grant revenue and expenditures throughout the fiscal year.

Recommendation: Conduct training that instructs all City employees regarding the requirement to monitor and document compliance with grant documents and establish procedures that allow for consolidated grant management throughout the year.

Management Response: The City did not have adequate procedures for monitoring, reporting or recording grant revenue primarily due to a disorganized chart of accounts. A clean up of the chart of accounts occurred in the conversion to a new accounting system and further refinement during FY 2009 to define funds will provide better clarity for the board and the departments. This will be an area of focus and process improvement for the remainder of 2009.

**CITY OF RUTLAND, VERMONT
SCHEDULE OF FINDINGS
FOR THE YEAR ENDED JUNE 30, 2008**

C. Findings and questioned costs - major federal award programs (continued)

08 – 06: Revenue recording – The City has not developed adequate procedures for accurately recognizing revenue by source. Approximately \$1,332,814 of grant and reimbursement activity was posted to miscellaneous revenue.

Recommendation: Develop procedures that require management to identify revenue by source prior to recording that revenue in the general ledger system of accounts.

Management Response: Miscellaneous revenue accounts are a legacy problem in MUNIS as the City did not correctly identify separate grant sources. More definition will be provided to grant revenues and other non-tax or fee revenues in the modified chart of accounts in NEMRC. Funds will be established according to accounting standards with approval by the Board of Finance.

08 – 11: Monitoring by Management – The Board of Aldermen is responsible for oversight of the financial assets, liabilities and activities of the City. The Board is presented only with cash and debt balances and with current budget to actual revenues and expenditures.

Recommendation: Management of the City should be presented with a complete set of financial statements at each review of the City's finances. This should include a complete balance sheet as well as budget-to-actual results from operations.

Management Response: The City agrees that the management should have a full set of financials—including budget to actual results and a balance sheet. By the last quarter of FY 2009, after audit adjustments have been entered for FY 2008 and the balance sheet established in the new accounting system, this will be provided to the Board and management of the City on a quarterly basis. This has been a goal of the Treasurer's office since 2007 but system configuration in MUNIS and data issues relating the previous accounting system negated that goal.

CITY OF RUTLAND, VERMONT
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
YEAR ENDED JUNE 30, 2008

A. Audit Findings - Financial Statements:

Certain control deficiencies identified in prior audits have not been fully corrected at June 30, 2007. Audit findings 07-1 through 07-23 were previously reported in the 2006 and the 2005 schedule of findings as findings 06-1 through 06-23 and 05-1 through 05-23, respectively. Findings 07-4 and 07-20 indicate those matters are now considered to be resolved. The other conditions described in prior audits also apply to fiscal 2007 and are repeated here with a description of the current status of those matters. Many of the management responses indicate that the City has taken steps directed at resolution of the findings in 2007 with continued actions planned for fiscal 2008.

07-1 Control Environment - material weakness:

Condition - The City has a significant number of deficiencies in design or operation of the system of internal control over financial reporting. Certain control deficiencies identified in prior audits have not been fully corrected at June 30, 2007.

We have identified these control deficiencies as material weaknesses in the City's internal control system. 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. The number and extent of the control deficiencies led us to conclude that a material weakness exists in the City's control environment.

The control environment sets the tone of an organization and is the foundation for all other components of internal control, providing discipline and structure. Internal control is the process effected by the Board of Finance, City management, and other personnel with oversight and review by the Board of Aldermen, to provide assurance about the reliability of financial reporting, the effectiveness and efficiency of City operations, and the compliance with applicable laws and regulations.

Recommendations - The City's Board of Finance and City management need to identify and analyze risks to achieving its financial management objectives, assess its internal controls over financial reporting and compliance, and then develop and implement written policies and procedures for critical accounting and reporting tasks. These policies and procedures should include assignment of all control duties, management responsibilities for task supervision, review by management and the Board of Finance, and further oversight by the Board of Aldermen.

Management's response/corrective action plan - The Board of Aldermen's Finance Committee is in the process of identifying financial risks, assessing internal controls, and developing written policies with the input of management and the Board of Finance. The Board of Finance will develop a timeline for management to create procedures to comply with those controls based on assessment of risk.

**CITY OF RUTLAND, VERMONT
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
YEAR ENDED JUNE 30, 2008**

A. Audit Findings - Financial Statements (continued)

07-1 Control Environment - material weakness (continued)

Castleton State College Students are due to report on Internal Control project to the Board of Aldermen by May 2008, which may help the Board of Aldermen and the Board of Finance to establish over-arching policies and a timeframe for completion. The Board of Aldermen has established objectives, but has not considered specific policy goals beyond the 2006 findings.

07-2 Financial Monitoring - Management and the Boards:

Condition - The City's accounting system does not presently provide regular and accurate interim reports for all funds, departments and programs. Reports of revenues and expenditures to budget provided to management and the Boards for the fiscal year 2007 were not accurate because significant financial transactions were not accurately recorded, general ledger and bank account reconciliations that would have identified errors were not completed, and errors that were identified by management were not corrected.

The City Charter assigns responsibility for the City's system of accounting and auditing to the Board of Finance, and provides for regular monthly reports to be made by each department to the Board of Finance and to the Board of Aldermen. Regular interim reporting of the financial results of City operations is a critical element of internal control which the City needs to effectively monitor financial activities. Without regular and accurate financial reports and supporting detail, neither management, nor the Board of Finance nor the Board of Aldermen can effectively monitor City expenditures, revenues, and cash flows.

Recommendations - We recommend the City accelerate efforts to provide regular, accurate and complete interim reporting for financial monitoring by management, the Board of Finance, and the Board of Aldermen.

Management's response/corrective action plan - Management is providing regular reports of revenues and expenditures to budget to the Board of Finance and the Board of Aldermen and posted to the City's website. However, management states it is unable to ascertain the completeness and accuracy of the information because general ledger and bank account reconciliations are not complete. Management has established an estimated timeline of February 2008 to accomplish general ledger and bank account reconciliations to support financial reporting. Reconciliation of cash accounts through the end of February will be complete by the March 17th Treasurer's report for period ending February 29, 2008. Reconciliations will be maintained from that point forward by an internal auditor who works part time. A/R and A/P reconciliations will be done quarterly.

