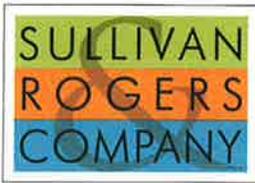


MELROSE PUBLIC SCHOOLS

REVIEW OF SYSTEMS OF INTERNAL CONTROLS  
OVER FINANCIAL OPERATIONS AND REPORTING

NOVEMBER 16, 2012





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Ms. Cyndy S. Taymore, Superintendent  
Melrose Public Schools

We have reviewed select areas of the Melrose Public Schools' systems of internal controls over its financial operations and reporting to assist the Melrose Public Schools in its effort to design strong, transparent, and clearly defined internal control policies and procedures.

We concentrated on the following areas of concern and performed the following:

- Reviewed the funds and accounts of the Melrose Public Schools, in the general ledger, to ensure the funds and accounts are structured and accounted for in a manner to facilitate consistent, transparent and fully inclusive financial reporting.
- Reviewed the system of internal controls over the budget process for the operating fund, grant funds, revolving funds and other funds under the control of the Melrose Public Schools to ensure the system of internal controls is well designed, documented and implemented.
- Reviewed the internal and external financial reports and the system of internal controls over financial reporting.
- Reviewed the system of internal controls over payroll and the use of the MUNIS system to encumber and accrue payroll.
- Reviewed the system of internal controls over purchasing and accounts payable including use of the MUNIS system to process, record and report transactions.

The results of our review are contained within this report. This report is intended solely for the information and use of the management and those charged with governance of the Melrose Public Schools and City of Melrose, Massachusetts and is not intended to be used by anyone other the specified parties.

*Sullivan, Rogers & Co., LLC*

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November 16, 2012

## Fund Accounting Structure

We have reviewed the Melrose Public Schools' fund accounting structure to determine that the accounts are structured in a manner to facilitate consistent, transparent and fully inclusive financial reporting.

The Melrose Public School's accounting system is based on a "fund accounting" structure. Fund accounting is the procedure by which resources for various purposes are classified for accounting and reporting purposes in accordance with regulations, restrictions, or limitations imposed by sources outside the school district (i.e. federal and state grant awards), or in accordance with directives issued by the governing board (i.e. Melrose School Committee). A fund is an accounting entity with a self-balancing set of accounts for recording assets, liabilities, fund balance and changes in fund balance (revenues, expenditures and transfers). Separate accounts are maintained for each fund to ensure observance of limitations and restrictions placed on the use of the resources. For accounting and reporting purposes, however, funds of similar characteristics are combined into fund groups. The fund groups usually encountered in a Massachusetts school district are as follows:

- General Fund
- Federal Grants
- State Grants
- Circuit Breaker
- Private Grants and Gifts
- School Choice and Other Day Tuition
- Athletic Revolving Fund
- School Lunch Revolving Fund
- Other Funds supported by local receipts
- Agency Funds (Student Activity Funds)

The Melrose Public Schools maintains separate funds on the MUNIS accounting system and, with one exception, has adequately grouped funds of similar characteristics. The Melrose Public School's fund groupings are as follows:

- Fund 0111 – General Fund
- Fund 1200 – School Lunch
- Funds 1400 to 1499 – Federal Grants
- Funds 1500 to 1599 – State Grants
- Funds 1600 to 1999 – Revolving Funds and Other Funds Supported by Local Receipts

The exception, where the Melrose Public Schools has not grouped funds of similar characteristics is in regards to student activity funds. The student activity funds are commingled with Revolving Funds and Other Funds Supported by Local Receipts. Student activity funds are agency funds and therefore should be maintained separate from all other fund groups. The agency fund group consists of funds held by the Melrose Public Schools as custodian or fiscal agent for others such as student organizations and clubs. Transactions of agency funds represent charges or credits to the asset and liability accounts and are not revenue and expenditure transactions of the Melrose Public Schools. Agency Funds are used to deposit funds that do not belong to and are not under the control of the School Committee, but rather are private

funds that belong to the depositor. The Melrose Public Schools is essentially providing a banking function for the depositor, and these funds are then disbursed at the direction of the depositor. Student Activity Funds are regulated by Massachusetts General Law (MGL) Chapter 47, Section 47.

