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November 4, 2011

To the Members of City Council
City of York, Pennsylvania

In planning and performing our audit of the financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund and the aggregate remaining fund information of the City of York, Pennsylvania, as of and for the year ended December 31, 2010, in accordance with auditing standards generally accepted in the United States of America, we considered the City's 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 City's internal control. Accordingly, we do not express an opinion on the effectiveness of the City's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be significant deficiencies or material weaknesses, and, therefore, there can be no assurance that all such deficiencies have been identified. In addition, because of inherent limitations in internal control, including the possibility of management override of controls, misstatements due to error or fraud may occur and not be detected by such controls. However, as discussed below, we identified certain deficiencies in internal control that we consider to be 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 consider the following deficiencies in the City's or Component Units of the City's internal control to be material weaknesses:

- **Redevelopment Authority - Self-Balancing Set of Books**

As noted in our prior year recommendation letter, the Redevelopment Authority of the City of York (the "Redevelopment Authority") does not have a separate complete self-balancing set of books. The City reports information for the Redevelopment Authority in its financial statements by compiling activity from cash summary statements provided by the Redevelopment Authority.

The inherent risk of having an unrecorded transaction in the financial statements is greatly increased by the practice of not having one general ledger where all transactions of the Redevelopment Authority are recorded.

We recommend the Redevelopment Authority maintain a separate self-balancing set of books. The books should include all balance sheet and income statement accounts and reflect all transactions incurred by the Redevelopment Authority. This will reduce the risk of transactions not being recorded. The end-of-year trial balance should be sent to the Finance Department so the City can include this information in its financial statements.

- **Audit Adjustments**

During our audit, we proposed multiple adjustments that, in our judgment, could have a significant effect, either individually or in the aggregate, on the City's financial reporting process. These audit adjustments are presented and disclosed in the communication with those charged with governance provided to the members of City Council. The City continues to make improvements in this area.

We recommend the City establish controls to ensure that all significant adjustments are made to the financial statements.

- **Allocation and Recording of Interest Earned in the City Treasurer/Control Account and the City's Accounts Payable Control Account**

As noted in our prior year recommendation letter, the City changed banks for multiple accounts, and some accounts changed from noninterest bearing to interest bearing. During our audit, we noted the City Treasurer/Control Account had accumulated interest earned in 2007, 2008, 2009 and 2010 that was not recorded in the City's general ledger. The amounts were recorded as reconciling items on the cash reconciliations for these accounts.

We recommend the City create a policy to track and allocate the interest earned in the City Treasurer/Control Account. The City Treasurer/Control Account is used to collect monies for the City, County and School District. The policy should address the equitable allocation of interest between the County and the School District and between the City's Governmental and Proprietary Funds.

We further recommend transferring the interest earned in these accounts to the School District, County and City's investment account on a monthly basis. The City's interest should be recorded in the general ledgers of the various funds based upon a monthly allocation calculation.

- **Cash Overdrafts**

As noted in our prior year recommendation letter, various funds had significant cash deficits as of December 31, 2010. The City covers the cash deficits in these funds by borrowing cash from other funds.

We recommend the City, as part of the budget process, consider preparing separate cash flow projections by fund. With document in hand, interfund borrowing, as well as the repayment of such borrowing, can be planned.

- **Interfund Receivables/Payables**

As noted in the preceding comment, we noted instances where certain funds had cash deficits. When a particular fund has a cash deficit and borrows funds from another fund, an interfund payable results in the fund that borrowed the funds and an interfund receivable results in the fund that paid out the funds. Over time, these interfund receivables and payables can grow as a result of the fund deficits. The City has not addressed the issue of paying down these interfund payables in the budget process.

We recommend the City, as part of the budget process, address the repayment of interfund receivables and payables. The balances of receivables and payables should be reviewed by management on an annual basis to determine if repayment is expected in a reasonable time period. If repayment cannot be expected, the interfund balances should be reduced and the amount that is not expected to be repaid should be reported as a transfer from the fund that made the loan to the fund that received the loan.

- **Controls Over Employer Pension Contributions to Plan**

For 2008, 2009 and 2010, the City did not fund the entire required minimum municipal pension obligation to the Pension Trust Funds by December 31 of the respective year. For 2008, the residual required minimum municipal obligation funded after December 31, 2008, was \$3,069,057, which was funded in January 2009. For 2009, the total required minimum municipal obligation for Fire and Police was \$4,905,420, of which \$655,912 was funded by the year ended December 31, 2009. The remaining balance of \$4,249,508 was not funded until February 2010. For 2010, the required minimum municipal obligation for Fire and Police was \$5,050,214, of which \$623,316 was funded by December 31, 2010. The remaining balance of \$4,426,898 was not fully funded until May 2011. The City recorded a liability for these amounts for the respective years in the General Fund and recorded a receivable in the Pension Trust Funds for the equivalent amounts due.

