

**Nassau County
Office of the Comptroller
Field Audit Bureau**



**Limited Financial Review
of the Westbury Water District**

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Comptroller

October 3, 2007

**NASSAU COUNTY
OFFICE OF THE COMPTROLLER**

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Background

Nassau County has over 200 special taxing districts providing services for town residents. More than half of the special districts are run by independently elected commissioners, the rest are run directly by town officials. In 2005, the office of Nassau County Comptroller Howard Weitzman conducted audits of sanitary special districts in Nassau County. A follow-up white paper discussed problems of waste, fraud and abuse in special districts generally.¹

Following the audits of sanitary districts, Comptroller Weitzman's office undertook audits of the financial operations of four water districts in Nassau County: the Hicksville Water District in the Towns of Oyster Bay and Hempstead, the Westbury Water District in the Town of North Hempstead, and the Franklin Square and East Meadow Water Districts in the Town of Hempstead.

Water districts are governments that exist solely to provide water for residents and commercial establishments primarily in unincorporated areas of towns. District expenses are paid through local property taxes and charges for water, generally based on the gallons used as measured by water meters.

This audit report reviews the financial operations of the Westbury Water District (the "District" or the "Water District"), one of the water districts that shares its Board of Commissioners ("Board") with, and provides administrative resources to, the local fire district (the "Fire District").

District operations are overseen by a Board consisting of three elected commissioners, who run for the position of "Water and Fire District Commissioner." Both districts share the same employer identification number and are considered one district by the Internal Revenue Service, the New York State and Local Retirement System and the Nassau County Department of Civil Service. The two districts collect separate real estate taxes from local residents and issue separate audited financial statements. The two Districts record only one set of Board minutes and the Water District's administrative employees perform 100% of the Fire District's financial and administrative functions.

In 2006, the Water District provided 1.03 billion gallons of water to a population of 20,500, operating 10 wells throughout its five square mile service area.² For 2006, homeowners in the District paid an average of \$203 in taxes in addition to a water charge averaging \$1.26 per thousand gallons. For a District homeowner who used 100,000

¹ *Nassau County Special Districts: The Case for Reform* (Dec. 19, 2005), www.co.nassau.ny.us/comptroller/auditreports.html

The individual sanitary district audits can be found at the same web site.

² Westbury Water District website: <http://www.westburywaterdistrict.com/>

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gallons per year, the average total cost of water was \$329.

The District's total expenses were \$3,695,861 and \$3,574,946 for the years ended December 31, 2005 and 2004. The District employed three elected commissioners, a Superintendent, five administrative and nine operations staff members. The District derives approximately 51% of its revenue from real property taxes, 41% from charges for water usage with miscellaneous revenues making up the remainder.

Audit Scope and Methodology

The scope of our audit was limited to an examination of the District's administrative policies and procedures, procurement practices, operating expenses, administrative expenses, and revenues for the years ended December 31, 2004 and 2005. Our ability to review the appropriateness of the transactions that occurred between the Water and Fire Districts and the accuracy of how each district separately recorded these interactions was severely limited. The New York State Comptroller has exclusive authority to audit the Westbury Fire District and, although the financial statements and the supporting records of the Westbury Fire District were under the direct control of the same board and superintendent, we were not permitted access to them.

Summary of Significant Audit Findings

Lack of Board Oversight

Inadequate Control of District Finances

We found that the Board did not meet its responsibility to control the District's finances. The Board did not pass a resolution to adopt the budget, did not always review and approve (or reject) budget transfers, did not require periodic financial reports such as budget-to-actual variations, nor assume any role in reviewing and approving the District's accounts. There was no evidence that the Treasurer performed any fiduciary oversight, other than to approve vouchers for payment and sign checks.

The Board consistently over budgeted expenses and under budgeted revenues. This practice artificially inflated the tax levy paid by District residents and resulted in the District generating a two year surplus of \$807,970. The District moved \$600,000 in accumulated surplus to the repair reserve of which \$400,000 was without Board approval.

Board minutes did not include ordinary business matters such as annual salary increases, employee benefits and fees even though the Superintendent informed us that he brought such matters to the Board's attention. The lack of active board involvement contributed to a lax internal control environment and a lack of accountability.

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Lack of Policies and Procedures

The Board had not adopted written operating policies and procedures for many key financial functions. We also found that the District lacked a formal code of ethics and conflict of interest policy.

Life Insurance Policies

The District spent \$18,702 in 2004 and \$23,597 in 2005 to purchase individual \$50,000 whole life insurance policies for each of its commissioners and all but one of its employees. These insurance purchases were beyond the scope of the District's statutory authority.

A commissioner was the insurance agent of record on three of the policies and may have received commissions for their purchase. This conflict of interest is an apparent violation of General Municipal Law §801. The District replaced three individual life policies with three new policies from a different carrier, at a higher premium, with no apparent increase in benefit.

The District's Employee Handbook stated that one policy would be provided to each employee. The Superintendent had three policies totaling \$150,000 of coverage. The Handbook stated that the District would be the beneficiary on the policy. Two commissioners, the Superintendent and the son of a former commissioner had policies naming them, not the District, as beneficiary.

Commissioners' Compensation

Per Diem Compensation

During the audit period the combined per diem compensation for the three commissioners was \$42,240 in 2004 and \$45,840 in 2005, based on a payment of \$80 per day, the maximum amount then authorized by New York State law. Commissioners claimed pay for approximately 3 ½ days a week during the audit period.

Because Fire District Commissioners serve without pay, when commissioners worked on Fire District matters, they were not entitled to pay. When the commissioners worked on Water District matters, they could be entitled to a per diem if the work was not unsubstantial. The Board did not require that commissioners describe the Water District work they did when they claimed a per diem. Time records consisted only of commissioner's initials on a calendar maintained by the Superintendent. Commissioners were paid a total of \$65,120 during the audit period for days when there were no board meetings and with no record of what work was performed.

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Health Insurance

As part of their compensation, the commissioners accepted a health insurance buy back for a total cost of \$18,000 over the audit period.

Commissioner's Retirement Reporting

Commissioners were only entitled to retirement credit for work done on Water District matters. The District reported to the New York State and Local Retirement System ("NYSERS"), for retirement credit purposes, that one commissioner worked 207 days in 2004 and 221 days in 2005, while another worked 169 and 176 days, respectively. (The other commissioner was already a State retiree). Two of the three Commissioners were also self employed. We could not ensure that the District was correctly reporting time worked to NYSERS because the District did not establish a standardized workday for commissioners by Board resolution, maintain a record of how many hours the commissioners worked, or record whether the commissioners worked on Water District, as opposed to Fire District, matters.

Employee Compensation

Lack of Authorization for Salaries

Personnel expenditures are the largest component of the District's budget, totaling \$956,710 in 2004 and \$1,101,313 in 2005, or 24% and 28% of operating expenses, respectively. We found serious internal control weaknesses.

The District has a salary progression schedule, however;

- there was no evidence that it was approved, or that compensation issues were discussed by the Board;
- the salaries of many employees exceeded the highest level of the progression schedule; and
- not all job titles were included on the progression schedule.