Regarding the account structure for expenditure accounts, the Melrose Public Schools has created accounts that use 10 segments and a character code to define an account and assist with performing budgetary control and financial reporting. The account structure is as follows:

- Segment 1 - Fund
- Segment 2 - Function
- Segment 3 - Grant Year
- Segment 4 - Grant Line
- Segment 5 - School Location
- Segment 6 - Subject
- Segment 7 - DESE EOYR Program
- Segment 8 - Grade
- Segment 9 - Object
- Segment 10- DESE EOYR Function
- Character Code - DESE EOYR Object

The account structure had been designed in a manner to facilitate both internal and external financial reporting. Management has the ability to sort its MUNIS financial reports on any segment in the account structure. There are various standard reports as well as reports that can be designed utilizing Crystal Reports, a feature in MUNIS. Therefore, MUNIS can be used to prepare external reports such as the Department of Elementary and Secondary Education (DESE) End of Year Financial Report (EOYR) and for Federal and State grant reporting. MUNIS can be used internally at every level of management and staff to review financial performance and monitor and control spending.

Additionally, the account structure is designed in a manner to allow for automated budgetary control. Budgetary control can be set at any segment on the account structure. It can be set to control spending for an individual account or a group of accounts by controlling it at the organization code level, the account level or utilizing a budget rollup code. Using the segments of the account, budgetary control can be handled differently depending on the nature of the account. For example, budgetary control may differ between fund groups. General fund expenditure budgetary control may be set at the school location level or the subject or on the individual account. For grants, budgetary control may be set at the grant line level. The Melrose Public Schools chart of accounts has been designed to provide flexibility to management so that budgetary control can be meaningful and automatic.

Revenue accounts have been created in the chart of accounts in conformity with the Uniform Municipal Accounting System of the Commonwealth of Massachusetts (UMAS). Revenues are identified by fund, grant year and by object. Revenue accounts have been created in a manner to facilitate financial reporting and budgetary control.

Though we found that the account structure has been designed to facilitate effective and efficient financial reporting and budgetary control, we found instances in which the accounts were not created in a

manner to take advantage of this functionality. For example, we found instances in the area of federal and state grants where the accounts were not created in conformity with the grant award and budgetary control was not properly set at the grant line. Therefore, the MUNIS information could not be used for budgetary control and grant reporting. Instead, the Business Office and those responsible for the grant used Excel worksheets and manual ledgers to monitor the grant. The Melrose Public Schools, through its Business Office should utilize MUNIS to account for the grants in accordance with grant award. Budgetary control should be set at the grant line.

### System of Internal Controls over the Annual Operating Budget Process

The Melrose Public Schools has an established budget process for each school year that involves all budget holders including, including but not limited to the School Committee, Superintendent, Business Manager, Curriculum Directors, Technology, Maintenance and Principals. We received a copy of the FY2013 Budget Development Timeline which documented each step of the budget process with deadline dates. There were 14 steps in total, beginning with the budget issuing guidelines to the budget holders on October 14, 2011 and ending with the budget presented to the Board of Alderman on April 2, 2012. Overall, the FY2013 Budget Development Timeline appears to be well designed to carry out an efficient and orderly budget process.

The budget holders for FY2013 were as follows:

- Administration
- Athletics
- Elementary Art
- Elementary Health
- Elementary Library-Media
- Elementary Music
- Elementary Physical Education
- High School
- Hoover School
- Horace Mann School
- Lincoln School
- Maintenance
- Middle School
- Roosevelt School
- SPED
- System-Wide
- System-Wide Professional Development
- Technology
- Winthrop School

The budget timeline for FY2013 was as follows:

STEP	DEADLINE
1. Budget Guidelines along with District Goals/Request for Goals are distributed to budget holders	October 14, 2011
2. Preliminary budget requests and goals are submitted to the Business Manager for review	November 10, 2011
3. Revenue and Grant 5-Year trend distributed to and presented to School Committee	November 15, 2011
4. Review/discussion of fees and public input on budget	December 6, 2011
5. Departmental and School budget meetings between budget holder, Superintendent and Business Manager to finalize budget requests	December 9, 2011
6. Completed budget submitted by budget holders to the Business Manager	January 20, 2012
7. Fees (Public Comment and Vote)	January 24, 2012
8. Budget presented to School Committee	February 14, 2012
9. School Committee review of Administration, Facilities, Technology, System-Wide budgets	February 14, 2012
10. School Committee review of Elementary Schools and SPED budgets	February 28, 2012
11. School Committee review of Middle School, High School, and Athletics budgets	March 13, 2012
12. Public Forum on budget	March 20, 2012
13. School Committee public budget deliberation discussion and vote on final budget	March 27, 2012
14. Present Budget to Board of Alderman	April 2, 2012

We received a copy of each of the FY2013 goals for each individual budget holder. The FY2013 goals are documented in an Excel worksheet that discusses the overall goals guiding the Melrose Public Schools FY2013 budget and the specific goals for each budget holder. It is a detailed record.