07-3 Warrant approval process not implemented:

Condition - For fiscal years 2005, 2006 and much of the fiscal year ending June 30, 2007, the City had not implemented a warrant approval process for disbursements as required by the City Charter. Chapter 10, Section 10-1 of the Charter states that "all bills legally contracted by any

**CITY OF RUTLAND, VERMONT
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
YEAR ENDED JUNE 30, 2008**

A. Audit Findings - Financial Statements (continued)

07-3 Warrant approval process not implemented (continued)

officer or board of said city and approved by a majority of the Board of Finance, shall be paid by warrant” directed to the Treasurer. The warrant shall show the indebtedness and shall refer to the appropriation under which the indebtedness was incurred. “No money shall be paid out of the city treasury except upon warrant signed by the mayor for bills approved by the board of finance, ...” The Charter provision is intended to separate the authority to expend funds from the actual disbursement of funds. This separation is an important component of internal control and is designed to safeguard assets and limit disbursements to budgeted or authorized expenditures.

All checks are signed with an automated signature card, which affixes signatures of the Mayor, Treasurer and City Clerk. The automated signature is a routine part of the processing cycle. The Charter requires warrant approval prior to check signature, whether the check signature is automated or not. We did not find any other documentation of approval by the Board of Finance of invoices to be paid.

Recommendations - The City needs to implement a warrant process for accounts payable which documents approval by the Board of Finance of the invoices to be paid. The warrant should be signed by the Mayor, or in the Mayor’s absence, by a majority of the Board of Finance, in order to comply with the City Charter.

The approval process for payroll also needs to be amended to comply with the City Charter. The Board of Finance is empowered to authorize department heads to approve the payroll, which is the current process. However, we noted in our control testing that paychecks were issued without the required signature from the department head. The effectiveness of this control should be improved by requiring the signed payroll report (warrant) to be returned by department heads to the Board of Finance when paychecks are picked up for distribution.

Management’s response/corrective action plan - During the fiscal year ending June 30, 2007, the City implemented a warrant approval process which provides review and signature of warrants before checks are written by two of the three Board of Finance members. In addition, the Treasurer now maintains control of the check signature card, and reviews the warrant and the check ledger sequence before providing the signature card for the check run.

Treasurer is providing dual control for Accounts Payable by approving, releasing and posting the batch after data entry and prior to check printing. After the batch is posted for the warrant date, it cannot be changed. Payroll direct deposit batch through web-based banking services also requires dual control (the majority of City employees use direct deposit).

The Finance Committee is considering a recommendation to require department heads to sign the payroll report upon receipt of paychecks or pay advices for distribution. The Committee is also considering how further separation of duties in accounts payable and payroll processing can improve controls.

CITY OF RUTLAND, VERMONT
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
YEAR ENDED JUNE 30, 2008

07-4 Unauthorized interfund loans:

Condition - During the 2005 fiscal year, the City loaned funds from several of the special revenue and agency funds that are either internally or externally restricted as to use, to the General Fund. The loans were not recorded in the general ledger. The loans were not authorized by the Board of Aldermen or the Board of Finance and the terms of the loans were not formally documented by a note instrument.

Recommendations - Loans between funds should be authorized in advance, with interest rates and repayment terms documented as though the transactions were conducted with an outside party. Funds with external restrictions on use should not be used for interfund loans, even if loans are intended to be temporary in nature. We recommend the City adopt a policy and procedures for interfund loans and other pooled cash arrangements.

Management's response/corrective action plan - During fiscal year 2007 the Board of Alderman voted to require the Treasurer to provide written notification to the Board of interfund transfers, loans and loan repayments. In addition, the Board requires the Treasurer to receive prior approval before transfers can occur from the four funds that are controlled by the Board of Aldermen, the Home Depot, Zamias, Stoolfire and LEPC funds. Management will create procedures for regular reconciliation of the general ledger due to/due from accounts.

Resolution - These interfund loans were repaid in 2006. In 2007, we consider this matter to be resolved.

07-5 Accounting Principles - New Reporting Model:

Condition - The Governmental Accounting Standards Board (GASB) establishes accounting principles for state and local governments. GASB Statement #34 requires implementation of a new financial reporting model which will change the appearance and content of the City's financial statements. In addition to the current fund accounting, the new model will include a Government-wide Statement of Net Assets and Statement of Activities. These government-wide statements will consolidate the individual governmental and proprietary funds into governmental and business-type activities and will report the consolidated financial position and operations on a full accrual basis of accounting.

The City has not completed implementation of the new financial reporting model by June 30, 2003 as required by GASB. Governmental capital assets and depreciation are required to be reported in the government-wide statements. The capital asset accounting must include infrastructure assets. The new reporting model also mandates the annual presentation of a narrative Management's Discussion and Analysis as required supplementary information accompanying the annual financial statements.

CITY OF RUTLAND, VERMONT
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
YEAR ENDED JUNE 30, 2008

07-5 Accounting Principles - New Reporting Model (continued)

Recommendations - We recommend the City establish control accounts for capital asset and depreciation balances in the general ledger and develop procedures to control and reconcile the current subsidiary ledger accounts. We also recommend the City establish an implementation plan for preparation of government-wide statements and for presentation of major funds.

Management's response/corrective action plan - Management will develop a plan to establish capital asset and depreciation balances in the general ledger for 2008, and develop procedures to control and reconcile the current subsidiary ledger accounts. Management will also establish an implementation plan for preparation of government-wide statements and for presentation of major funds and other GASB 34 requirements, with implementation most likely for 2010. Conversion to NEMRC, including a clean up of the chart of accounts, is a first step toward future efforts to convert to GASB #34 compliant statements.

