

**NORTH KINGSTOWN AUDIT COMMITTEE**

**December 23, 2008**

**Town Hall Conference Room**

**6:30 pm**

**PRESENT WERE:**        **Ned McCrory, Chairman**  
                              **Richard August**  
                              **John McNamee**  
                              **Jeff Wadovick**

**ALSO PRESENT:**        **Patricia Sunderland**

A tape recording of this meeting was made to supplement the written record.

**I.        Call to Order**

- Chairman McCrory called the meeting to order at 6:30 pm.

**II.       Pursuant to RIGL 42-46-6, Notice of this meeting has been posted on the Secretary of State's Website**

**III.      Review/Discuss draft copy of the 6/30/2008 financial statements with Braver, P.C.**

Jim Wilkinson opened the discussion...

At this point, draft has been reviewed with management of Town and School. The finance statements are presented in the format of a Comprehensive Annual Financial Report and it was recommended to read the narratives, introductory sections and the management & discussion analysis, this is where the story is told through columns, tables and numbers.

Opinion is an unmodified report meaning the financial statements are presented in accordance with generally accepted accounting principles applicable to government. **Highlights:**

Page 12 & 13 are the governmental wide financial statements presented on a full accrual basis consolidated similar to a business enterprise, not kept on the basis of budgetary reporting so they are really not that meaningful for assessing operating results. The presentation provided to the Town Council will articulate the adjustments for year to year, however they are not that meaningful...a little premature at this point.

**Discussion of fund balances:**

- Page 14 – General Undesignated Fund Balance totaled \$8.6M which was slightly below last year. The total fund balance in the general fund is approximately \$10.8M. In addition to the \$8.6M undesignated fund balance, the general fund has reserved \$1.5M for the golf course irrigation project as well as \$685,000 for encumbrances (unfilled purchase commitments at year end).
- Page 14 – School Unrestricted Fund balance was \$495,659 up slightly from prior year. There are a number of reservations/designations from the fund balance: \$10,000 for participation in GHGRI (Town's group health insurance), \$1,128,000 for encumbrances, a reservation for school cafeteria fund.

Much discussion precipitated around the deficit in the school cafeteria fund. Generally, in the governmental wide financial statements, assets are recognized to the extent that they are current assets (cash or convertible to cash within the year). As part of the school's unrestricted fund, the due from other funds, there is a receivable in there that is due from the cafeteria fund (\$300,000 +/-) The \$244,000 + is a portion of the receivable that won't be collected within a year because the fund has no resources and the \$244,000 is a deficit in that fund but rather than reserving the asset piece there is just an earmarking of fund balance designating that is incapable of receiving this balance based on historically what has been happening in this fund over the past few years. Jeff Wadovick reiterated that they reserved it assuming that it was not going to be collected. Jim noted that this practice is similar to other governments presenting this as an advance rather than a "due to/due from", it is not coming in within the year to be appropriated and spent.

This issue is a big issue for Jeff Wadovick noting that the deficit has doubled in FY 2008. Noted the cumulative deficit in the prior year of \$122,000 and the deficit spent for FY 2008 is \$122,000. Questioned whether the auditors have spoken to management to determine a plan of action on addressing this issue. Mr. Wilkinson explained that they have spoke to the school administration and they alluded to the fact that it was hopeful that it would be turning around. Effectively, expenses exceeded revenues by 10% which is not a small issue, it is a major issue which Mr. Wilkinson felt that there is some structural stuff that needs to be looked at in the fund. A discussion has been continuing on to determine whether they should actually make this transfer to the fund to wipe out the deficit or continue to carry the

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receivable with the hopes that the cafeteria fund will be able to pay the school unrestricted fund at some point. Jeff Wadovick is more concerned about moving forward rather than backward and if the fund is going to continue to lose money then they would need to budget to lose money. They are losing their spending authority because of the loss. Jeff understood from the administration when they were in attendance at a meeting regarding the cafeteria that they were anticipating a loss but certainly not this significant, he had noted a loss of approximately \$58,000. John McNamee questioned whether some of this loss was due to cutbacks in state/federal funding. Jim noted that federal/state funding increased by \$35,000 however, revenues were down from \$1,084,000 to \$911,000, the operating loss is \$372,000, up by \$100,000 offset by additional grants of \$35,000. Jim noted that management was aware of a management comment coming on this issue and give them the opportunity to respond and a corrective action plan should be developed. In theory, as Jeff Wadovick pointed out, the school can subsidize the school cafeteria fund, however, does not believe that was their intent.

Chairman McCrory pointed out that the employees in the cafeteria fund were hoping for a break-even year, not a loss of \$60,000 which is where they were at the point when they met with the audit committee earlier in the year, since that time the loss of \$60,000 has doubled to \$122,000 in the FY 2008 audit. The chairman pointed out the acceptable situation that a \$60,000 loss had decreased to approximately \$30,000, however, it is a completely different situation when the \$60,000 loss had doubled, which is not acceptable. Chairman McCrory reflected back to a comment that Mr. Wilkinson had made that the loss is shown as a receivable with the expectation that it would be paid back in the future but questions whether this operation can really accomplish that, he felt that was unrealistic.