The Board did not approve raises which exceeded the norm. The Superintendent received increases of 12.72% and 8.76% in 2004 and 2005, respectively. Four other employees received increases ranging from 5.82% to 8.9%, exceeding the 3.5% to 4% typically given to other employees. There was no documentation to explain the rationale for the different raises.

Inadequate Time Records

The District had time clocks to record hours worked, but no procedures governing their use. Some employees regularly clocked in and out; others, including those with the same titles, did not record time worked at all. Even when employees used the time cards, they were paid for time not reflected on the time cards. The Superintendent advised that he

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did not rely on time clock records to record the payroll. Instead, he prepared timesheet summaries for each employee but employees were not required to certify the summaries.

Overtime Practices

The District paid out \$129,331 in 2004 and \$159,585 in 2005 for overtime that cannot be audited for proper authorization and legitimate business purpose due to the failure to maintain overtime records.

Supervisors did not authorize overtime in writing or retain records to explain the need for the overtime. While the Employee Handbook provided that overtime pay applies to hours worked in excess of weekly minimums, three part-time administrative employees received overtime pay based on work time in excess of the normal business day, and not on their weekly total.

Mis-Reporting Part-Time Employees' Time for Pension Purposes

The District reported two of three reduced schedule employees as full time to NYSERS, therefore giving them credit for time not worked.

Personal Use of Business Vehicle

The District provided a new, \$45,000 2005 GMC Yukon for the Superintendent. The District did not have a policy regarding the use of District vehicles and there was no Board authorization for personal use. The Superintendent's personal use appeared excessive as the odometer showed over 11,000 miles in the first six months of vehicle ownership. The District is five square miles and the Superintendent lives 8/10ths of a mile from District headquarters.

Procurement of Professional Services – Lack of Competitive Procurement

The District did not comply with GML §103 and its own policy for the procurement of goods because purchases were routinely made without soliciting quotes or bids from vendors.

We also found that the District's procurement policy, last revised in 1992, does not require the solicitation of alternate proposals for services, including legal, engineering, accounting and insurance. As a result, the District used the same engineering firm, lawyer and accountant for at least 15 years, and bought liability insurance costing \$114,168 in 2005 and \$91,264 in 2004 without engaging in a competitive procurement process to evaluate whether other firms would provide better or more cost effective services.

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Undefined Legal Services

The District paid its attorney \$20,000 each year without an engagement letter to specify the legal services to be provided and without invoices from the attorney to specify the work performed. It was unclear what legal services were provided. In addition to the fees paid under the retainer agreement, the attorney was paid \$7,685 to perform unnecessary reviews of District claim vouchers filed with the Town of North Hempstead.

Over Reliance on Engineering Firm – Possible Conflict of Interest

The District contracts with one engineering firm to advise it on repair and construction of District facilities. The engineering firm provides advice to the Superintendent who proposes projects to the Board. Once approved by the Board, the firm prepares the bid specification documents, performs the engineering work related to the project and monitors the work of a third party on the project. The services provided by the engineering firm create an apparent conflict of interest since it has a substantial economic interest in the advice it gives the District concerning construction or repair projects.

The engineering firm was paid \$300,000 during the audit period for services related to capital projects; however the District did not adequately review the firm's invoices for accuracy prior to payment.

Oversight of External Auditor and Audited Financial Statements

Government auditing standards require auditors to be free from personal impairments to independence. The Board failed to ensure this because it permitted the auditor to prepare source documents, adjusting and closing journal entries, budget transfers, financial statements and the auditor was allowed sole discretion to make adjustments to the District's financial books and records. The District's long-time auditor/accountant resigned as auditor in 2005 and then limited her services to accounting thereafter, without a retainer agreement specifying the cost or services to be provided.

The District failed to issue 1099s as required by the IRS for payments made to the auditor and the attorney.

The audited financial statements contained misstatements as the District:

- did not account properly for life insurance policies by categorizing the premium as a General Unallocated Insurance cost, instead of as an employee life insurance cost under employee benefits; and
- understated the sale of materials and overstated the sale of services.

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District Acting as Vendor

The District required that new connections to its water system be made using supplies purchased from the District. The District also sold engineering services during the audit period. It is not clear that the District is authorized by law to act as a vendor of services. The District may only sell property as authorized by the Town and then it must turn over the receipts to the Town. Our review indicated that the District kept the income from its sales. The District recorded sales of \$7,031 in materials and \$42,125 in services to the public over the audit period.

We found inadequate internal controls over the sales. The Board did not approve the District's written price list for materials and services; require written contracts when substantial services were provided, or require the Superintendent to review and approve all bills before issuance.

Affiliation between the Westbury Water and Fire District

The audited financial statements of the Westbury Water District do not disclose the nature of its relationship with the Westbury Fire District. With no authority to audit Fire Districts, our ability to review transactions between the two districts was limited.

A State Comptroller opinion states that charge backs between a fire and water district run by a single board of commissioners under section 186(3) of the Town Law are not permitted. Our audit disclosed that the District charged back Westbury Fire District for services that were provided by the District. The amounts billed included: \$2,000 per month for undefined administrative costs; \$212.50 per month for legal fees; and \$75 per hour for mechanics to work on fire district vehicles.

Non-Compliance with Civil Service Reporting

The District is obligated to file payroll certifications annually to the Nassau County Civil Service Commission in accordance with New York State Civil Service Law §100. We found that three of the District's employees (including the Superintendent) were not listed on the Civil Service payroll certifications filed for 2004 or 2005.

Lack of Internal Controls

We found that the District operated with inadequate internal controls in the following areas:

- **Purchasing and Receiving** - There was an inadequate segregation of duties; the purchasing process was informal; purchase requisitions and receiving reports were not used; and purchase orders were rarely used. We also found that the

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- District did not always ensure that vouchers included claimant's certifications or that warrants were properly approved before payment. Payments claimed by commissioners or Superintendent were approved for payment even though the commissioners and Superintendent did not certify their own claims.
- Weak Internal Controls over Cash Receipts - We found that: checks received were not restrictively endorsed when the mail was opened; there was an inadequate segregation of duties; customers paying bills in person were not always issued pre-numbered receipts; and there were no controls over the inventory of pre-numbered cash receipt books.
 - Lack of Management Review of Original and Revised Customer Invoices - We found a lack of managerial oversight over the billing process to ensure accuracy of the original billing or rebilling to correct errors in meter readings.
 - Lack of Bank Reconciliations - The bank reconciliation for the operating account was inadequate as it was not prepared using a standardized format and was not signed, or dated, by the preparer nor reviewed by management. The District's money market and repair reserve accounts were not reconciled. The accounts had combined balances of \$1,864,117 and \$1,419,941 as of December 31, 2005 and 2004, respectively.
 - Inadequate Fixed Asset Controls - There were no controls in place, such as a reconciliation of acquisitions to the cash disbursement records, to ensure that all capital asset purchases were identified and capitalized in the financial statements. Weak controls over fixed assets may have resulted in the District incurring unnecessary insurance costs on one vehicle that was no longer in use.