The Municipal Pension Plan Funding Standards require that any amount of minimum obligation of the municipality which remains unpaid as of December 31 shall have interest charged from January 1 of the year in which the minimum obligation was first due until the date of payment. The rate of interest charged shall be paid at the greater amount of the interest rate utilized for the actuarial valuation report or the discount rate applicable to Treasury bills issued by the Department of Treasury of the United States with a six-month maturity as of the last business day in December of the plan year in which the obligation is due. The total calculated accumulated interest due as of December 31, 2010, was \$488,457, which was funded in July 2011. The City provided a liability for this amount in the financial statements for the year ended December 31, 2010.

We recommend the City institute procedures to ensure the minimum municipal obligation is funded prior to December 31 of the same year. In order to fund the pension timely, the City must review the budget process in order to meet the cash flow needs to fund the minimum municipal obligation by year-end.

- **Controls Over Preparation of the Schedule of Expenditures of Federal Awards**

Throughout our audit process, we noted multiple errors on the original schedule of expenditures of federal awards provided to us by the Grant Coordinator. These errors were corrected based on the audit procedures and through further review and follow-up with the Grant Coordinator and the Deputy Business Administrator.

We recommend the City institute procedures to ensure that an accurate and complete schedule of expenditures of federal awards is maintained. The Grant Coordinator should prepare and update this schedule on an ongoing basis throughout the year. In order to prepare this schedule accurately, it is important to ensure that the Grant Coordinator receives all required information from the departments administering the grants. In addition, the Grant Coordinator will need to reconcile information maintained by the grants administrator to the general ledger in BBAS.

- **Controls Over State Grants - Redevelopment Assistance Capital Program Renovation - Northwest Triangle Project (City of York Redevelopment Authority)**

The Redevelopment Authority entered into a grant agreement with the Commonwealth of Pennsylvania for the purpose of an urban revitalization project. The RACP (Northwest Triangle) program is a significant and complex project, and there were many conditions that had to be satisfied under the grant agreement in order for the Redevelopment Authority to receive the grant funds. From 2008 through 2011, the Redevelopment Authority submitted three applications for grant reimbursements for costs incurred through December 31, 2010. In 2010, the Commonwealth of Pennsylvania approved the first request submitted for costs through December 31, 2008, and submitted reimbursement to the City in the amount of \$2,456,876. Applications 2 and 3 were processed by the Commonwealth in 2011.

During our audit process and per review of the Commonwealth-approved grant reimbursement request for applications 1 through 3, we noted that there were significant reductions in total allowable costs credited to the program from the original applications submitted by the Redevelopment Authority. The expenditures submitted for the Redevelopment Authority's first three requests totaled \$9,068,722. However, the approved revised applications from the Commonwealth totaled \$6,267,097 for a reduction of credited allowable cost to the program in the amount of \$2,801,625. During our audit and per review with the Redevelopment Authority management, we noted the Redevelopment Authority did not have a detailed accounting and full explanations for the composition of this reduction in total allowable costs.

Through communications with the Commonwealth and per review with the Redevelopment Authority management, we noted that the Commonwealth is not reimbursing interest expense incurred on the program until the amounts are paid. Interest incurred has been added to the Redevelopment Authority's line of credit, and the Commonwealth has indicated that it is not yet eligible for reimbursement as it has not been paid. Total line of credit interest expense claimed on the original first three reimbursement requests totaled \$1,170,375. The disallowed interest makes up a portion of the \$2,801,625 reduction of allowable costs referred to in the preceding paragraph.

The Redevelopment Authority utilized a line of credit to fund a significant portion of the project's expenses as well as unpaid accumulated interest on the line. The Redevelopment Authority intends to utilize the grant funds received from the RACP grant to pay down the outstanding balance on the line of credit. As of December 31, 2010, the amount outstanding on the line of credit was \$4,470,397. With the significant delay in the Redevelopment Authority receiving funds from the project, the City has incurred significantly more interest than originally anticipated, which was added to the line of credit.

In addition, a third-party developer is no longer providing a local match for the residential portion of the project. The Redevelopment Authority is seeking alternatives to securing a replacement for this local match. As a result of the above facts and circumstances, these issues can significantly impact the overall project costs and the ability of the Redevelopment Authority to meet cash flow demands of the project and provide funds required to repay the line of credit. The Redevelopment Authority does not have an updated cost projection and cash flow needs analysis and plan for this project.

We recommend the Redevelopment Authority meet with the Commonwealth to get a full and detailed accounting and explanations as to why the costs submitted for the original application were reduced and not approved. As a result of this follow-up, the Redevelopment Authority should be able to identify exactly which costs submitted on the original applications were not approved. This follow-up is extremely important as the Redevelopment Authority should identify the reasons why the costs were not approved and if additional information should be provided that would result in the allowance of these expenditures. In addition, it is important for the Redevelopment Authority to identify which costs will not be allowed with respect to the project in the future.