We also received a copy of the FY2013 School Budget Guidelines issued on October 14, 2011 to the budget holders from Joseph F. Casey, Superintendent of Schools. The memo described the role of the principals

and other budget holders in the budget process and the manner in which they will complete the budget worksheets. The instructions stated that all non-salary budget requests be itemized using the budget entry worksheet(s) and that the amounts entered into the worksheet reflect the FY2013 budget needs/request. Budget holders were also asked to provide a list of any projected staff changes such as retirements, resignations, leaves of absence, etc. and if any position(s) can be reduced due to enrollment or any other reason. Requests for additional staff would only be considered if they are necessary to address enrollment and/or SPED needs.

We received and reviewed the budget worksheets for FY2013. Each school was given its own budget worksheet on Excel and was asked to update the worksheet. The Excel worksheets were designed with consistency for each school and when required was tailored to that specific school's needs. Each worksheet showed the due date, the name of the budget holder and was divided into tabs for each major budget line item. For example, the Technology budget worksheet had a tab for computer supplies, a tab for computer equipment and a tab for computer maintenance. Each worksheet for a school was set up in a similar manner. For example, the budget worksheet for the Horace Mann School had a separate tab for instructional materials, instructional supplies and other instructional materials. Each individual tab was very detailed. The summary tab showed the budget that was approved from FY2012 and the budget amount requested for FY2013. Where the budget worksheets fall short is that the individual tabs do not show comparison from prior years. Budget worksheets given to the budget holders should show the most completed prior year actual, the prior year original budget and revised budget for each line item.

The salary and wages and employee benefits budgets are not prepared at the school level by the principals and other budget holders. These budgets are prepared by the Business Office and allocated to the schools in the overall budget worksheet. The principals and budget holders have input on the needs but the actual costs are calculated at the Business Office, taking into consideration the needs of each school. Currently, salaries and wages are calculated for each employee on a very detailed Excel worksheet at the Business Office, which is a time consuming process. We will discuss later in this report how using MUNIS Salary and Benefit Projections will save time and improve accuracy in calculating the payroll budget.

Where the budget process falls short in design and execution is that the Melrose Public Schools is not using the MUNIS accounting information system to facilitate the budget process. The Excel worksheets may be well thought out but they are time consuming to populate with historical information, formulas, and they are not widely and easily accessible while the budget process is in play. The MUNIS accounting information system has a budget module that can be accessed by all budget holders and management and there is no need to manually enter historical data and roll forward worksheets because information is available in real time. In addition, the MUNIS system can create a salary and benefit budget projection based on the current salary and benefit data tables already maintained by the Melrose Public Schools for normal every day payroll processing. The MUNIS system already has this information and use of the Excel worksheets is not needed.

In addition, little is mentioned in the budget process related to the expenditures funded by federal and state grants. Even though these grants do not require the School Committee authorization, the majority of these grants are funding initiatives and expenditures that meet the School Committee's goals and federal and state requirements. The majority of these expenditures would otherwise be paid for through

taxation and/or local receipts. The budget process should take these projected expenditures and revenue sources into consideration.

### Budgets for Grant Funds

The Melrose Public Schools accounts for each grant in its own fund and by grant year. The Melrose Public Schools chart of accounts is designed to facilitate processing grant revenues and expenditures so that each grant year is separate and distinct. A revenue and appropriation budget is created on the MUNIS accounting system for each grant year. Unfortunately, in some cases the budget that is put into MUNIS is not a reflection of the budget as shown on the grant award. Grant awards need to be expended exactly as stipulated in the award. Through our interviews and observations we noted that in some cases the grant managers would not use the MUNIS reports because of this problem. The grant managers maintained their own set of records either on Excel or manually. This is counterproductive and is a breakdown in internal controls over grant expenditures. We recommend that the Melrose Public Schools ensure that the MUNIS budgets for grants mirror the grant award and that those responsible for monitoring the grants use MUNIS for such purpose.