The matters covered in this report have been discussed with officials of the District during this audit. On August 1, 2007, we submitted a draft report to the District with a request for comments. The District's comments, received on September 7, 2007, are included as an addendum to this report (Appendix I). It should be noted that, of the 16 audit findings detailed in this report, the District only responded to four.

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AUDIT FINDINGS AND RECOMMENDATIONS

Audit Finding (1):

Lack of Board Oversight

Inadequate Control of District Finances

We found that the Board did not meet its responsibility to control the District's finances. From a review of the Board minutes, we found that the Board did not:

- pass a resolution to adopt the budget. The Superintendent informed us that the Board reviewed the budget that he manually prepared and directed him to send it to the town for approval;
- review and approve or reject budget transfers during the fiscal year. Except for a transfer of \$200,000 in surplus funds into the Repair Reserve, the Board did not approve any of the budget transfers that were made during the audit period. The District's accountant, through a series of year end budget transfers, transferred money within the budget to those accounts that were under budgeted without evidence in the minutes of the commissioner's approval [See Audit Finding 7];
- monitor financial transactions by requiring periodic financial reports, such as a Treasurer's Report, to detail financial transactions and budget to actual variations, for review and approval at each board meeting; and
- assume any role in reviewing and approving the District's accounts. There was no evidence that the Treasurer performed any fiduciary oversight, other than to approve vouchers for payment and sign checks.

The annual budget is the basis for determining the tax levy and the amount that the District is authorized to spend. The Board did not accurately budget revenues and expenses. We determined that the District consistently over budgeted expense categories such as Source of Power, Supply and Pumping, Transmission and Distribution and Hospital and Medical Insurance, even though actual past spending showed it needed less money. The District also under budgeted revenues by not including known revenue sources, such as payments in lieu of taxes in the budget. This combined practice of over budgeting expenses and under budgeting revenues artificially inflated the tax levy paid by District residents.

The District's General Fund balance increased from \$1,629,363 to \$2,437,333 due to a surplus of \$807,970 during the audit period. In 2004 and 2005, the District transferred \$600,000 of the surplus to the repair reserve (in addition to the \$500,000 budgeted) and did not designate any purpose for the remaining \$207,970 surplus. Of the \$600,000 transferred, only \$200,000 was approved by the Board. The unbudgeted and unapproved movement of an additional \$400,000 to the reserve was not explained by an emergency that could not wait for a Board meeting. During the audit period, the District's repair reserve increased by \$1,145,124, but the District expended only \$569,568 from the reserve

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Lack of Policies and Procedures

The District's Board is responsible for establishing and ensuring compliance with a system of internal controls over operations. We found that the Board had not adopted written operating policies and procedures for functions such as:³

- cash disbursements
- cash receipts
- payroll
- time and leave
- travel, meetings and conferences
- educational expenses
- petty cash
- fixed assets
- system user procedures

We also found that the District lacked a formal code of ethics and a conflict of interest policy. While the District's policies "do not necessarily need to outline in specific detail each and every step of a particular transaction... [they] should provide guidance to help promote and maintain accountability."⁴

We also reviewed the Board minutes to obtain an understanding of the District's operations and the role of the Board. The minutes lacked detail with respect to discussions of District business and did not include matters that ordinarily appear in board minutes, such as annual salary increases, employee benefits and fees. The Superintendent informed us that he brought matters such as employee compensation and fees to be charged to the Board's attention, but there was no record in the minutes that these matters were discussed. [See Audit Finding 4] The lack of active board involvement contributed to a lax internal control environment and a lack of accountability. There was no clear evidence in the minutes that the Board took an active role in monitoring the District's operations and setting an authoritative "tone from the top."

Audit Recommendations:

The Board should:

- a) adopt the budget and approve budget transfers by resolution;
- b) require the Treasurer to provide and present periodic financial reports to the Board for its approval, including an explanation of variances between the actual and budgeted financials;

³ This was also the subject of a management comment by the District's external auditor in 2005.

⁴ A study of Cash Internal Control Practices for Local Governments in New York State, State of New York, Office of the State Comptroller, Division of Municipal Affairs, 2000-PS, pg. 4

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- c) prepare accurate budgets to ensure that the budget does not overstate the size of the tax levy necessary to perform District services;
- d) issue written policies for the operating, financial and systems procedures, including an operating manual describing how each job function is to be performed and how incompatible functions are segregated;
- e) establish internal controls and oversight over operations;
- f) adopt a written code of ethics and a conflict of interest policy that prohibits self-dealing and precludes favoritism; and
- g) include in the Board minutes matters brought to its attention by the Superintendent, and drafting resolutions to reflect key decisions and actions authorized by the Board.

Audit Finding (2):

Life Insurance Policies

No authority to purchase individual life insurance policies

The District purchased \$50,000 individual whole life insurance policies for each of its commissioners and all but one of its employees⁵ despite the fact that in 1993 it received an opinion from the Office of the New York State Comptroller (“OSC”) stating that the District did not have the authority to purchase life insurance policies because no statute authorized the District to purchase life insurance.⁶ We were informed by the Superintendent that the District relied on a contrary legal opinion provided by an attorney. The District did not follow up with the OSC to discuss the merits of its attorney’s opinion. The premiums incurred by the District to provide individual whole life insurance policies to its employees were \$18,702 in 2004 and \$23,597 in 2005. The cash surrender value of the policies as of December 31, 2005 was \$52,950.

After the date of the OSC opinion, a statute was enacted authorizing special districts to purchase group life insurance policies for their employees.⁷ With the change in law, the District would have been authorized to obtain group life insurance coverage. However, there is still no statutory authorization for the District’s practice of providing individual life insurance policies for employees and commissioners.

The District’s Employee Handbook (Handbook) states that the District will provide life insurance for employees. Employees, who remain with the District to age 65, and then retire, have the option of receiving the policy or its cash surrender value. According to the Handbook, the District is both the owner and the named beneficiary and receives the proceeds from the insurance company should the employee die while employed at the District. In that case, the Handbook states that \$45,000 of the proceeds is paid to the

⁵ One employee was deemed ineligible for life insurance by the insurance company.

⁶ See NYS Comptroller Opinion, File No. 0591147 (March 23, 1993).

⁷ See N.Y. Gen. Mun. L. § 93 (2007).

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decedent's estate and \$5,000 to the surviving spouse of the employee.

Since the District lacks the authority to provide individual life insurance policies to employees under the law, it also lacks the power to turn over ownership of District purchased life insurance policies to its employees upon retirement.

Failure to follow Employee Handbook provisions

The District did not comply with the terms of its Handbook concerning insurance. The Superintendent was provided coverage greater than provided in the Handbook. The Superintendent's initial \$50,000 policy was issued on August 28, 2002, and a second policy for the same level of coverage was issued nine days later with a premium cost of more than double the first policy. The District purchased a third policy for the Superintendent in 2004, bringing total coverage to \$150,000. There was no stated business purpose or evidence of Board approval for the second or third policies. While the third policy was cancelled in 2006, the Superintendent continued to be the only District employee with two life insurance policies for total coverage of \$100,000.