We recommend the Redevelopment Authority review the issue with respect to the Commonwealth not allowing interest as an allowable cost until paid. The interest on this project has been incurred by the Redevelopment Authority and added to the line of credit. The Redevelopment Authority needs to address the issue of how it expects to pay this accumulated interest in order to satisfy the Commonwealth's requirements for an eligible cost under the program.

In addition, we recommend the Redevelopment Authority complete an updated cost projection and cash flow needs analysis and plan for this project. As a result of the above facts and circumstances, these issues can significantly impact the overall project costs and the ability of the Redevelopment Authority to meet cash flow demands of the project and provide funds required to repay the line of credit. The project's cost projections and plans and analysis developed by the Redevelopment Authority should address the funding issues related to the project. First, the plan and analysis should address the Redevelopment Authority's ability to timely meet all of the matching requirements required under the grant. Second, the plan and analysis should address the Redevelopment Authority's ability to meet cash flow needs with respect to the line of credit and minimize additional interest incurred. Additionally, the plan and analysis should address the Redevelopment Authority's ability to meet the other cash flow demands with respect to the project and enable the Redevelopment Authority to complete the project as timely as possible.

Due to the significant scale and complexity of this project, we further recommend the City's Finance Department and Grant Coordinator provide additional oversight over this program. The City should monitor the status of this grant program to ensure all grant requirements are being met and the funding sources and cash flow needs of the project are adequate.

- **Federal Grants**

Refer to our separate Single Audit Report for findings related to federal grants.

In addition, during our audit, we noted certain matters involving the internal control and other operational matters that are presented for your consideration. This letter does not affect our report dated November 4, 2011, on the financial statements of the City of York, Pennsylvania. We will review the status of these comments during our next audit engagement. Our comments and recommendations, all of which have been discussed with appropriate members of management, are intended to improve the internal control or result in other operating efficiencies. We will be pleased to discuss these comments in further detail at your convenience, perform any additional study of these matters, or assist you in implementing the recommendations.

OTHER RECOMMENDATIONS

- **Consider Updating Indirect Cost Allocations to the Sewer and Sewer Intermunicipal Funds**

As noted in our prior year recommendation letter, the City charges indirect costs to the Sewer and Sewer Intermunicipal Funds based on budgeted expenditures multiplied by an indirect cost allocation factor. The indirect cost allocation factor is not based on an updated indirect cost allocation plan.

We recommend the indirect cost allocation factor be updated to a more recent plan in conjunction with an update of a City-wide indirect cost allocation plan prepared in accordance with OMB-87.

- **Controls Over the Administration of Unclaimed Property**

As noted in our prior year recommendation letter, the Treasurer's office stopped performing the administrative function over unclaimed property. The cash account utilized for depositing these funds and transferring them to the Commonwealth was closed in 2008.

Per review with management, this responsibility will be administered by the Finance Department. Management has informed us that, as of the report date, a separate cash account has not been opened for this purpose, and the Finance Department is working on procedures to administer unclaimed property.

We recommend the Finance Department open a separate cash account for the purpose of administering unclaimed property. The Finance Department should also set up procedures to administer and account for unclaimed property in accordance with Commonwealth law. It is important the City institute procedures immediately to address the administration of unclaimed property in accordance with Commonwealth statutes.

- **Review Collateralized Public Funds Under PA Act 72**

The Pennsylvania Legislature enacted Act 72 in 1971 enabling financial institutions to pledge collateral on a pooled basis for the purpose of providing security for public deposits in excess of the FDIC insurance limitations.

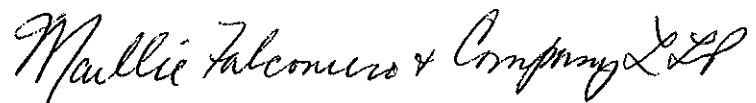
As noted in our prior year recommendation letter, the City does not have formal written agreements with the depository and the custodian. This is not unusual as many public bodies rely on Act 72 with no written agreement or policies set up to monitor collateral. However, considering current economic conditions, we believe it is important the City institute procedures to evaluate and monitor the collateralization provided by the depositories.

We recommend the City have a written agreement with the depository and separate custodian regarding Act 72. The City should refer to its attorney with respect to setting up this agreement with the depository.

We wish to thank the City for the opportunity to be of service in these matters. We would like to thank the staff for the many courtesies extended to us during the course of our audit.

This communication is intended solely for the information and use of the Mayor, members of the City Council and management of the City of York, Pennsylvania, and is not intended to be and should not be used by anyone other than these specified parties.

Very truly yours,



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