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Board of Selectmen
Town of Pepperell
1 Main Street
Pepperell, MA 01463

Dear Members of the Board:

In planning and performing our audit of the financial statements of the Town of Pepperell, Massachusetts as of and for the year ended June 30, 2016, in accordance with auditing standards generally accepted in the United States of America, we considered the Town of Pepperell, Massachusetts' internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Town of Pepperell, Massachusetts' internal control. Accordingly, we do not express an opinion on the effectiveness of the Town of Pepperell, Massachusetts' internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses.

A deficiency in internal control 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 and correct misstatements on a timely basis. A material weakness is a deficiency or combination of deficiencies in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

We do not consider the following items to be significant deficiencies or material weaknesses. They are informational matters that we want to communicate to you.

We, also, want to point out that this is the second year in a row where we have no findings to report. During this two year period, an excellent job has been done relating to recording, reporting and reconciling all accounting transactions. We want to commend the Town personnel for their efforts.

Uniform Guidance

An audit must be performed in accordance with the federal single audit act requirements only when an entity expends more than \$750,000 of federal funds during a fiscal year. However, even if an entity expends less than \$750,000 in federal funds in a fiscal year, it is still required that all entities who receive any federal monies, have certain procedures and controls in place.

On December 26, 2013, OMB published its comprehensive overhaul of federal grant administrative, cost accounting, and audit policies in the Federal Register. This final guidance, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards, supersedes and combines the requirements of eight existing OMB Circulars (A-21, A-50, A-87, A-89, A-102, A-110, A-122 and A-133). The Uniform Guidance significantly reforms federal grant making to focus resources on improving

performance and outcomes with the intent to reduce administrative burdens for grant applicants and recipients and reduce the risk of waste, fraud, and abuse.

The Uniform Guidance is a substantial document that addresses (among many other topics) cost principles, internal controls, procurement requirements and audit requirements. The Uniform Guidance is effective December 26, 2014. New and incrementally-funded awards issued on or after December 26, 2014 will be subject to the Uniform Guidance. Audit Requirements will apply to audits of fiscal years beginning on or after December 26, 2014 (i.e fiscal year 2016).

One of the primary focuses of the new Uniform Guidance (as it relates to grantees) is internal controls over federal grants. The meaning of “must” and “should” as they are used throughout the Uniform Guidance is clarified. “Must” is not optional, “should” is recommended.

Section 200.303 of the Uniform Guidance addresses internal controls and states:

The non-Federal entity (i.e. the Town) must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States and the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).
- (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.
- (c) Evaluate and monitor the non-Federal entity’s compliance with statute, regulations and the terms and conditions of Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.
- (e) Take reasonable measures to safeguard protected personally identifiable information and other information the Federal awarding agency or pass through entity designates as sensitive or the non-Federal entity considers sensitive consistent with applicable Federal, state and local laws regarding privacy and obligations of confidentiality.

The “Internal Control Integrated Framework” issued by the COSO commission identifies five components of internal control that they believe should be considered in every system of internal control.

The five components are:

- (1) Control Environment (The “tone at the top” should promote and expect ethical behavior.)
- (2) Risk Assessment (Consider what could go wrong and what is its impact.)
- (3) Control Activities (What controls have we established – reconciling, approvals, oversight...)
- (4) Communication and Information (Is pertinent information captured, identified and communicated on a timely basis? Are records and information systems sufficient to provide reliable reporting and to demonstrate compliance with the federal award?)
- (5) Monitoring - Are the internal controls operating as intended? Have controls become outdated or obsolete? Monitoring occurs in the course of everyday operations; it includes regular management & supervisory activities and other actions personnel take in performing their duties.

The Uniform Guidance requires that the internal control policies and procedures must be in writing. Topics that must be addressed in the internal control procedures document relating to procurement include the following:

- Must maintain oversight to ensure contractors perform within the terms, conditions and specifications of the contracts or purchase orders
- Must maintain written standards of conduct covering conflict of interest with respect to employees engaged in the selection, award and administration of contracts
- Must maintain written standards of conduct covering organizational conflict of interest.
- Must avoid acquisition of unnecessary or duplicative items.

The Uniform Guidance raises the threshold for the requirement of an audit performed under the Single Audit Act to \$750,000 of federal expenditures in a fiscal year. Although the Town may not fall under the requirements of the Single Audit Act in the near future, we recommend that the Town become familiar with the new requirements of the Uniform Guidance and develop written internal control policies and procedures in order to comply with the Guidance.

Implementation of New GASB Pronouncements

As we noted in the past, the GASB has been very active during the past few years in creating new GASB statements that apply to Governments throughout the country. We have noted below the new pronouncements that become effective during fiscal year 2016 and after. Some of these Statements may not be applicable to the Town. We will work closely with the Town to determine which statements are required to be implemented by the Town.

During fiscal year 2016, the following GASB pronouncements were implemented:

- The GASB issued Statement No. 72 *Fair Value Measurement and Application*. The standard created a hierarchy of the valuation methods used in determining the fair value of investments. The implementation of this pronouncement required new disclosures related to the Town's investments.
- The GASB issued Statement No. 76, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*. The implementation of this pronouncement did not impact the financial statements.
- The GASB issued Statement No 79, *Certain External Investment Pools and Pool Participants*. The implementation of this pronouncement did not impact the financial statements.

The following GASB pronouncements will be implemented in future fiscal years:

- The GASB issued Statement No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68*, which is required to be implemented in fiscal year 2017.
- The GASB issued Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, which is required to be implemented in fiscal year 2017.
- The GASB issued Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, which is required to be implemented in fiscal year 2018.
- The GASB issued Statement No. 77, *Tax Abatement Disclosures*, which is required to be implemented in fiscal year 2017.

- The GASB issued Statement No. 78, Pensions Provided through Certain Multiple-Employer Defined Benefit Pension Plans which is required to be implemented in fiscal year 2017.
- The GASB issued Statement No 80, Blending Requirements for Certain Component Units—an amendment of GASB Statement No. 14 which is required to be implemented in fiscal year 2017.
- The GASB issued Statement No 81, Irrevocable Split-Interest Agreements, which is required to be implemented in fiscal year 2018.
- The GASB issued Statement No 82, Pension Issues—an amendment of GASB Statements No. 67, No. 68, and No. 73 which is required to be implemented in fiscal year 2018.

Management is currently assessing the impact that the implementation of these pronouncements will have on the basic financial statements. Management's current assessment is that GASB Statements #74 & 75 will have a significant impact on the Town's basic financial statements by recognizing the entire actuarially accrued liability and expense, related to the Town's Other Post-Employment Benefits.

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This communication is intended solely for the information and use of management, those charged with governance and others within the organization, and is not intended to be and should not be used by anyone other than those specified parties.

After you have had an opportunity to consider our observations, we shall be pleased to discuss them further with you. We would like to thank you for the cooperation and courtesy extended to us during the course of the engagement.

Very truly yours,

Giusti, Hingston and Company

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