The District also did not consistently follow its Handbook's requirement that the District be the beneficiary for the life insurance policies. On four policies, the District named employees' family members as beneficiaries instead of the District. The four deviations were on policies for two of the three commissioners, the second policy for the Superintendent and a policy for an employee who is the son of a former commissioner. Additionally, we found another instance of inequitable treatment in that the one employee who was not insurable was not provided with an alternative benefit of equal value.

Conflict of Interest: Commissioner as Agent

A District Commissioner was the insurance agent of record on three of the insurance policies written through the Massachusetts Mutual Insurance Co. One of those three policies was the second policy purchased for the Superintendent. The commissioner should not have sold insurance policies to the District. General Municipal Law § 801 prohibits municipal officers, including special district commissioners, from having an interest in a contract with the local municipality for which he is an officer, where he has the power or duty to negotiate, prepare, authorize or approve the contract or payments.

Wasteful Practices in Purchasing Insurance

In 2004, the District replaced three existing individual life insurance policies with three new individual life insurance policies from a different insurance carrier, which resulted in higher premiums without any apparent increase in benefit. In addition, the District failed to immediately cancel two of the four policies that were replaced, resulting in duplicate coverage. This error was first discovered in 2006 as a result of the District responding to one of our audit requests and the District cancelled the two policies receiving the cash surrender value of \$3,901. The Superintendent was unable to provide a business purpose

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for the new policies, stating only that the District relies on the recommendations of its insurance broker.

Audit Recommendations:

The District should:

- a) terminate its individual policies in compliance with the Town Law. The District should consider different approaches to correcting this situation such as canceling the policies immediately or transferring the ownership and cost of each policy to the respective employee and obtaining the cash surrender value from the employee; and
- b) not transact business with Commissioners and should develop a conflict of interest policy consistent with GML §801 that prohibits its employees from conducting any transaction with or for the District that could give rise to even the appearance of a conflict of interest.

Audit Finding (3):

Commissioners' Pay and Benefits

Commissioners' Pay

During the audit period commissioners were compensated at a per diem rate of \$80 per day. The State Comptroller has opined that the per diem is due for each day "actually and necessarily spent in the service of the district."⁸ In order to be entitled to this compensation, the services rendered must not have been "wholly nominal and unsubstantial" or "trivial or inappreciable," in the words of the State Comptroller.

In 2005, the commissioners were paid for 573 days, an average of 191 days per commissioner -- almost four days every week. As shown in the table below, the combined earnings of the three commissioners were \$42,240 in 2004 and \$45,840 in 2005. Based on a review of the board minutes, we determined that the commissioners held 49 meetings in 2005, almost one a week, and commissioners were paid \$11,920 in 2004 and \$11,040 in 2005 for attendance at board meetings. The commissioners received \$30,320 in 2004 and \$34,800 in 2005 for other unspecified work on non-meeting dates.

⁸ N.Y. Op. State Comptroller 90-49 (1990); N.Y. Town Law §216 (2007). During the audit period the daily rate could not exceed \$80 per day. The statutory maximum has since been raised to \$100 per day.

AUDIT FINDINGS AND RECOMMENDATIONS

| | Per Diem Compensations Paid to Commissioners | | | | | | | | |
|----------------|---|---------------------------|-----------------|--------------------------|---------------------------|-----------------|---------------------------|---------------------------|-----------------|
| | <u>2004</u> | | | <u>2005</u> | | | <u>Audit Period Total</u> | | |
| | Number of Meetings | Number of Per Diems | Earnings | Number of Meetings | Number of Per Diems | Earnings | Number of Meetings | Number of Per Diems | Earnings |
| Board Meetings | 52 | 149 | \$11,920 | 49 | 138 | \$11,040 | 101 | 287 | \$22,960 |
| Other | | 379 | \$30,320 | | 435 | \$34,800 | | 814 | \$65,120 |
| Total | | <u>528</u> | <u>\$42,240</u> | | <u>573</u> | <u>\$45,840</u> | | <u>1101</u> | <u>\$88,080</u> |

The Board has not set forth any policies requiring board members to attest to time they work or to provide written descriptions of the District business they performed on the days when there were no board meetings. The District kept no records of the work done by the commissioners on dates when the Board did not meet; Commissioners would indicate that they had worked on water district business on a particular day by initialing a calendar maintained by the Superintendent. Thus, the appropriateness of per diem payments totaling \$65,120 during the audit period for days when there were no board meetings could not be determined.

Fire District Commissioners are prohibited by law from receiving any compensation for their service to the District.⁹ The Water District Commissioners also serve as Commissioners of the Fire District. We could not test compliance with this law because the District keeps no records concerning the nature of business transacted by the commissioners on the non-meeting days when they work. We note that the agenda of the weekly Water District board meetings included Westbury Fire District business. [See Audit Finding 9]

Commissioners' Retirement Reporting

The New York State and Local Retirement System ("NYSERS") requires that employers report the number of days actually worked.¹⁰ For elected officials, the governing board of a municipality is directed to establish a standard workday to be used as the basis for retirement system reporting; the officials' work day has to be at least six hours long. The District has not established a standard workday. Elected officials must keep a record for one month of hours worked each day and duties performed directly related to the position, which is used as the basis for reporting time worked. To determine the number of days reported, NYSERS prescribes taking the total number of hours worked by the elected official, based on the record of activities, and dividing that total by the standard work day that was established by board resolution.

The District reported to NYSERS that one commissioner worked 207 days in 2004 and 221 days in 2005, while another commissioner worked 169 days in 2004 and 176 days in 2005 to NYSERS for retirement credit purposes. In addition to working for the District,

⁹ Town Law §174(3) (2007). Only a commissioner acting as secretary of a fire district may be compensated.

¹⁰ New York State and Local Retirement System Employer's Guide. June 2004, p. 100.

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the two commissioners are self employed and spend part of their time conducting fire district business. Commissioners serve on an unpaid basis for the fire district and should not receive retirement credits for the time worked on fire district business. (The third commissioner is already a New York State retiree and his time is not reported.) The number of days worked reported to NYSERS could only be correct if the commissioners worked a minimum of six hours per day on water district business between three and four days a week throughout the year. We could not ensure that the District was correctly reporting time for commissioners because no record was maintained of their activities and the hours they worked during the course of the days reported.

Health Insurance for Commissioners

Pursuant to the District's Handbook, commissioners are offered fully paid health insurance or the option of a health insurance buyback. The commissioners each received the health insurance buyback of \$3,000 per year, totaling \$18,000 during the audit period.

Audit Recommendations:

We recommend that the Board:

- a) set standards that must be met in order for commissioners to receive per diem compensation. The standard should require that the commissioners maintain a contemporaneous record of the date, time and number of hours worked, as well as the nature of the work performed;
- b) require commissioners to sign in and out;
- c) perform a one month study of commissioner's work hours, excluding those hours worked on fire district business, and establish, through Board Resolution, a standard workday for elected officials;
- d) only report time to NYSERS consistent with NYSERS regulations; and
- e) consider terminating health insurance coverage and buy-back options for commissioners.

