ROSELLI, CLARK & ASSOCIATES
Certified Public Accountants

RCA
CPA

**TOWN OF NANTUCKET, MASSACHUSETTS**

Management Letter

Year Ended June 30, 2020

# TOWN OF NANTUCKET, MASSACHUSETTS

MANAGEMENT LETTER
YEAR ENDED JUNE 30, 2020

TABLE OF CONTENTS

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**TRANSMITTAL LETTER**

Select Board
Town of Nantucket
Nantucket, Massachusetts

In planning and performing our audit of the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the Town of Nantucket, Massachusetts, (the "Town") as of and for the year ended June 30, 2020 in accordance with auditing standards generally accepted in the United States of America, we considered the Town's internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Town's internal control. Accordingly, we do not express an opinion on the effectiveness of the Town's internal control.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity'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 entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal controls.

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 by the entity's internal control.

Our consideration of internal control was for the limited purpose described in the first paragraph and may not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified. This communication is intended solely for the information and use of management, the members of the Select Board, and others within the organization, and is not intended to be and should not be used by anyone other than these specified parties.

Roselli Clark & Associates

Roselli, Clark & Associates
Certified Public Accountants
Woburn, Massachusetts
December 31, 2020

## EVALUATION OF TOWN OPERATIONS

Fiscal 2020 will always be remembered for what is arguably, one of, if not, the beginning of one of the Nation's most daunting historical challenges. In January 2020, a virus known as Covid-19, made its appearance in the United States. Within two months, it's devastating effects were being experienced on a large-scale basis and became a pandemic. In order to mitigate the wide-spread impacts, the entire Nation came to a virtual stand-still as schools, colleges, and non-essential businesses and activities were all shut down and citizens were required to shelter in their homes.

Because the resultant unemployment skyrocketed to levels never seen before, it had, and continues to have a dramatic impact on the world economy; This impact has been felt at the Global, National and Local level.

While the Town could never prepare itself to face such an unprecedented challenge, years of strong fiscal management set up the Town to withstand this tragedy, better than most. Despite the economy being locked down for basically the entire fourth quarter, the Town was still able to ride the back of a strong first half of the year and end the year with positive operations and balance a budget for fiscal 2021.

The following are some key financial highlights:

1. Unassigned fund balance increased by $0.7 million.
2. The OPEB fund increased to $3.7 million.
3. Stabilization funds increased to almost $6.8 million.
4. Levy capacity was almost $3.2 million.

This along with continued strong financial management has enabled the Town to maintain its top bond rating of AAA. This is the highest bond rating a community can receive and enables the Town to reduce its financing costs on its future borrowings.

In addition, the strong financial position will leverage the Town's efforts to mitigate the economic impacts of Covid-19 in fiscal 2021 and beyond.

The remainder of this letter addresses items of interest that we are communicating to the Town in the form of "Informational Items"; (these are not considered findings) and a section labeled "Findings and Recommendations", which are our observations in areas that the Town is encouraged to devote attention to. Improvements in these areas are recommended in an effort to improve internal control and efficiency.

## INFORMATIONAL ITEMS

### Other Postemployment Benefits

The Town has been aggressively managing its OPEB Trust for several years now. Annual funding has allowed the plan assets to grow to almost $3.7 million and funding OPEB has become hardcoded in the Town's annual budget.

Despite this, the Town's unfunded liability continues to grow and has reached almost $125 million as of June 30, 2020. This is about a $40 million increase since fiscal 2015.

One of the largest drivers in calculating the unfunded liability is the discount rate. The current year valuation uses a discount rate of 3.75% which is low compared to many other communities. Each percent is worth about $20 million in valuation.

The Town should consider evaluating efforts to increase the discount rate. This could be accomplished through a combination of policy changes:

1. Increase annual funding to OPEB.
2. Adopt a funding schedule that uses the pension funding windfall that becomes available once the pension is fully funded.
3. Consider converting the investment policy to a modern portfolio with a greater equity allocation rather than fixed income. Since the investment goal is a long-term objective it should be managed like pension assets, whereas it is currently managed more like an intermediate vehicle.

The combination of these efforts could lower the liability considerably.

### Network Security

In the prior year, we alerted the Town to continue to monitor its network security (the Town had a network security assessment completed recently). We remind the Town that given the remote processing of its financial transactions during this social distancing period that network security becomes more vulnerable and should continue to be evaluated on an ongoing basis.

### New GASB pronouncements

The GASB approved two new pronouncements these were extended and go into effect in fiscal year 2021and 2022.