07-6 General ledger accounting - operation and controls:

Condition - We had to propose a significant number of adjusting journal entries to the general ledger at the end of the 2007, 2006 and 2005 fiscal years to complete the accounting cycle. These adjustments reflect unrecorded transactions that occurred during the year or the correction of recording errors that were not corrected by management during the year. These transactions should have been recorded and the errors detected and corrected by the City in the month in which they occurred.

Recommendations - The City should expand the current operating procedures and supervisory controls to insure that all transactions are recorded in the general ledger contemporaneously and that activity is recorded accurately. These procedures and controls should include the monthly reconciliation of significant general ledger accounts. These include not only the cash accounts, but also other significant asset, liability, or operating accounts. Required monthly adjustments and corrections need to be made promptly. Management should review general ledger account balance reconciliations and adjusting entries to insure all transactions are recorded currently and recorded accurately. Documentation should be retained for all adjustments to recorded balances and for their review by management.

Management's response/corrective action plan - Additional staff is now moving forward with fiscal year 2008 cash reconciliations now that beginning balances have been established. Adjustments are being made using an established procedure, as errors are discovered, with documentation retained by the Assistant Treasurer. Some routine monthly and quarterly closing/reconciliation procedures are established. The Treasurer will approve monthly cash reconciliations, and quarterly A/R and A/P reconciliations based on established formats, providing a basis for reliable financial reporting.

CITY OF RUTLAND, VERMONT
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
YEAR ENDED JUNE 30, 2008

07-8 General Ledger not maintained for all funds:

Condition - Special revenue and expendable trust fund activity was not recorded contemporaneously on MUNIS. For 2007, while we found payments from these funds were processed through the MUNIS AP system, significant revenue activity was only recorded when cash account reconciliations were completed after fiscal year end. In addition, MUNIS did not record the due to/due from entries related to the payments correctly, and adjusting entries to correct these accounts were only completed after fiscal year end. The year-end recording of activity was consistent with prior years. However, unrecorded transactions are a material weakness in the City's controls over its financial assets and heighten the risk of errors or fraud.

Recommendations - We recommend that the City record all its financial activity contemporaneously into its MUNIS general ledger system. Contemporaneous recording of the activity will improve the City's ability to exercise appropriate controls over its funds, reduce the risk of fraud, and reduce the time burden on staff related to manual bookkeeping. It will also assure that the City is compliant with federal administrative requirements that require reimbursement requests to be supported by the grantee's general ledger.

Management's response/corrective action plan - Management has examined several options on dealing with grant budgeting and recordkeeping to help ensure the process is understandable and the projects can easily carry over year to year. Procedures are being developed based on these discussions. Trust, grant and other project accounts activity is now recorded in MUNIS. City Clerk, Recreation Department and some other minor accounts are depositing through the Treasurer's office so that activity is recorded contemporaneously.

07-9 General Fund - unrecorded activity and recording errors:

Condition - The City of Rutland did not record all of the City's General Fund activity in its general ledger. During fiscal 2007, material transactions through the City's main cash account were not recorded until requested by the auditor. Material differences were identified in bank reconciliations but were not analyzed to determine the nature of the difference and to identify corrections that were needed. Cash receipts to and disbursements from the City's ACH cash account were not recorded for six months of the fiscal year. Unrecorded activity and recording errors resulted in \$707,161 in net unclassified revenue reported in the 2007 financial statements.

Implementing transactions without recording them is a material weakness in the City's controls over its financial assets and heightens the risk of reporting errors or fraud.

Recommendations - We recommend the City record all its financial activity contemporaneously into the MUNIS general ledger system. Prompt recording of the activity will improve the City's ability to exercise appropriate controls, improve its ability to forecast cash flow, and reduce the risk of errors or fraud.

**CITY OF RUTLAND, VERMONT
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
YEAR ENDED JUNE 30, 2008**

07-9 General Fund - unrecorded activity and recording errors (continued)

Management's response/corrective action plan - Transactional work (over the counter revenue) is now recorded and posted daily. New revenue charge codes have helped identify miscellaneous revenue. Batch processing in MUNIS has not been entirely reliable. Transfers to the school are recorded and property tax payments to the school are budgeted in a contra revenue account. Additional staff is moving forward with fiscal year 2008 cash reconciliations now that beginning balances have been established. Some routine monthly and quarterly closing/reconciliation procedures are established.

07-10 Interfund transactions and balances:

Condition - The City did not properly record certain interfund receivables and payables. Transactions were posted to the accounts in one fund without the corresponding entries in the other affected fund. For 2007 we noted that pre-audit balances between funds did not agree by significant amounts, as also noted in both 2006 and 2005. City accounting personnel were aware that recording errors existed between funds but had not resolved the problem or corrected the out of balance condition. Audit adjustments were proposed to correct this condition.

Recommendations - Treasurer's staff should be properly trained (and MUNIS should be set up) to record interfund transactions in both funds. Monthly reconciliations should be performed on due to/due from balances in all funds to ensure that interfund balances net to zero on an entity-wide basis.

Management's response/corrective action plan - Efforts are in progress to review, reconcile and correct errors in the due to/due from accounts, although monthly reconciliations are not completed. We have implemented use of an AJE request form with supporting documentation attached to identify due to/due from adjustments that need to be made manually in an effort to speed the monthly reconciliations.

07-11 Cash and investment controls - accounts not in general ledger:

Condition - In the 2007 audit we noted that three City bank accounts are not recorded in the general ledger, one account for the City Clerk, and two accounts for the Recreation Department.

In the 2006 and 2005 audits, we noted five bank accounts that were not recorded in the general ledger, including accounts used to record wire transfers and the payment of tax withholdings. Also the investments and related investment income in two trust funds were not recorded on the MUNIS general ledger. For two additional accounts maintained by the Recreation Department the Treasurer's office did not have records regarding the existence or authorized signers for these accounts. Audit adjusting entries were proposed to include the significant accounts in the general ledger.