Audit Finding (4):

Employee Compensation

Lack of Authorization for Salaries

Personnel expenditures are the largest component of the District's budget, totaling \$956,710 in 2004 and \$1,101,313 in 2005, or 24% and 28% of operating expenses, respectively. An important element of internal control involves the approval process for salaries and salary increases to be paid to employees. This is particularly crucial for an employer where there is no collective bargaining agreement in place governing salaries and benefits.

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We found serious internal control weaknesses that allowed significant deviations from the salary review policy stated in the District's Handbook. The Handbook states that "each employee will be classified on an annual basis according to the District's salary progression schedule which takes into account job classification, performance, leadership, and judgment among other qualities to classify employees."¹¹

We found:

- Most salaries were not paid in accordance with the District's salary progression schedule. The schedule contained ten steps, based on the first ten years of employment. The District had many long term employees who received salaries that were beyond the highest salaries of the tenth step. There was no written basis or authorization for the salaries paid these employees. We also found that the District employed individuals in certain positions, such as a secretary and a treasurer, that were not included on the salary progression schedule.
- Although employees received raises in both 2004 and 2005, the Board minutes lacked any discussion of employee compensation for those years. In both 2004 and 2005, certain employees received salary increases in excess of the average increase without any documentation as to the rationale for the deviation from the average. The Superintendent received increases of 12.72% and 8.76% in 2004 and 2005, respectively. Four other employees received increases ranging from 5.82% to 8.9%, above the 3.5% to 4% typically given to other employees.
- Personnel folders lacked salary authorizations, as well as other information such as IRS form W-4, "Employee Withholding Allowance Certificates." This lack of documentation was the subject of a management comment by the District's 2005 external auditor issued on May 3, 2006, but was still unresolved as of the date of this audit.

Inadequate Time Records

Although the District invested in time clock equipment, and took the time to file and retain the timecards for one year, the Superintendent stated that he did not rely on them to record the payroll. We found that the only records supporting the payroll for the audit period were timesheet summaries prepared by the Superintendent. The District did not require employees to certify the time recorded on the summary.

The District had no procedures governing the use of time clocks. Of the District's 18 employees:

- one, the Superintendent, did not have a timecard or any other time record; and
- 17 had time cards; however two employees did not use them at all and the other

¹¹ Westbury Water and Fire District Employee Handbook , Subject 9, page 7.

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15 employees' use was inconsistent.

We also found one instance where two employees had identical salaries and titles; however, one used the time clock while the other did not.

We reviewed 68 timecards for the 17 employees for a four-week period in February 2006 and found that timecard use was haphazard and did not produce a record that could be relied upon for timekeeping purposes. We found that 50 of 68 cards reviewed had deficiencies, including:

- 10 instances of days where employees did not punch in;
- 50 instances of days where the employee did not punch out; and
- 6 instances where there was no time punched in or out on days for which the employees were paid.

We found that even when employees punched both in and out, the Superintendent's records differed from the time clock records.

- The overtime hours recorded by the field workers on their time clock cards were 22.4 hours less than the hours paid per the payroll in eight instances during our test month of February 2006.
- The Superintendent made adjustments in the week of February 19, 2006 to pay 10 employees for 203.5 hours overtime worked in previous weeks. We found that for all ten of these employees, the overtime for which they were paid could not be traced to their timecards.

As a result, employees may have been paid for regular time and overtime that was not worked. The lack of time records supporting the hours worked in the District is a serious weakness in internal control because it increases the risk that employees could be paid for undocumented time off.

We also found that the District destroyed the time clock records at the end of each year, a violation of the New York State Records Retention Regulations requiring such documents to be retained for six years.¹²

Overtime Practices

We found that there were inadequate controls over the authorization and reporting of overtime. The Superintendent advised us that the Foreman verbally informed him of the need for overtime. No written authorizations were obtained. While the Superintendent made a record of the reasons overtime was worked, he disposed of them after the pay cycle in which the employees were paid.

The District's lack of a procedure and approval process for overtime was the subject of a

¹² N.Y. Comp. R. & Regs. Tit. 8, § 185.14 (2007).

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comment in the external auditor's 2005 management letter. The District paid out \$129,331 in 2004 and \$159,585 in 2005 for overtime that cannot be audited for proper authorization and legitimate business purpose due to the failure to maintain overtime records.

The District's Handbook states that overtime pay applies to hours worked in excess of 40 hours per week for operations staff and 35 hours per week for administrative staff. The District did not comply with the policy outlined in the Handbook; overtime was paid based on the number of hours worked in a day, not a week. Three part-time administrative employees received overtime pay based on time worked in excess of their normal business day rather than the total hours worked weekly. The overtime payments erroneously paid to these three employees totaled \$2,775 in 2004 and \$4,196 in 2005. The Superintendent stated that he was not aware of the overtime policy outlined in the Handbook.

Mis-reporting part-time employees' time for pension purposes

The District reported two of three reduced schedule employees as full time to NYSERS, and did not pro-rate their hours worked for the District. A third reduced schedule employee was reported correctly. This practice results in certain employees receiving service credit towards their pension for time not worked.

Audit Recommendations:

The District should:

- a) ensure that all employees' attendance records are recorded using the timecard system;
- b) check all timecard records for completeness and accuracy prior to being submitted for payroll;
- c) base payrolls on the timecard records;
- d) modify the salary progression schedule to reflect the District's pay practices and require Board approval of the schedule;
- e) document the rationale for raises that do not conform to the District's salary progression schedule;
- f) take steps to ensure that salary and withholdings authorizations are documented and retained in employees' personnel folders;
- g) authorize and pay overtime in accordance with policies outlined in the Handbook;
- h) cease the practice of awarding overtime pay to administrative employees who work a reduced schedule unless they work more than 35 hours per week;
- i) correct the time reported to NYSERS; and
- j) retain all records for six years in accordance with New York State regulations regarding record retention.

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Audit Finding (5):

Personal Use of Business Vehicle

The District did not have a policy regarding the business and non-business use of District vehicles. The Superintendent acknowledged that he used the District's 2005 GMC Yukon, purchased new for \$45,000, for commuting, however, there was no Board resolution authorizing the use of the vehicle for commutation or personal travel. He was the only employee who took a car home. The District imputed a taxable value of \$720 for this benefit in reporting the Superintendent's taxable income on his 2005 W-2 form. It did not impute income for 2004, although it should have.

We reviewed the mileage on the Superintendent's vehicle and found that he drove over 11,000 miles in the first six months of ownership. The District is only 5 square miles, and the Superintendent lives .81 miles from the District headquarters. We find it extremely unlikely that business use and commutation could account for the number of miles accumulated. There was no evidence that the Superintendent was authorized to use the car for personal purposes and that he reimbursed the District for any personal use.

Audit Recommendations:

The Board should:

- a) resolve whether District employees are allowed to commute in District vehicles, and if so, which employees are granted the privilege;
- b) establish a vehicle use policy covering appropriate use of the vehicles and for reimbursement to the District if personal use is permitted;
- c) require the Superintendent to reimburse the District, or the District should impute income, for all non-business use of the vehicle; and
- d) correct the report to the IRS of the value of the use of the vehicle to the Superintendent to reflect the mileage used for personal reasons.