**GASB 84** which requires the Town to record certain custodial fiduciary activities such as student activities as special revenue funds goes into effect during fiscal year 2021.

**GASB 87** which requires the Town to revise the manner in which it accounts for its operating leases goes into effect in fiscal year 2022. Previously, governmental entities reported their leases similarly to how private entities reported leases under ASC 840.

While finance leases would be capitalized on the balance sheet, operating leases would be reported in the footnotes. However, GASB 87 requires that all operating leases now be accounted for as finance leases.

As a result, leases previously classified as operating leases will not only be capitalized on the statement of net position, but also be reported differently in the statement of activities.

**Nantucket Regional Transit Authority (update)**

Currently, the Town serves as a service provider for the Nantucket Regional Transit Authority, or NRTA. The services extend to payroll, and payroll related benefits. In a prior year letter to management, we outlined the risks associated with such an arrangement and recommended the Town pare back in those areas it can.

The Town began evaluating this suggestion and has taken some remedial actions; however this is still a work in progress as it involves complicated areas of human resources and will take more time to discuss with legal counsel prior to reaching a more knowledgeable conclusion.

## FINDINGS AND RECOMMENDATIONS

### Tax Recap Process

The completion of the Tax Recap is a very important step in the annual municipal financial cycle as it is the financial document completed and then approved by DOR that allows the Town to set its annual tax rate.

Our review of this process determined that not all expenditures were included in the fiscal 2020 tax recap when submitted to the DOR. Thus, the document was not accurately completed.

The Town was fortunate that its local receipts were well above forecast, and this covered any potential short fall that may have existed. In addition, the Town contacted the DOR immediately upon our communication of this situation and learned that no remedial action needs to be undertaken.

Th Finance Department has established procedures that it will put in place for fiscal 2021 to avoid a repeat occurrence of this issue.

### Closing Process

The current fiscal year audit was a very challenging audit due to the social distancing restrictions imposed by the Governor. As a result, the majority of the audit was completed remotely, and this placed many challenges on both the financial staff and our audit team. In addition, there were numerous distractions such as managing the Cares Act, balancing the fiscal 2021 budget and working remotely. Despite this, we are pleased to report that the Finance Department closed the books on time and allowed us to complete the audit on time. This is a significant achievement given that many communities through-out the Commonwealth have fallen well behind in closing the books.

The challenging close caused the financial department to overlook a handful of items that most likely would have been completed properly in a normal situation.

These include:

1. Not making all budget entries to records. This caused deficits at year-end, some of which may need to be raised when setting the tax rate and
2. Not making all Cares Act and FEMA transfers.

It is important that the Town closes its books in time to complete a thorough internal review. Such exceptions that we observed could be avoided with ample review time.

### DESE/Chart of Accounts

The Massachusetts Department of Elementary and Secondary Education (DESE) requires all school districts to maintain an accounting system in accordance with 603 CMR 10.03(3)(a) which states:

> Each school district shall utilize a financial reporting system that permits the reporting of all school district expenditures by fund source, object and function and permits the reporting of certain costs by program and school. The fund

> source, object, function, program, and school classifications for which reporting shall be required shall be those identified and described with specificity in the guidelines published by the Department.

The current MUNIS general ledger chart of accounts utilized by the Town and School does not include the DESE object codes and utilizes the DESE function codes inconsistently. As a result, the School is not in compliance with DESE regulations. In addition, the completion of the annual DESE End of Year Financial report is made more cumbersome as many costs must be allocated using multiple spreadsheets. We recommend that the School update its chart of accounts to comply with DESE guidelines. This will most likely be a project that takes more than one fiscal year due to the need to redesign the chart of accounts and to have MUNIS implement the changes while keeping the historical activity in the general ledger. This would also be an opportune time for the Town to examine whether non-school accounts should also be updated to enhance reporting capabilities.

**Abatement Accounts (repeated)**

The Town currently maintains approximately thirty abatement accounts in its general ledger. These reflect accounts for years going back into the 1980's. Under the municipal modernization act that was authorized into law in 2016, communities are allowed to consolidate these into one account. We suggest the Town make the necessary journal entries to accomplish this. This will clean up the general ledger and eliminate many accounts with deficits that are not true deficits under the new regulations.

**Tipping Fees (repeated)**

Tipping fees for the landfill are billed and collected by the Department of Public Works. The department's skill set is managing and performing public works projects; its efficiency and effectiveness in managing financial-based processes is not as great as within the Collector's Department.