### Budgets for Revolving Funds

Revolving funds automatically receive an appropriation budget as funds are received and recorded into the MUNIS accounting system. The MUNIS accounting system has a mechanism which the Melrose Public Schools uses to automatically increase the appropriation budget as revenues are received. Budgetary control is set so that purchase orders and expenditures cannot be entered into the MUNIS system greater than the budget. Therefore, the risk of overspending is maintained at a low level. This budget process is effective for gifts and donation funds; however it is not effective for revolving funds that are considered integral to the annual operations of the Melrose Public Schools. These integral funds are called "Applied Funds" by the Melrose Public Schools. Applied Funds are as follows:

- Athletic Revolving
- Circuit Breaker
- Concessions
- Computer - E-Rate
- Facilities
- Kindergarten
- Medicaid Revolving
- Music Revolving
- Tuition/Transportation Revolving
- Education Stations - After School Program

Applied Funds are budgeted for in the annual budget process. However their annual budgets are not entered into MUNIS. In order to use MUNIS for the annual budget process the Melrose Public Schools will need to convert the Applied Funds to annual funds and budget accordingly.

### External Financial Reporting

We reviewed the financial reports submitted to the Department of Elementary and Secondary Education (DESE) for the past 3 years and noted that the annually required financial reports were filed on time and accurately. An independent compliance audit is performed each year the Melrose Public Schools End of Year Financial Report and no material findings were reported in the past 3 audits.

The Melrose Public Schools federal grants are audited as part of the City of Melrose's Single Audit. We received a copy of the past 3 audits. There was no material findings and/or questioned costs reported related to the grants administered by the Melrose Public Schools.

### Internal Financial Reporting

The Melrose Public Schools internal financial reporting is hampered by the fact that there is limited access to the MUNIS accounting information system within the Melrose Public Schools. Access to the MUNIS system is limited to the Business Manager and staff of the Business Office. The majority of all budget holders have no access to MUNIS. They have to rely on receiving periodic MUNIS reports from the Business Office. These reports are not disseminated on a regular basis. Additionally, the MUNIS reports do not always mirror the Excel budget worksheets that the budget holders were involved with during the budget process.

We noted that even in the business office, personnel with access to MUNIS will continue to use Excel worksheets or manual worksheets that they are more comfortable with. This is time consuming and unnecessary.

We recommend that all budget holders be given access to the MUNIS system and be trained on reporting functionality.

We recommend budget holders be asked to review and approve year-to date budget to actual expenditure reports quarterly and that these reports be maintained on hand at the central office until after the year-end audit.

We recommend that the School Committee be provided with a standard package of MUNIS generated year-to-date financial reports on a regular basis throughout the school year.

The Melrose Public Schools should refrain from utilizing Excel reports because these reports are labor intensive to prepare, prone to error and do not necessarily agree with information on the MUNIS system. Using MUNIS reports will strengthen internal controls over financial reporting because the information contained in MUNIS will be reviewed and there will be a greater chance that errors or irregularities will be detected timely.

## Payroll

Melrose Public Schools employs approximately 530 full time equivalents and in FY2013 appropriated approximately \$22,500,000 in salaries and benefits, representing almost 90% of the total annual operating budget. The Melrose Public Schools pay employees through the MUNIS payroll system; however the MUNIS payroll system is underutilized. Administrative personnel at the schools as well as employees of the Business Office expend significant time budgeting for payroll on Excel worksheets and processing payroll using manual attendance cards and worksheets. There are three features of the MUNIS payroll system that the Melrose Public Schools should use to save significant time and improve financial reporting and budgetary control over payroll. The features are as follows:

- *Salary and Benefit Projections* - The salary and benefit projection module can be used in conjunction with the budget module to calculate payroll expenses for the next year. The projection is created by copying the live master files into a separate space in MUNIS. Melrose Public Schools is then able to simulate all the changes that would normally take place over the course of a projection period. The projection can be proofed and posted to the budget module. It is an efficient and accurate tool for budgeting salaries and benefits, representing 90% of the total budget.
- *Payroll Encumbrances* - Next to budgeting for salaries and benefits, the most important step in ensuring that the funds are available when needed is through encumbering. The Melrose Public Schools has the ability to use MUNIS to encumber employees' salaries and benefits at the beginning of the year for the entire year. The encumbrance is based on the actual calculation of salaries and benefits in the MUNIS payroll tables. Therefore, on day one of the school year, management will know exactly what is being used and what is available in the salaries and benefits budget. As payroll is expended each period, the encumbrance is liquidated equal to the amount expended.
- *Time and Attendance* - The MUNIS time and attendance program is designed to eliminate paper processing and manual record keeping by using MUNIS as the record keeper. Currently, the schools maintain manual records and send manual records to the Business Office to enter into MUNIS which is inefficient and a duplication of effort. The Time and Attendance program interfaces with MUNIS payroll and takes the place of the manual records currently be maintained. The information is entered once, then reviewed by the Business Office and then imported into payroll. Some of the advantages of using MUNIS time and attendance are as follows:
  - Allow the individual schools to enter time worked and or absences directly into MUNIS.
  - Allow the Schools to enter substitute teacher time worked directly into MUNIS.
  - Allow the schools and departments to report on and verify their payrolls

## Purchasing

The Melrose Public Schools does not use the MUNIS system to initiate and process requisitions and purchase orders. Currently, the Melrose Public Schools uses manual purchase orders generated from Excel. The schools and departments complete the purchase order, print it and send it to the School Business Manager for approval. Once the purchase order is approved by the Business Manger, it is entered into MUNIS. This manual system does not provide adequate budgetary control. When the purchase order is initiated, no budget check is performed. There were instances noted where purchase orders were presented to the Business Manager incomplete and with no account number. There is no record that a purchase order is in process until it is entered into MUNIS, which occurs at the very end of the process.

The Melrose Public Schools should be using the MUNIS purchasing module at the inception of the requisition process. This module will decentralize and automate the entire purchasing process from inception of a requisition to generating a purchase order to receiving the goods of services and paying for them through accounts payable. MUNIS offers an automated workflow that will guide a requisition through the system. You assign approvers and the requisition has to be approved electronically by each approver before it moves to the next approver. From the moment a requisition is entered into the system there is a record of it that never is deleted, it just changes status. Also, a requisition cannot be initiated without an expenditure account number to charge. If there is no available budget, the requisition cannot be entered. Using the MUNIS purchasing module will help ensure compliance with Massachusetts General Law (MGL) on procurement, Chapter 30B. The Melrose Public Schools can set different dollar thresholds for the approval process. Documents supporting compliance with MGL Chapter 30B can be scanned and attached to a purchase order. Fully implementing the MUNIS purchasing module will strengthen internal controls over purchasing and provide real-time accountability.

We recommend the Melrose Public Schools implement a decentralized requisition and purchasing process using MUNIS.

## Accounts Payable

The Melrose Public Schools utilizes a centralized accounts payable process where all invoices and bills are presented to the Business Office for payment. On average, it takes well over one month to process a bill for payment. It takes at least 2 weeks to process the bill in the Business Office and then another 2 weeks to process it at the City Auditor's Office before it is then given to the Treasurer to pay. This is a long time and we were told that the Business Office receives calls from vendors looking for payment. However, we noted that bills are carefully matched with purchase orders and reviewed closely by both personnel at the Melrose Public Schools and the City Auditor's Office.

At this time, we do not recommend decentralized accounts payable entry. However, we recommend that the Melrose Public Schools consider providing additional resources to the accounts payable function. Currently there is only one accounts payable clerk.

### MUNIS implementation and training

The MUNIS automated accounting system is underutilized at the Melrose Public Schools. As discussed in previous sections of this report, MUNIS is inaccessible to the majority of budget holders. MUNIS is a powerful tool for budgetary control and financial reporting and should be used throughout the district for preparing the annual budget, preparing grant budgets, processing payroll, initiating and approving requisitions and purchase orders, processing accounts payable and generating all internal and external financial reports. MUNIS has security built into its system. When transactions are processed through MUNIS, they are better protected and information is more timely available to all users. Using MUNIS will inherently create more transparency and accountability.

In order to operate in today's work environment the Melrose Public Schools needs to fully utilize the automation at its disposal. To do this, the Melrose Public Schools will have to invest in new equipment but also must provide training and support to the end users. We recommend the Melrose Public Schools develop and implement a systematic plan to fully automate its system of internal controls using the MUNIS system. The change cannot happen overnight and must be carefully planned and executed over a reasonable and realistic time period.