Audit Finding (6):

Non Compliance with General Municipal Law §103 and District Procurement Policy

Procurement of Goods

General Municipal Law §103 requires that items purchased for more than \$10,000, or where more than \$10,000 of an item is likely to be purchased in a year, be procured through sealed competitive bids. GML §104-b requires that the District promulgate procedures governing procurement not subject to the bidding requirements of §103. The District's procurement policy requires:

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- two written price quotes for purchases of goods between \$1,000 and \$2,500; and
- three written quotes for purchases between \$2,500 and \$9,999

We found that the District did not comply with GML §103 because purchases were routinely made without soliciting quotes or bids from vendors. The District made purchases of similar items aggregating more than \$10,000 per year from single vendors that should have been bid, but were not. Examples of these purchases included caustic soda (\$22,005 in 2005 and \$66,162 in 2004), water meter parts (\$83,246 in 2005 and \$65,162 in 2004), water testing (\$29,519 in 2005 and \$51,746 in 2004) and asphalt paving repairs (\$34,050 in 2005). Included in the purchase of water meter parts were three individual purchases of greater than \$10,000.

We also reviewed ten purchases under \$10,000 and found no evidence that the District sought other price quotes as required by its procurement policy.

Procurement of Services

The District's procurement policy states that "the following shall not require the soliciting of alternate proposals (a) Contracts or proposals for technical services, including but not limited to architecture, medical, legal and engineering, it being the opinion of the Board that because of the nature of these professional services and skills, the best interest of the Districts would not be served by employing the lowest bidder. (b) Services requiring special skills and knowledge (computer programming, artistic, consulting, training, public relations, finance)."

We disagree with this policy. The District used the same engineering firm, lawyer and accountant for at least 15 years without engaging in a competitive procurement process to evaluate whether other firms would have provided better or more cost effective services. Because the District has not given other professional firms the opportunity to compete for its business, the District cannot know whether it is obtaining the best possible price or the highest possible quality of work from its engineer, lawyer or accountant.

Attorney

The District paid its attorney \$20,000 each year for undefined legal services without a written agreement as to what services the fee covered as is required by New York's Judiciary Rules.¹³ Because there was no engagement letter, no bills specifying the work that was done, and no reference in the minutes of matters referred to the attorney, it was unclear what legal services were performed to earn this fee.

In addition to the \$20,000, the attorney was paid \$7,685 during the audit period to review

¹³ See N.Y. Codes R. & Regs. Art. 22, §1215.1 (2007) requiring that attorneys provide clients with a written letter of engagement describing the legal services to be provided and the fees to be charged.

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claim vouchers submitted by the District to the Town of North Hempstead for payments from capital funds. The Town Comptroller advised us that the Town's claims processing procedure does not require review by the District's attorney, and we found no business purpose for outside counsel to be paid for such a review.

Engineering

The District contracted with Dvirka and Bartilucci ("D&B") for engineering services. The District retained D&B for \$4,000 annually pursuant to a retainer agreement which provided that a representative of the firm must attend periodic meetings of the Board. The firm was paid a total of \$300,000 (inclusive of the retainer amount) during the audit period.

The District did not adequately review D&B's invoices for accuracy. D&B billed the District for services based upon the hourly salary of each employee assigned to the job and a markup multiplier. However, the District did not maintain a list of engineering personnel and their hourly rates to confirm that the charges were appropriate.

From our interviews we learned that all construction or repair projects undertaken by the District were based on the recommendation of the Superintendent after consulting with D&B. Once the Board approved a project, D&B prepared the bid specification documents, assisted the District in determining the lowest responsible bidder, performed engineering work related to the project and supervised the project. Thus, D&B advised the District as to whether engineering work was needed and earned substantial fees by working on those projects the Board decided to undertake. This created a potential conflict of interest because D&B had a substantial economic interest in the advice it gave the District concerning construction or repair projects.

Insurance

The District spent \$114,168 in 2005 and \$91,264 in 2004 on liability insurance. We found no evidence that the District requested proposals from brokers or solicited bids on insurance policies before choosing a broker and purchasing insurance.

Audit Recommendations:

- a) The District should:
 1. comply with GML §103 and its own procurement policy by obtaining bids for purchases over, or for items aggregating over, \$10,000 and quotes for purchases over \$2,500;
 2. request proposals for insurance broker services and obtain bids for liability insurance;
 3. request proposals for all professional services on an annual or other routine basis;

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4. adopt a policy requiring annual retainer agreements from each provider of professional services;
 5. reconsider its practice of having its outside counsel review claim vouchers prior to submission to the town for payment and determine whether the review is necessary and the expense is justified; and
 6. obtain up-to-date lists of engineering personnel and their hourly rates and verify that the District is being billed correctly.
- b) The District needs to ensure that the engineering recommendations are prudent and necessary, and avoid contractual relationships that give rise to potential conflicts of interest and the appearance of impropriety.
- c) The District should:
1. separate the function of engineering advisor and engineer performing the recommended work. The District, for example, might hire an engineering firm to serve exclusively as an advisor on the need for repair or construction work and separately procure an engineer to perform the work; and
 2. competitively procure engineering services consistent with the requirements of the General Municipal Law. The District should consider procuring engineering services for repair and construction on a project by project basis, rather than giving one firm an annual contract to do all engineering work in the District.

Audit Finding (7):

Oversight of External Auditor and Audited Financial Statements

Government auditing standards require auditors participating in audit assignments to be free from personal impairments to independence.¹⁴ The District relied on its accountant, (who was also the auditor for 2004) for the preparation of the 2004 financial statements and supporting schedules. The Board failed to ensure the auditor's independence because it permitted the auditor to prepare source documents, adjusting and closing journal entries, budget transfers, and financial statements. In addition, there was no evidence of Board oversight or any review and approval of transactions by District management. The auditor had sole discretion to make adjustments to the financial books and records of the District. [See Audit Finding 1]

The auditor, acting also as the accountant, maintained custody of the District accounting records away from District premises without leaving back up copies on site. The records were not available at the District at the time of our audit and had to be brought to the

¹⁴ United States Government Accountability Office Government Auditing Standards, Chapter 3.07 (Jan. 2007).

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District for our review.

The District's long-time auditor/ accountant (former auditor) resigned from her position in 2005 and limited her services to accounting services. The District then engaged a separate CPA firm to perform the audit. However, it did not enter into a retainer agreement with the accountant (former auditor) to specify what services were to be provided or the cost of these services. The lack of Board oversight over the work of the former auditor continued as of the date of this report.