**CITY OF RUTLAND, VERMONT
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
YEAR ENDED JUNE 30, 2008**

07-11 Cash and investment controls - accounts not in general ledger (continued)

Recommendations - The City should record all cash and investment accounts and activity in the general ledger. The City needs to establish procedures and controls to insure that all accounts are authorized and all transactions recorded and subject to the City's internal controls. The Treasurer's office should receive all statements directly from the bank or broker in order to record activity and reconcile the statements to the general ledger.

Management's response/corrective action plan - The ACH account, tax withholding accounts, and the investments accounts are recorded in the general ledger in 2007. During 2008, the Treasurer's office obtained control and records activity for the City Clerk's account and the Recreation Department accounts except for one account for the Godnick Center.

The City maintains a combined payroll function for the City and the City School District. Management intends to propose a separation of the payroll function between these two components, utilizing separate payroll accounts and separate employer identification numbers for federal and state reporting.

07-12 Cash controls - bank reconciliations:

Condition - The City did not reconcile all cash balances in the MUNIS general ledger to the bank statements. The General Fund cash reconciliations were attempted but were not complete when we arrived for the audit. The beginning cash balance at March 31 was reconciled by recording the unreconciled variance to a suspense account. Material unrecorded transactions were identified on the bank statements during the bank reconciliations, but no entries were recorded in the general ledger until requested by the auditor. The City was also unable to reconcile the payroll cash account within a reasonable variance, although the City identified outstanding checks for the payroll account and some of the other differences.

Recommendations - The City needs to improve control over its cash assets. Bank statements should be reconciled to the check book balance and the general ledger balance promptly at the end of each month. Monthly cash reconciliations are a basic control procedure designed to protect these liquid assets from loss through fraudulent transactions and to improve the City's ability to forecast cash flows.

Management's response/corrective action plan - Management has established a timeframe of February 2008 to have all of its cash account reconciliations up to date. The Treasurer's office is making this a top priority.

CITY OF RUTLAND, VERMONT
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
YEAR ENDED JUNE 30, 2008

07-13 Revenue accounting and controls - property taxes:

Condition - The City does not use the accounts receivable asset account in the MUNIS general ledger to control activity of the detail accounts receivable ledger. The revenue was not reconciled to the billings and receivables during the 2007, 2006 or 2005 fiscal years. Adjustments, abatements and any other changes were recorded in the tax revenue and receivable software, but were not recorded in the MUNIS general ledger. Amounts turned over as delinquent were not recorded in MUNIS. Several proposed audit adjustments were necessary to record all the activity in MUNIS and to balance the property taxes receivable at year end with the detail records. See finding 07-25 - Property Tax Revenue and Receivables Accounting Conversion regarding the inadequate management supervision and review, process monitoring, reconciliation controls, and supporting documentation for the two property tax software conversions which were implemented during fiscal 2007.

Recommendations - We recommend the City develop additional control procedures over tax revenues and tax accounts receivable. These procedures should include monthly procedures to reconcile the detail accounts receivable ledger to the general ledger control account. Adjustments to the accounts should be documented to demonstrate the need for the adjustment and should include documented review and approval of the adjustment by supervisory personnel that have not prepared or recorded the adjustment. Adjustments should be performed monthly and the documentation should be maintained in an organized and orderly manner.

Management's response/corrective action plan - NEMRC, the stand alone property tax program, must be reconciled to MUNIS and to the grand list for fiscal 2008. Year to date collections are being monitored by the Treasurer's office resulting in stepped up notification and tax sale activity. Management intends to prepare quarterly reconciliation of tax revenues in 2008.

07-14 Revenue accounting and controls - Sewer and Water Funds:

Condition - There is limited monitoring of sewer and water revenues to insure that the operating revenues cover the expenses of these proprietary funds. The Water Utility Fund had a 2007 net loss of \$400,393 and the Sewage Disposal Fund had a 2007 net loss of \$ 677,297. Losses have occurred for several years without sufficient remedial action.

Sewer and water billing and accounts receivable are maintained in the MUNIS system, but there is no reconciliation of the detail accounts receivable ledger to the general ledger balance. For fiscal 2007, sewer accounts receivable and revenue were reduced by audit adjustment to reflect the subsidiary detail balance. For fiscal 2006, both water and sewer were reduced by audit adjustment to reflect subsidiary detail balances.

CITY OF RUTLAND, VERMONT
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
YEAR ENDED JUNE 30, 2008

07-14 Revenue accounting and controls - Sewer and Water Funds (continued)

Recommendations - We recommend the City develop appropriate control procedures over Sewer and Water Funds revenues and accounts receivable. Monthly controls should include the monitoring of the collections by DPW, and the monitoring of revenues in relation to expenditures. Control procedures should include a monthly procedure to reconcile the detail accounts receivable ledger to the general ledger control account.

Management's response/corrective action plan - Collections are being monitored as a joint effort of the Treasurer's Office and the Mayor's Office. There are questions about the integrity of the master customer file. Management will develop procedures to implement based on a risk evaluation. Management intends to prepare quarterly reconciliation of water and sewer revenues in 2008.

In addition, management suggests that the Board of Aldermen (acting as the Board of Sewer Commissioners) consider reviewing rate study format, process and methodology, possibly with an outside vendor to ensure accuracy to maintain proper revenues to cover expenditures. The Board may also wish to analyze the rate structure and assess the current process for reading, billing and collection of accounts.

07-15 Revenue accounting and controls - Parking Meter Fund receipts:

Condition - There is limited monitoring of Parking Meter Fund revenue and receivables. Parking tickets are recorded and maintained in the AS400 until collected in the Treasurer's office. They are recorded in the MUNIS accounts after collection. Monthly or bimonthly reports from the AS400 provide summary data on Tickets Paid during the period and Tickets Removed during the period (both number of tickets and amount), but the AS400 does not maintain data on Total Tickets Issued during a period or during the fiscal year because the AS400 wipes out data on a ticket when it is paid. This lack of complete data on tickets issued constitutes poor internal control over parking ticket revenues.