Jim pointed out that the cafeteria fund is the biggest area of concern in the entire document because this is outside the budgetary appropriations. This is an enterprise fund being operated as a business. Jeff Wadovick felt the audit committee should put some pressure on the school committee to try and correct this ongoing deficit. Perhaps the school committee should reserve some money in their upcoming budget to make the fund whole and correct it going forward, Jeff's opinion is that they are never going to make up for the deficit and charge the kids extra money for their lunch to make up for the deficits. Keeping in mind that once the money has been appropriated to the school it becomes their money of which the Town has no control over so Jeff is recommending that the school committee reserve the money to cover the deficit and correct the problem and move forward before they come back to the town for the \$300,000 +/- accrued loss. In Jeff's opinion, a \$495,000 undesignated fund balance is not a huge amount of money for a fund with a \$58M budget.

John McNamee inquired as to whether they could review the current year to date trial balance to determine where they were at that point in time. Jeff pointed out that this particular operation tends to be very behind in recording of their revenues. Mr. McNamee felt that management should be looking at the income from the operations before federal/state matches are applied. It has been communicated to the committee that the cafeteria fund does not get the revenues from the vending machines that had previously been stipulated which is an operating that they compete with, however, the revenues generated from the vending machines is not this significant.

Richard August pointed out that during his review/analysis of the vending machines, the two schools with the highest number of vending machines is the high school and Davisville Middle School and although he has not had communication with administration on the vending machines at the high school he did note that the machines at the middle school were unaccessible until after school hours and did not feel they were competing with the cafeteria. Mr. August reiterated that they had made good strides and noted that there was a goal to at least break even which, clearly, had not happened before year end. Mr. August felt this is an area that needs to be addressed and at least outsourcing the operations to a vendor particularly if they guarantee the operation will break even or profit. In Mr. August's opinion, it makes little sense to layoff people and cut programs/personnel to support an operation that has been running a deficit year after year. Mr. August noted that the school business manager does update the council, financially, on how the fund is operating against budget. Chairman McCrory requested the year-to-date analysis of the cafeteria fund for the first six months of the year to be discussed at the next meeting.

Another major fund:

- Page 14 – Debt Service Fund – no change in their fund balance, however, noted two capital projects funds: Farmland/Open Space and Public Safety Facilities. A \$4M bond was issued for Farmland/Open Space Fund and the initial cost for the Public Safety Facilities of \$900K +/- was advanced by the General Fund and the bond will be issued in January to reimburse the General Fund which will resolve that deficit.

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Chairman McCrory inquired on when the Town is required to reflect our Other Post Employment Benefit liability and asked that Mr. Wilkinson elaborate. Mr. Wilkinson pointed out that the Town is required to report in the governmental-wide statements full accrual, not the fund statements, that liability as calculated by our actuarial. The Town is required to implement effective June 30, 2009. The required contribution to prefund the benefits is calculated by the actuarial and generally, due to budget cutbacks, these required contributions are not prefunded. A liability is reported on the government wide financial statements of what the required contribution is and what the cost is on the pay as you go basis, net OPEB liability. This does not hit the fund statements, another reconciling item. Mr. Wilkinson explained that if the actuarial calculated the town's required contribution \$3M to fund these benefits but the town was continuing on its "pay as you go" basis which may only be \$1M, that \$2M liability is what gets reported on the government wide statements. This number fluctuates depending on your work force. This will hit the statement of net assets, not budgeted, it is viewed as a GASB disconnects in governmental accounting. The actual present value of benefits will be noted in the footnote.

- Page 16 & 17 – Statement of Operations – Major Funds – the General Fund recognized an excess of revenues over expenditures of approximately \$385,000 on a \$70M budget, considered within the "norm". The School Department ended the year with a surplus of approximately \$586,000 and the Debt Service broke even.

Jim brought the issue up to the committee that the Governmental Accounting Standards Board is looking at clarifying the use of special revenue funds. They are looking at these funds as to having an external restriction or regulation or law that requires these funds to be set up so that Town's are not setting these little "kitties" along the way. The Town has two of these types of special revenue funds: Termination Retirement Reserve Fund – a fund in which the payout of sick and vacation accrual is allocated at the time of retirement based on contractual obligations and Health Insurance Reserve fund – a fund in which we appropriate money to for future funding of the OPEB liability and once the trust fund gets established to fund the town's liability this fund will be transferred to the trust and be absolved. Typically, the town budgets for these reservations in their operating budget.

- Page 20 – Statement of Operations – Proprietary Funds – Water Fund and QD Recreation Fund. These funds are viewed as being quite healthy, operating well. Both of these funds have transfers to their appropriate Capital Reserve Funds.
- Page 25 – Footnotes – Recently Issued Accounting Standards – Statement 49 – Pollution Remediation. It is too early to tell what this will mean to the financial statements the town is still in the investigative stages with its two landfills that have already been closed. Statement 51 – Intangible Assets – generally for colleges/universities developing patents, not applicable to the town.
- Page 55 – Worker's Compensation Fund - \$50,000 liability had been being carried over 10 years which had been closed out during the year.
- Page 60 & 61 – Reconciliation between Fund Statements and Budgetary Reporting – Jim noted that, primarily, the General Fund difference is that the General Fund recognizes the use of prior year fund balance of \$671,000 as a revenue source, however, under generally accepted accounting principles not reportable as a funding source to fund the budget.