The audited financial statements contained misstatements:

- The District did not account properly for life insurance policies. The District categorized the premium cost as a General Unallocated Insurance cost, instead of employee life insurance cost under employee benefits. Additionally, the cash surrender value was not recorded on the Balance Sheet. The premiums incurred by the District to provide individual life insurance policies to its employees were \$18,702 in 2004 and \$23,597 in 2005. The cash surrender value of the policies as of December 31, 2005 was \$52,950.
- The District's financial statements understated the sale of materials and overstated the sale of services. We reviewed eight bills and noted that \$8,518 in materials were sold, however, \$6,642 of this was incorrectly posted to the service revenue account in the general ledger. [See Audit Finding 8]
- Prior to 2005, the District relied on its former auditor to determine when the issuance of a 1099 was required. We were advised by District staff that a 1099 was not issued to the former auditor prior to 2005 or to one of its law firms for 2005 even though each was paid in excess of \$600 for those years. The Internal Revenue Service (IRS) requires entities to file a Form 1099-MISC (a "1099") for each person to whom it has paid at least \$600 for services.

Audit Recommendations:

The District should ensure that:

- a) the District's Chief Financial Officer approves all journal entries and prepares the financial statements;
- b) the Board approves any budget transfers;
- c) revenue from sales is posted to the correct accounts in the general ledger;
- d) all assets are recognized in the financial statements;
- e) it complies with IRS regulations and issues 1099s for all individuals paid \$600 or more for services in a year. With respect to 1099s that were not filed for prior years, the District should take the necessary steps to file the forms with the IRS; and
- f) back-up copies are maintained in the District offices of all financial records maintained by the accountant or auditor.

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Audit Finding (8):

District Acting as Vendor

Sales Proceeds

The District requires that new connections to its water system be made using supplies purchased from the District.¹⁵ The District also sold engineering services during the audit period. It is not clear that the District is authorized by law to act as a vendor of parts and services. The District may only sell property as authorized by the Town, and there is no statutory authorization for the District to sell services beyond the authority to prescribe how water connections will be made.¹⁶ Moreover, according to the law, when the District sells property, the receipts should be paid to the Town, not the District.¹⁷ Our review indicated that the District received and kept the income from its sales.

Inadequate Controls over Billings for Sales and Services

The District recorded sales of \$7,031 in materials and \$42,125 in services to the public over the audit period. The Board did not:

- approve the written price list for materials and services the District provides;
- require written contracts with customers when substantial services were provided. We found that the District billed a contractor \$10,000 for engineering services without a contract to define the services provided or the fee. The handwritten bill did not include any backup detailing who performed the service or any description of the work performed;
- require the use of pre-numbered invoices to help ensure that all revenues are accounted for; and
- require the Superintendent to review and approve all bills before issuance. The Superintendent stated that applications for water service were pre-approved and that he verified that the customer purchased proper materials for the service from the District. However, we identified a bill that had not been approved and noted that other bills contained a signature stamp used to evidence the Superintendent's approval, making it unclear if the Superintendent had actually performed his review.

¹⁵ While the Town Law authorizes the District to prescribe how water connections are made, Town Law §§ 201, 215(15), the statute does not appear to authorize the District to become the exclusive vendor of equipment used to connect to the system. The District should review this practice with the Attorney General and, in addition, review whether federal and state anti-trust requirements apply to its requirement that it be the exclusive vendor of supplies used for water connections.

¹⁶ Town Law §§ 201, 215(8)

¹⁷ Town Law §215(8)

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Audit Recommendations:

1. The Board should review whether it has the statutory authority to sell goods and services, to retain the money it receives rather than giving it to the Town and to require that connections to the water system be made only with parts it sells.
2. Assuming the District is authorized to sell equipment and services and keep the receipts, it should improve its control over billing and cash receipts. The District should:
 - a) approve by resolution all fees and price lists for services rendered and materials sold by the District to third parties;
 - b) require written contracts to document services to be performed and fees to be charged;
 - c) establish written procedures to ensure that all bills for materials and services are reviewed and approved by the Superintendent; and
 - d) require pre-numbered billing forms to be used and accounted for.

Audit Finding (9):

Affiliation between the Westbury Water and Fire District

Financial Statements

The Westbury Water District shares its Board of Commissioners with, and performs the financial and administrative functions of the Westbury Fire District. Each District currently issues its own set of audited financial statements. We found that the audited financial statements of the Westbury Water District do not disclose the nature of its relationship with the Westbury Fire District, potentially misleading a reader of the financial statements to believe that the two districts are independent of one another.

Our ability to review the appropriateness of the transactions that occurred between the Water and Fire districts and the accuracy of how the Water District identified and recorded these interactions on separate general ledgers was limited because we do not have the authority to audit Fire Districts. Although the financial statements and the supporting records of the Westbury Fire District were under the direct control of the same Board and Superintendent, we were not permitted access to them.

Allocation of Expenses to Westbury Fire District

Our audit disclosed that the Westbury Water District billed the Westbury Fire District for services that were provided by the Water District. The amounts billed included:

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- \$2,000 per month for undefined administrative costs;
- \$212.50 per month for legal fees;
- \$75 per hour for mechanics to work on fire district vehicles; and
- work done by the Plants and Grounds crews.

A State Comptroller opinion states that charge backs between a fire and water district that is run by a single board of commissioners under section 186(3) of the Town Law are not permitted. Specifically, the opinion explains:

there is no provision of law which authorizes the Water District to charge the Fire District for these or any other clerical or administrative services. Accordingly, it is our opinion that no such chargeback may be made. Indeed, since the tax base is the same, such a chargeback would serve no substantive purpose other than to reduce the amount needed to be raised by the Water District and increase the amount to be raised by the Fire District by an identical amount. However, the taxpayers of the District would still be paying the same total amount for fire and water service.¹⁸

Further, the charges were not supported by labor analysis. The Superintendent acknowledged that these charges have not been reviewed for reasonableness during his tenure, which began in 2002 and could not provide any documentation to show when these charges were last examined.

Audit Recommendations:

The District should:

- a) disclose the relationship between the District and the Westbury Fire District in the financial statements, including the services each district performs for the other and value of the services provided;
- b) consult with the State Comptroller to determine if it is permissible to prepare and issue consolidated financial statements for the “Westbury Water and Fire District” to provide transparency with respect to their relationship to one another and the transactions impacting their budgets, budget transfers, actual spending and fund balances;
- c) terminate the practice of allocating expenses back to the Westbury Fire District; and;
- d) require the attorney to bill the two districts separately.

¹⁸ Opinion of the New York State Comptroller, 1981 N.Y. St. Comp. 204.

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Audit Finding (10):

Purchasing and Receiving

The District did not establish controls to ensure that purchases represented necessary business expenses and that the goods received were the goods ordered. The District's purchasing process was informal, purchase requisitions and receiving reports were not used, and purchase orders were rarely used. Instead:

- verbal purchase requests were communicated to the Superintendent by the foreman or office staff;
- the Superintendent determined the vendor;
- the foreman or office workers placed the orders by phone or fax;
- the goods were received by the same individuals who placed the orders; and
- there was no comparison of goods received to vendor invoices and purchase orders to ensure that the goods received were the type and quantity ordered.

There was an inadequate segregation of duties because the foreman placed orders, received goods and the vendor's invoices.