Recommendations - We recommend that parking ticket recordkeeping be moved to MUNIS, so that complete records will be available of tickets issued during a period, tickets removed and tickets collected.

Management's response/corrective action plan - Regular clean up of parking ticket data has been accomplished and new staff trained on the AS400. The City has reviewed two parking ticket systems to date in preparation for conversion to new parking ticket system software in fiscal 2008. New procedures will be established with implementation of the new system.

CITY OF RUTLAND, VERMONT
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
YEAR ENDED JUNE 30, 2008

07-16 Revenue accounting and controls - other receipts:

Condition - Miscellaneous receipts are deposited promptly but are not recorded in the general ledger when received. The daily amounts were accumulated in a spreadsheet which became the basis for a monthly journal entry, but the spreadsheet was discontinued during fiscal 2007, before alternate procedures to record the receipts directly in MUNIS were developed and tested to confirm codes which assigned the revenues to general ledger accounts were working as intended. Management identified a problem with certain revenue charge codes, but was not able to identify and quantify the extent of the problem. This condition likely contributed to the unclassified revenue recorded in the financial statements.

There was limited monitoring of general bills receivable. During 2007 the City identified and corrected errors in recording billing and collections which resulted in a \$34,060 reduction in the balance of the general bills receivable recorded in the 2006 audit. Internal controls over the general billing process are not adequate. General bills are generated at the end of each month by Treasurer's staff, but not reviewed for accuracy. Collections were not followed up if not paid, but collection efforts during 2008 reduced past due receivables substantially. Penalties and interest were not accrued on past due general bills. General bills records for 2007 and prior years contained multiple accounts for a single customer. General bills were filed monthly by date of payment receipt, then alphabetically within the month, which makes monitoring of specific customer accounts difficult.

In prior years, miscellaneous receipts were credited against expense accounts in the general ledger instead of being recorded as revenues. In 2007, there were some instances in which expenses were charged against revenue accounts. The revenue and related expense should be recorded at the gross amounts in the City's financial records and in the financial statements. When used for grant funds, this net accounting method violates federal administrative requirements that require that reimbursement requests be supported by the grantee's general ledger. Audit adjustments were proposed in fiscal 2007, 2006 and 2005 to correct these errors.

Recommendations - We recommend that all miscellaneous receipts and other reimbursement amounts be recorded as revenue when earned or when received. These amounts should be recorded in MUNIS immediately for better control over the asset, and reducing staff time needed to process these receipts. Recording general bills and other reimbursements, as appropriate, as revenue when earned will enable the City to better manage assets and improve cash flow. The departments that provided the service which results in general bills should review those invoices for accuracy before they are mailed. MUNIS reports should be available to these departments so that they can monitor the collections. Written policies and procedures should be developed to establish a timetable and assign responsibility for collections follow up.

CITY OF RUTLAND, VERMONT
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
YEAR ENDED JUNE 30, 2008

07-16 Revenue accounting and controls - other receipts: (continued)

We recommend that all grant revenues be recorded in the general ledger accounts which identify their source as state or federal revenues. The expenditures incurred which earn the state or federal revenues should also be recorded in specifically identified general ledger expense accounts. All grants should be recorded so that the revenue and expense are recorded at the gross amounts in the general ledger.

Management's response/corrective action plan - New revenue charge codes and general ledger object codes for common reimbursement revenues have been created to better identify miscellaneous receipts and better clarify the policy against netting revenues and expenditures. Department heads receive a monthly revenue and expense detail report to monitor collections. A new general bills accounting clerk has cleaned up the general bills process and has begun to review the status of collections monthly. More procedures are needed to define the roles for creating invoices and sending bills to provide for better accuracy. Collections will also involve the City Attorney.

07-17 Health/Dental insurance reimbursements from retirees lack appropriate controls:

Condition - The City does not exercise appropriate controls over the process of obtaining reimbursement for providing health and dental insurance to retirees. There is no tracking of the retirees, the insurances being provided to each retiree, and the costs of those services; no calculation of the reimbursements that should be received according to the appropriate contract and current insurance costs; and no monitoring of collections.

Recommendations - The City needs to assign an individual to identify all retirees and the insurance coverage and period of coverage they are entitled to by contract. The costs of the insurance coverages being provided need to be determined, and the amount of reimbursement the retiree is responsible to provide calculated under the appropriate contract. This information needs to be updated regularly when insurance costs or the retiree's status changes. The revenues should be recorded in MUNIS when earned (i.e., the insurance coverage paid), and accounts receivable recorded and monitored for collections. Notifications or invoices should be sent promptly when a change in costs or status occurs, or when reimbursement is not received promptly. Because employment and health information is governed by strict privacy laws, these tasks should be assigned as responsibilities of Human Resources staff who have access to personnel files.

Management's response/corrective action plan - The Treasurer has created an employee census, with a special retiree subset, to identify errors relating to benefits and reimbursements. The retiree group is now included in the general bills files and the general bills accounting clerk is billing retirees for benefits based on amounts authorized by the Treasurer or Human Resources Administrator. Procedures need to be written to document the process and the roles of Human Resources and the general bills accounting clerk.

CITY OF RUTLAND, VERMONT
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
YEAR ENDED JUNE 30, 2008

07-18 Accounts payable management and controls:

Condition - The City does not use the full capability of the MUNIS A/P module to exercise control over accounts payable. Invoices are entered into A/P only when they are to be paid. The bill drawer, containing unpaid invoices, was the only complete record of unpaid bills that were payable at any given time.

Recommendations - Invoices should be entered into MUNIS as soon as approved for payment by the appropriate department. The invoice due date or prompt payment deadline should be entered so that the A/P system can track invoices due for payment. Use of the MUNIS capabilities will improve monitoring of accounts payable so that prompt payment discounts will not be missed, cash needs can be better projected by the Treasurer, and the City will be able to implement warrant control over disbursements and complete interim financial reports.