We observed that the department's receivable aging deteriorated significantly. This occurs when amounts billed are not collected efficiently. Such a process, if left uncorrected, could lead to a write-off of a Town asset. Additionally, the build-up of receivables is a consumption of the Town's cash resources.

We recommend the Town's Finance Department to assess this situation and determine the cause for this. Once this is completed, a plan should be developed to bring this under control.

**Water Inventory (repeated)**

In the prior year, we completed observation tests at the Wannacomet Water Department. The purpose of our test was to evaluate the controls associated with its inventory. We made the following recommendations as a result of our procedures:

1. Perform physical inventory counts periodically (semiannual is preferred, annual at a minimum)
2. Compare actual counts to the inventory records.
3. Investigate any variances.

4. Consider surveillance in the building, especially in the inventory areas.
5. Limit access to the "locked" room.
6. Place the meters in the locked room instead of the unlocked front room.
7. Write-off any variances that can't be resolved.
8. Write-off old obsolete inventory.

We understand that the Water Department Office Manager retired, and then the Covid pandemic hit. As a result, implementing these recommendations was understandably not given a high priority during the year. We understand that this is an area that will be addressed and corrected by the close of fiscal year 2021.

**Consolidation of Bank Accounts (repeated)**

The Town currently maintains almost sixty bank accounts. Many were set up years ago and do not seem to serve a purpose. The Town should review each bank account and determine why it is being used and close those that can be consolidated into other accounts.

In addition, in certain situations, the Town maintains dedicated bank accounts for certain of its fund balances such as the Cafeteria (School Lunch), the Ambulance, Health Insurance Trust and others. These accounts are used for deposits of the various activities they are set up for, however it does not appear that these bank balances are "trued" for disbursements of these activities made from the general depository. If the Town chooses to set up dedicated accounts so that each activity earns its own interest, it is important for the Town to adjust these to the fund balance amount on a periodic basis, or alternatively, in those situations where dedicated accounts are not required to be maintained by statute, they should be closed and consolidated into the depository account.

**Payroll Tests (repeated)**

In the prior year, we tested twenty-five employees as part of a payroll test. We discovered that five had not completed and passed the State Ethics examination and eleven were missing I-9 Forms in their files. We recommend that the Town bring into compliance all employees who are currently in violation of these Human Resource covenants. In addition, we recommend that the Town begin a process whereby periodic payroll audits are completed as part of the Town's quality control process of payroll/personnel.

*We did not conduct specific tests in this area in the current year, however we are aware that the Town has yet to set up an internal audit process to satisfy the prior year comment.*

**Old Personal Property Receivable Balances (repeated)**

The Town has done a nice job cleaning up most of its old receivable balances. This was a comment in several previous letters to management. Both boat excise and motor vehicle excise are now carried for approximately six years on the Town's general ledger. However, the Town still maintains personal property taxes dating back to 1989, which serve to clutter the general ledger. Many of these balances are immaterial in relation to the overall Town activity and the only means of collection enforcement is through small claims court or enforced through nonrenewal of business permits.

In order to address this further, the Collector's Office can create a schedule and identify the holder of each account. This could then be cross referenced to the Town Clerk's Office where business permits are maintained. In doing so the Town could learn which businesses are still active and if in default, either revoke the business permit or not renew the business permit on next renewal.

Once these efforts have been exhausted, a request to the Assessors to abate the tax under MGL Chapter 59 Section 71 makes most sense using the following steps:

a) If the collector is satisfied that a tax on tangible personal property is uncollectible because of death, absence, poverty, insolvency or other inability of the person assessed to pay, he/she may notify the assessors under oath that these taxes cannot be paid. The assessors must decide within 30 days after receipt of the notice whether to abate the personal property taxes.

b) If an abatement is granted, the assessors must certify the abatement in writing to the collector. The certification will discharge the collector from any further obligation with respect to this tax.

DEPARTMENT OF MUNICIPAL FINANCE

TOWN OF NANTUCKET

(508)228-7200
Finance Department
37 Washington Street
Nantucket, MA 02554

TO: Audit Committee

CC: C. Elizabeth Gibson, Town Manager

FROM: Brian E. Turbitt, Finance Director

DATE: July 1, 2021

RE: Town of Nantucket FY20 Management Letter

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Enclosed are the responses to the FY20 Town of Nantucket Management Letter. The management letter for FY20 does not include any significant deficiencies. The letter does include informational items and Findings. The management letter has been reviewed and the Finance Department has worked very hard to review how the close cycles and reviews are done, to ensure that they are done in a timely and efficient manner.