Jim indicated that the town is a little unique in the motor vehicle excise tax in that they defer the revenue received in the current year.

John McNamee questioned page 57 – funding deficit. This information is always two years behind. Assuming from a budgetary standpoint, the town addresses their required contributions. To some extent the town's will be required to compensate for the deterioration in the market value in the pension funds. Mr. McNamee noted that the education expenditures do not currently reflect the debt service payments so the analysis is not complete unless you take into consideration the school department's debt service.

Chairman McCrory questioned the per pupil cost for Jamestown students. Mr. August noted that this cost lagged assessed based on historical data, building in a structural deficit to educate the children from Jamestown. There was some modification because they do provide transportation to their students. Some view its too high, some too low.

- Page 133 – Compliance of Single Audit – Town recognized a little less than \$3M in federal assistance. This section is specific to the school because the town has not received any federal funding. The last audit report

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including a finding of the lack of time and attendance however since then, this issue has been remedied. There are no federal findings or requirements, or lack of, to note. The school has complied with the issues that were reported last year in implementing a time and attendance policy/procedure.

Jim Wilkinson commended the town for implementing a whistleblower hotline. Mr. Wilkinson pointed out that this opportunity should be communicated to all employees and making it readily available. Mr. Wilkinson noted that repeat comments will appear in the 2008 financial statements regarding an accounting manual, the cafeteria fund deficit as well as the lack of control in the school activity funds. A recurring comment over disbursements, maintaining documentation of the paid bills, stamping it paid...some of the bills weren't available for backup of expenditures. When asked the question regarding the process, Lindsey Albermaz explained that the schools which were selected this year, Wickford and Hamilton Elementary, all cash disbursements need to have two signatures and the Principal must sign off on the expense for payment. The auditors select at least 25 transactions and a few that were selected they could not provide the back up. The revenues generated are from various fund raisers and tracked by activity, club, band, etc. It's a pooled account with a ledger kept for each activity. The town is really just acting as a custodian and there are typically a lot of problems, the auditors acknowledge that there is a significant amount of fraudulent activity because there is no segregation of duties. This bookkeeping is reported utilizing Quicken.

John McNamee questioned best practices. Mr. Wilkinson answered that by stating that they had recommended that the school business office take over the issuance of payments, reconciliation, monitoring transactions. It needs to be brought under the internal controls of the school/town and check requests will not be immediate. Dual control over accounting is required while at these fund raising events. Chairman McCrory questioned if a class of 10 years ago had a \$10,000 balance where did the money come from? Fund raisers? Parking lot fees? Jeff Wadovick questioned whether the audit committee is empowered to visit these schools and perform special work on the student activity funds? Mr. Wadovick thought they could look at how the whole process is run from cash receipts/cash disbursements, the internal controls and whether all the funds within the student activity fund are applicable. Or can the audit committee recommend firms to do this particular work. Mr. McNamee indicated that policies should be put into place whereby if they are reunion funds they are put into one reunion account otherwise the burden is put on the schools/principals to do the accounting for these accounts which technically are agency funds within the town. Questioned the town's responsibility because they are not under the town's internal control. Mr. McNamee does not feel the audit committee should be spending time on these agency funds when there is a much bigger areas within the town/school budgets. He is not in favor of doing a special investigation of the activity funds. Chairman McCrory questioned Jim Wilkinson about the fact that if the audit committee were in favor of this then they would be committing the town's time and money to investigate an area that really isn't under the town's purview? Mr. Wilkinson responded, "Yes", but the town does have a fiduciary responsibility and that the town is the custodian of this fund and if anything does happen wonders if there is recourse back? There are a number of municipalities that have the same comments of Jim's clients.

Jim Wilkinson noted that he believed under the new Uniform Chart of Accounts administered by the Department of Education that there is a new reporting requirement for the activity funds which require them to report on a quarterly basis. Mr. McNamee questioned if there was a requirement to have activity funds??

Discussion was wrapped up with an explanation of the types of testing that was performed with management.

MOTION made by Jeff Wadovick, seconded by John McNamee that the town accept the financial statements as presented with the pending draft items to be resolved before December 31, 2008. Vote: unanimous.

**IV. Correspondence**

Mr. August noted the letter sent to the school committee in accordance with a motion from the December 4<sup>th</sup> meeting regarding the relationship between the AD and the Booster's Club. Mr. August noted that the letter offered that a member of the audit committee be available at a school committee meeting where this item will be addressed and Mr. August offered his representation.

**V. Public Comment**

**VI. Next Meeting – not yet determined**

**VII. Adjournment**

MOTION made by John McNamee, seconded by Jeff Wadovick to adjourn. Vote: unanimous.