Management's response/corrective action plan - A management committee is working on solutions to address this finding. A change was implemented in 2007 to require signatures by two-thirds of the Board of Finance to approve warrants authorizing expenditures. Other changes are also described in 07-3 above. Further changes will be proposed as a set of *Procedures for Purchasing and Payables* to include a more centralized process. Some procedural changes can be made in FY 2008, and system changes will be made in 2009 with conversion to NEMRC for the purchasing and payables functions.

07-19 Pension payments:

Condition - During fiscal year 2007 the City's pension expense was overstated by \$990,396 due to an error in recording the transmittal of the Rutland Public Schools employer contribution to PRIAC at the beginning of the fiscal year. This error was identified during the 2006 audit and supporting documentation provided to management twice during the 2007 fiscal year, but the general ledger was not corrected prior to the 2007 audit. An audit adjustment was proposed to correct the error.

During the fiscal years 2004, 2005, and 2006, we found that payments of employee contributions and City contributions to the pension plan were not made regularly. Because these contributions were not remitted regularly, it was difficult to reconcile the payments to payroll records or to other records. It appears that there may be an error in the City's books related to recording the pension payments transmitted in December 2004, and a variance between the transmittal instructions and how the contributions were recorded by PRIAC.

Recommendations - We recommend that the City work with PRIAC and its actuary to review the covered wages and the employee and employer contributions during the years 2004 and 2005 in order to determine that appropriate contributions were made and correctly recorded. We recommend that the City regularly transmit employee contributions and employer pension

**CITY OF RUTLAND, VERMONT
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
YEAR ENDED JUNE 30, 2008**

07-19 Pension payments: (continued)

payments to the pension plan. The amount of the employee contributions and the employer pension payments should be reconciled to the employee withholdings and to the covered wages, and to the required payments as determined by the City's actuary. After payments are made, the receipt and recording of the payments by PRIAC should be reconciled to the payments and transmittal instructions from the City.

Management's response/corrective action plan - For fiscal 2007, City employee contributions are remitted to PRIAC monthly. The City employer contribution is remitted through two payments per year. Rutland Public School contributions are now remitted directly by the school and the City is provided a remittance advice.

The pension committee will seek outside professional support in reviewing the historical pension contributions and the associated valuation reports. A likely next step is an audit of the pension fund to address possible errors in prior years.

07-20 Document Organization - Financial and Personnel:

Condition - Recordkeeping in the Treasurer's office was not well organized, making it difficult to retrieve specific documents needed for the audit. Documents were not always available or not able to be located. Records for fiscal years previously closed and audited were still taking up limited storage space in the "vault" area, while more current records were stored elsewhere. While this condition existed through fiscal 2008 it was clear while performing 2007 audit procedures during fiscal 2008, that the Treasurer's office had organized its recordkeeping so that current information was accessible in the vault area, and that bank statements, payroll information and personnel files were appropriately organized and filed securely in locked file cabinets or a secure room.

Personnel files are not organized by employee, with all required forms related to that individual's employment. Personnel records are filed with all of the required forms (W-4's, I-9's, medical insurance, dental insurance, etc.) mixed together so that specific documents could not be easily located upon request.

Recommendations - The Treasurer's office should review each of its processes to determine which reports should be retained and determine how best to file those reports. Time should be taken to properly file and store files to ensure that the integrity of all records is maintained. Personnel files should be maintained for each employee and retiree, and confidential information should be in locked files to limit access to authorized parties.

**CITY OF RUTLAND, VERMONT
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
YEAR ENDED JUNE 30, 2008**

07-20 Document Organization - Financial and Personnel (continued)

Management's response/corrective action plan - Done. Human resources records are reorganized, and personnel files are kept locked and payroll information is kept in a secure room with keypad entry. Older personnel and payroll records are stored in a locked storage room. Financial records stored in the vault have been reorganized, with older records cleared from the vault and stored in a locked storage room. The Treasurer's office will be looking at what records need to be generated and maintained by state guidelines, to reduce paper expenses over time. Scanning documents to preserve records and reduce space needs will be considered for the future.

Resolution - This matter is considered to be resolved.

07-21 Duties of the Treasurer's Office:

Condition - The City Treasurer's office has custody of cash, responsibility for recording financial transactions, and reconciles the bank statements. In addition, the Treasurer's office has accumulated many other responsibilities including printing and mailing water and sewer bills and property tax bills via an outside vendor, while it also receives payment for these bills, posts receipts against accounts receivable and posts those receipts to the general ledger.

Assigned duties that combine the custody of cash and responsibility for recording transactions is a lack of separation of duties that increases control risk. During 2006, one individual had custody of cash, responsibility for recording transactions, and reconciled the bank statements for several funds. Another individual maintained the personnel files and handled payroll, and therefore had the opportunity to pay unauthorized employees. The roles and responsibilities of the office had not kept pace with best practices in fiscal control.

The Treasurer's office workload is not well distributed between staff, and the Treasurer's office may not be appropriately staffed. We were told that staff do not have time to thoroughly review their own work and properly file or document things. When someone is out ill, on vacation, or for some other reason unable to perform their own duties, there is little time to help with the counter and still take care of necessary duties.

Recommendations - We recommend the Treasurer evaluate the current workload of the office and determine how each task fits with the mission of the office and how to accomplish appropriate separation of duties. Separate the responsibility for handling cash receipts and cash disbursements from responsibility for reconciling the general ledger to subsidiary accounts and to bank statements. A manager or other appropriate person should make independent comparison of deposits on bank statements to general ledger postings and validated deposit slips. The Treasurer should review reconciliation documentation and any adjusting entries made to the books.

The Treasurer should also establish written job descriptions and titles which list the skills required and assign appropriate personnel to the positions. This will help to clarify the role each person plays in the control process, and identify where training is needed to improve skills. The Treasurer should establish a business calendar to schedule daily, weekly and monthly

CITY OF RUTLAND, VERMONT
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
YEAR ENDED JUNE 30, 2008

07-21 Duties of the Treasurer's Office: (continued)

responsibilities of the office. The business calendar will help the office plan appropriate staffing, and determine how to deal with peak periods and meet financial reporting deadlines.