**INFORMATIONAL ITEMS**:

1) **Other Post-Employment Benefits**: The Town has recognized the significant impact that OPEB will have in FY20 and beyond. The Select Board did adopt a policy that would direct the savings in the pension assessment to the OPEB trust fund. This is anticipated to begin in FY2038, once the unfunded pension obligation schedule is met. That will dedicate the pension funding to OPEB when the pension system is fully funded.

   The Town is working with its investment advisors on a long-term strategy for the investment of the OPEB funds. The Town's goal is to be able to, over time, increase the discount rate that it can use in its valuation.

2) **Network Security:** The Town takes the security of its network infrastructure very seriously, especially while so many employees were working from remote locations during the pandemic. The Town working through its IT Department has implemented various network security trainings, offered by the Commonwealth of Massachusetts. The Town continues to develop additional strategies to protect the integrity of the network.

3) **New GASB pronouncements:** The Town is aware of both the new GASB pronouncements and will be prepared to implement them during the required implementation years.

4) **Nantucket Regional Transit Authority:** The Town has reviewed this, and will work with the NRTA to either implement an agreement that outlines the administrative support functions that it provides for them, or define a transition period prior to ceasing to provide the administrative support to the NRTA

**FINDINGS AND RECOMMENDATIONS**:

1) **Tax Rate Recap Process:** The Town during the tax rate setting process for FY2020 neglected to include the capital exclusion in the levy limit calculation. The expenditures were included as authorized. Upon the notification by the auditors of this issue, the Finance Director immediately reached out to the DOR to discuss the issue. The Town was very fortunate to have had receipts more than the budget, which were able to cover this error. After discussion with DOR, it was determined that no other action was necessary by the Town.

   There were discussions with all individuals who participate in the tax rate recap process, and a new review process was implemented, that included a review of the document, and the Annual Town Meeting actions to ensure that everything that was approved included in the recap by the Town's audit firm. This process was utilized for the FY21 Tax Rate Setting process.

2) **Closing Process:** The closing process for FY20 was a difficult one with the global pandemic in full effect. The Town did close the books timely, and consistent with the schedule that it has maintained over the last few years. The Town has worked very hard to strengthen its closing process every year. The issues that were highlighted have been discussed and reviews focused in those areas have been done on a more frequent basis. One of the issues that arose during the FY20 audit was specifically focused on the CARES Act. This program was implemented near the end of the Fiscal Year, with guidance on expenditures evolving while trying to administer the program. The review process has been enhanced, and all expenditure accounts are reviewed monthly to ensure that any expenditures that should have been charged to the CARES Act are journaled into the account in a timelier manner.

3) **DESE/Chart of Accounts:** The Finance Director and the School CFO have been in communication regarding this finding. It is the intention of both the Finance Director and the School CFO to bring the chart of accounts for the school into compliance. The conversion of the chart of accounts, will be a multiyear process, and will involve not only the Town and School, but the town's software provider as well. The expectation is that this will take more than 1 year to implement; preliminary work is expected to begin in FY21, with a goal of completing it in FY22.

4) **Abatement Accounts:** The Town has created one (1) abatement account, and all abatement balances have been transferred to this account. Moving forward this account will be the only one used.

5) **Tipping Fees:** The Finance Director and the DPW Director have been discussing this issue. One option that has been discussed is for this to be brought into the Collector's office. While other options are being explored a new policy to determine who can access charging at the facility, and how to better manage the receivables list is being developed. The focus is on the credit granting process, as well as the possibility of using outside collection agencies to service the delinquent balances. As a start, the Town has been liening delinquent balances to tax bills

when that is a possibility. The Town does recognize that an increasing accounts receivable will certainly put a strain on the financial operations of the Solid Waste Facility.

6) **Water Inventory:** This observation is still being worked on. It is expected that a process will be developed and implemented in both FY21 and FY22.

7) **Consolidation of Bank Accounts:** The Town Treasurer has been reviewing the number of accounts and does consolidate when the opportunity arises. The focuses have been on making sure during the AP warrant process that the funds are transferred from all the necessary bank accounts, as wells as reviewing periodically to ensure that the accounts have been "trued" up.

8) **Payroll Testing:** The HR and Payroll Departments have begun periodic reviews of employee files to ensure that all required forms are in fact in the employee files. It is our understanding that the Auditors will be doing a random sampling of this again in FY21.

9) **Old Personal Property Receivable Balances:** This is a work in process, and it is expected that it will be completed in FY22. The Collectors office will be working with the Assessor's Office to complete this process in FY22. The goal was to have this done sooner, however with the transitions over the last year in the offices and the pandemic, this has not been able to be completed as of yet.