Management's response/corrective action plan - The duties of the Treasurer and Assistant Treasurer have been well defined to provide for separation of duties between custody of cash and recordkeeping. Some duties have been shifted between transactional staff in the Treasurer's office to adjust the workload. Cross training of current staff and shifting of payroll duties to HR will help to provide greater separation and more effective collections operation. This will also entail updated job descriptions relating to updated procedures. Part-time accounting help used to reconcile accounts has also helped in separation strategies.

Additional Recommendation - Current accounting standards state that management or employees of each organization should have the skill and knowledge of generally accepted accounting principles necessary to record financial transactions and to prepare that organization's financial statements.

The City needs to have an experienced general ledger accountant with skills in current governmental accounting and reporting requirements. This person should direct the accounting and financial reporting function of the City. The City will need to address the authority and responsibility associated with such a position and determine where the position fits with the current management structure. This chief accountant would provide guidance and training to other staff members on accounting matters. This position would assist the Treasurer and Assistant Treasurer with the preparation, or review and approval, of general journal entries and the monthly reconciliation and reporting duties. The position will improve the overall efficiency of the Treasurer's Office by increasing the speed and accuracy of accounting for non-routine transactions. The position can also support internal control objectives by assignment of duties to segregate incompatible functions and through more monitoring of control activities. We recommend the City add an experienced governmental accountant to direct the accounting and financial reporting function of the City.

Additional management Response - Management supports greater separation of duties beyond what has been established in FY 2008, with greater definition of the responsibilities of the Treasurer and recordkeeping/reporting function of the Assistant. The addition of internal auditing for the purposes of reconciliation has provided more accounting skill and assists the Treasurer in the development of journal entries and reconciliation by the Treasurer. The Treasurer and Assistant Treasurer will obtain more training in relating to government accounting and more intensive GFOA training opportunities in 2008 and 2009. The Assistant Treasurer is prepared to pursue more advanced accounting study and credentials. Management acknowledges experience and abilities can be further developed to obtain necessary levels of expertise required. Continuing to improve knowledge, skills and abilities (KSA) of all staff is important for continuity and to build on existing experience and valuable institutional knowledge.

CITY OF RUTLAND, VERMONT
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
YEAR ENDED JUNE 30, 2008

07-22 Annual financial statements and audits:

Condition - The accounting records and financial statements for fiscal 2007 were not adequately prepared for audit. For fiscal 2007 the trial balance was out of balance when presented for audit. The General Fund, the Water Utility Fund, the Parking Meter Fund and several special revenue funds were out of balance. Also, as noted in earlier findings and in prior

years, material transactions were not recorded in the general ledger and reconciliations of general ledger accounts to supporting records were not performed. We proposed a significant number of adjusting journal entries to the general ledger for fiscal 2007, as in the prior two years.

The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America is the responsibility of management. In the City Charter of the City of Rutland, the Board of Finance bears the responsibility for accounting and reporting. Under the Charter, the Board of Aldermen is required to provide for an audit at the close of each fiscal year, and the auditor shall report results to the Board of Aldermen. The City Treasurer is the primary point of contact for the preparation and the maintenance of the records which support the financial statements because the disbursement and collection duties and related recordkeeping are the Treasurer's responsibility.

The City is not complying with Chapter 11, Section 11-5 of the City Charter which provides that the City report shall be published by November 15 each year and that it shall contain a clear statement of the financial affairs of the city, including a record of all expenditures, and receipts of City money and salary of every employee. While the Charter does not require audited financial statements by November 15, we noted that neither the 112th, the 113th, nor the 114th Annual Report contained a record of all expenditures, receipts and disbursements of City money.

Recommendations - We recommend the Board of Finance work with City management to ensure the City meets the required financial reporting deadlines of the City Charter and federal regulations. We recommend the Treasurer and other members of the Board of Finance prepare a detailed schedule with specific deadlines for the tasks that need to be completed each year to close out the fiscal year and prepare the financial statements and supporting records for audit.

Management's response/corrective action plan - The fiscal 2008 target for completion of the financial statement audit will be November 15 in order to comply with the Charter and to meet our lender's requirements. Regular reconciliation will be the most important task to ensure readiness for the audit process. The audit comment can be addressed with additional training and outside professional support, if initial training is completed by July 1, 2008, with a commitment to continue this effort.

Audit Comment - The auditors conclude that achievement of this target will require the addition of the position recommended in the prior finding.

**CITY OF RUTLAND, VERMONT
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
YEAR ENDED JUNE 30, 2008**

07-23 Accounting and Controls for State and Federal programs:

This finding is reported in Section B as it only concerns controls for federal awards.

07-24 Abandoned property:

Condition - The payroll account included \$4,202 of outstanding checks at June 30, 2008, which were also listed as outstanding at June 30, 2006, 2005 and 2004. On July 1, 2006, the Vermont Unclaimed Property Law revision became effective, and provided that the dormancy period for wages and other compensation for personal services decreased to one year, and also provided that the dormancy period for property reported by governmental entities decreased to one year. The law requires organizations to review their records annually and transfer accounts that have reached specified dormancy thresholds to the State Treasurer, who serves as a custodian of the funds until the rightful owners claim them.

Recommendations - We recommend the City implement an annual review in compliance with the statute; perform any required due diligence to locate the owners of these outstanding payroll checks; file an Unclaimed Property Report with the State Treasurer; and transfer the accounts to the State Treasurer.

Management's response/corrective action plan - The City will report to the State as required by law. A policy will be written to report to the State annually.

07-25 Property Tax Revenue and Receivables Accounting conversion:

Condition - The City changed its tax revenue and accounts receivable detail ledger to MUNIS at the beginning of the 2007 fiscal year. A lack of planning for the conversion and management control over the process was evident. There was no plan for the conversion. There was no documented reconciliation to the prior year closing balances. There was no testing to determine that MUNIS would process tax receipts according to the City's process. MUNIS did not apply property tax payments according to the City's process, but posted a quarterly payment to municipal taxes across multiple quarters and calculated a penalty and quarterly interest. Taxpayer accounts were assessed penalties and interest where they should not have applied. It was determined that MUNIS would not be able to process tax receipts correctly for fiscal 2007, nor could it be programmed to handle state mandated property tax changes for fiscal 2008, so the City changed its tax revenue and accounts receivable detail ledger to NEMRC during March of the 2007 fiscal year. Again there was no documented reconciliation of the NEMRC balances to the MUNIS balances or to the prior year closing balances.

In addition, the City was processing abatements, adjustments, and corrections to property valuations well into the fiscal year due to a reappraisal and errors in property classification by the Assessor which required the City to issue adjusted bills and corrected bills.

**CITY OF RUTLAND, VERMONT
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
YEAR ENDED JUNE 30, 2008**

07-25 Property Tax Revenue and Receivables Accounting conversion (continued)

We requested a list of the adjusted bills and corrected bills, and a list of accounts on which penalties and interest had been incorrectly applied. A list was not readily available to determine summary amounts of the impact of the changes and errors on the City's tax revenue and receivables for testing. Copies of each individual tax bill were available, but the Treasurer's office did not summarize the changes and errors to determine the complete impact.

Management supervision and review, process monitoring, reconciliation controls, and supporting documentation for the property tax conversions were all inadequate. This condition likely contributed to the unclassified revenue recorded in the financial statements.

Recommendations - It is important to maintain control over financial assets at all times. During software conversion, monitoring controls are needed to insure all accounts are retained and ending balances equal beginning balances. Reconciliation procedures should be applied and retained to document all accounts are converted accurately. Management supervision and review of the conversion process is necessary to insure the process is completed as planned and financial assets are protected. Effective software conversion requires a detailed plan addressing every step in the process, providing an adequate timeframe, and providing controls over the integrity of the data. The conversion process also requires monitoring of the planned procedures during the actual conversion. We recommend the City develop a policy to govern future software conversion projects.

This recommendation for controls over software conversions will apply to the anticipated change from MUNIS to NEMRC for accounting software, and from the AS400 to the proposed new parking ticket system.

Management's response/corrective action plan - A conversion plan is being developed by management, in cooperation with the current and proposed vendors (MUNIS and NEMRC) for the GL and additional programs. Management anticipates utilizing professional services of an outside accountant to ensure conversion reconciliation is achieved to avoid the issues that occurred with the AS-400 to MUNIS to NEMRC conversions.

B. Audit Findings - Federal Awards:

07-26 Accounting and Controls for State and Federal programs:

Condition - The City participates in several state and federal programs and is required to maintain separate accounting records to support reporting requirements. The City is also obligated to establish controls over compliance with program requirements. The Treasurer's office maintains program accounting records and managers within individual departments administer the program requirements. For fiscal 2007 the Treasurer's office was not able to correctly quantify federal expenditures. Activity for these programs was not timely recorded in the City's accounting system, but was summarized at year end. A number of adjustments were proposed to correct account balances for these state and federal programs.

**CITY OF RUTLAND, VERMONT
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
YEAR ENDED JUNE 30, 2008**

07-26 Accounting and Controls for State and Federal programs (continued)

For fiscal 2006 and 2005 the Treasurer's office was not able to identify all programs which received and expended state and federal funds. The activity for several of these programs was not recorded contemporaneously in the City's MUNIS accounting system, but was summarized at year end, and only then entered into MUNIS. A significant number of year-end adjusting entries were prepared to correct account balances for these state and federal programs.

Recommendations - We recommend the City identify all state and federal programs, establish central files for program descriptions, requirements, and reporting regulations, and identify an employee for each program. Internal controls for compliance with program accounting and administrative requirements should be performed regularly and documentation retained. Proper classification of transactions is particularly important for federal funds, because the City has significant additional requirements for reporting and program compliance and additional audit requirements under the Single Audit Act.

Management's response/corrective action plan - Management has improved the organization of grant files, separating them by state and federal funding. Some paperwork still needs to be tracked down for the files, and a policy will be written instructing department heads to provide the Treasurer's Office with all documentation on a timely basis. The Policy has been established and sent to Department Heads by memorandum. A location for City grant files has been identified and established in the Treasurer's vault. The Board of Aldermen could consider drafting a policy regarding approvals for grant application and recordkeeping to support these initiatives, including assigning grant fiscal operations to the Treasurer's office to support the audit findings.

07-27 U.S. Department of Housing and Urban Development funds passed through to sub-recipient:

Condition - The City did not record the receipt and expenditure of U.S. Department of Housing and Urban Development funds for the Forest Park Redevelopment Initiative as a revenue and an expenditure in its general ledger because the funds were passed through to a subrecipient. The City did include the expenditure on its Schedule of Expenditures of Federal Awards.

Recommendations - We recommend that all grant revenues be recorded in general ledger accounts which identify their source as state or federal revenues. The expenditures incurred which earn the state or federal revenues should also be recorded in specifically identified general ledger expense accounts. Recording federal or state revenues passed on to a subrecipient is important because the City as a pass-through entity is responsible for identifying to the subrecipient the award information and applicable compliance requirements, monitoring the subrecipient's use of the award through reporting, site visits, regular contact or other means, and ensuring that subrecipients expending \$500,000 or more in Federal awards have met the audit requirements of OMB Circular A-133 within 9 months of the end of the subrecipient's audit period; and ensuring that the subrecipient takes timely and appropriate corrective action on all audit findings.

Management's response/corrective action plan - The City will record all grant revenues in the GL and develop a plan to bring RRA financial recordkeeping into the Treasurer's Office as a component unit of the City by start of FY 2009.