Audit Recommendations:

The District should:

- a) ensure that the functions of placing orders, receiving goods and reviewing vendor invoices for payment are adequately segregated;
- b) document and control the purchasing and receiving functions by using purchase orders and receiving reports;
- c) compare the receiving reports to the approved purchase orders and requisitions to ensure that all goods ordered are received; and
- d) ensure that invoices are properly supported by an approved purchase order, receiving report and bill of lading prior to submission to the board for approval;

Audit Finding (11):

Approval of Payment Warrants

The District did not comply with its own procedure, which requires that vendors certify that services were rendered or goods provided and that warrants were approved by at least two commissioners before invoices were paid.

We found that the commissioners signed warrants approving the payment of vouchers totaling approximately \$3.9 million during the audit period. We judgmentally selected and tested 53 of these vouchers, totaling \$537,523, and found that 37 were not certified by the claimant, many of which were submitted by the commissioners and

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Superintendent for payment to themselves.

We reviewed 62 warrants from a population of 102 warrants approved during the audit period and found that two warrants, totaling \$70,754, were approved by only one of the three commissioners.

Audit Recommendations:

The District should:

- a) require vendor certifications on all vouchers prior to approval of warrants; and
- b) require approval by at least two commissioners of warrants prior to payment.

Audit Finding (12):

Weak Internal Controls over Cash Receipts

During our review of the cash receipts process we found that the District could not be assured that all cash receipts were deposited or had been properly posted to customer accounts. Weaknesses included:

- checks received by mail were not restrictively endorsed when the mail was opened;
- incoming receipts were not listed by the employee opening the mail for comparison against bank deposit;
- the two employees who opened the mail also posted the customer payments to the billing system;
- customers paying bills in person were not always issued pre-numbered receipts; and
- there were no controls over the inventory of pre-numbered cash receipt books, such as a log accounting for the numerical sequence of used and unused receipts.

Audit Recommendations:

The District should:

- a) require the checks be restrictively endorsed when the mail is opened;
- b) ensure that the employee who records cash receipts is different than the employee who lists the incoming checks and that the total listed is compared to the deposit amount; and
- c) establish controls over the receipt books and require that a pre-numbered receipt be issued for all cash and checks received at the District's public counter.

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Audit Finding (13):

Lack of Management Review of Original and Revised Customer Invoices

We found a lack of managerial oversight over the billing process to ensure that all customers are accurately billed. The Superintendent did not review:

- procedures performed by the billing clerk, such as comparing counts of meters read to the number of meter readings input, to ensure that the information input into the billing system was accurate;
- billing corrections made as a result of reviews of extraordinarily high or low usages to ensure that the meter readings were accurate; and
- reconciliations which evidence that the number of bills produced agreed to the number of accounts in the billing cycle.

In addition, the District periodically had to re-issue bills, primarily to correct errors in meter readings detected after the bill had been issued. For example, there were several large dollar value adjustments made due to undetected leaks and erroneous meter readings. In those cases, the District used a five year average bill as a basis for issuing billing adjustments. These adjustments resulted in reductions to customer bills totaling approximately \$164,000 during the audit period. We found that:

- there was no evidence that the Superintendent reviewed and approved these adjustments and revised bills prior to their being issued;
- there is no written policy controlling the process of issuing revised bills; and
- the documentation for the revised meter readings supporting the revised bills were retained for one billing cycle, if at all, and not the six years required by the New York State Records Retention guidelines.¹⁹

Audit Recommendations:

The District should:

- a) review the reconciliations prepared by the billing clerk to ensure that:
 1. meter readings are accurately input into the system;
 2. bills are produced for every account in each billing cycle; and
 3. bills properly reflect the amounts due from each customer;
- b) adopt a written policy to be followed as to when it is appropriate to reduce a customer's bill and the supporting documentation required;
- c) require the Superintendent's review and approval of corrected bills prior to

¹⁹ N.Y. Comp. Codes. R. & Regs. Tit. 8, § 12.[210] (Schedule MI-1, Appx. K) (2007).

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- mailing to the customer; and
- d) retain documentation supporting billing corrections in the customer's files for six years as required by New York State records retention guidelines.²⁰

Audit Finding (14):

Lack of Bank Reconciliations and Lack of Controls over Check Stock

The District had three bank accounts: general operating, repair reserve and a money market account. There were frequent transfers between the general operating account and the money market account.

We found that the District did not prepare bank reconciliations for the money market and repair reserve accounts. The bank reconciliation for the general operating account was prepared informally on an adding machine tape and was not signed and dated by the preparer or reviewed by management, although it was reviewed by the District's accountant.

In addition, the District:

- did not have any controls in place over its check stock, such as a log of used, unused or voided checks; and
- did not retain all voided checks. The District could not locate three of 37 voided checks.

Audit Recommendations:

The District should:

- a) prepare formal bank reconciliations for all accounts using a standard bank reconciliation format;
- b) require the preparer to sign and date the reconciliations;
- c) require a manager to review and approve the reconciliations;
- d) require an employee independent of the check preparation process to maintain a log of unused, used and voided checks; and
- e) retain all voided checks.

Audit Finding (15):

Inadequate Fixed Asset Controls

The District contracted with an outside appraisal firm to prepare a report that included the original and carrying value of all capital assets. This report was used by the District to

²⁰ *Id.*

AUDIT FINDINGS AND RECOMMENDATIONS

capitalize assets for financial statement presentation.

The appraiser prepared the report from a manual list of purchases and deletions for items over \$1,000 maintained by the Superintendent. However there was no control in place, such as a reconciliation of acquisitions to the cash disbursement records, to ensure that all capital asset purchases were identified and capitalized in the financial statements.

We found a deficiency in the District's reporting for capital assets in that seven assets purchased by the District with a total value of \$25,590 were not included in the capital assets report.

We also found that the weak controls over fixed assets may have resulted in the District incurring unnecessary insurance costs. A non-operational vehicle was insured by the District at a cost of approximately \$1,400 annually.

There were also internal control weaknesses over the deletion of fixed assets because the Board did not approve the disposal of three assets with a total original cost valuation of \$16,450. Although the assets were fully depreciated the Board should approve the disposition of assets. The lack of Board oversight increases the risk that assets may be disposed of without authorization and that the District may not be receiving the fair market value of the asset disposed.

Audit Recommendations:

The Board should establish procedures to:

- a) identify all assets purchased that are eligible for capitalization and reconcile to the cash disbursements records;
- b) approve all planned asset dispositions, including the expected proceeds, if any, from the disposition; and
- c) ensure that assets that are no longer in use are removed from District's insurance policies in a timely manner.

Audit Finding (16):

Non-Compliance with Civil Service Reporting

The District is obligated to file payroll certifications annually to the Nassau County Civil Service Commission in accordance with New York State Civil Service Law §100. We found that three of the District's employees (including the Superintendent) were not listed on the Civil Service payroll certifications filed for 2004 or 2005.

Audit Recommendations:

The District should comply with New York State Civil Service Law and file complete

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payroll certifications with the Civil Service Commission.

APPENDIX

DISTRICT'S RESPONSE AND AUDITOR'S FOLLOW-UP

Pursuant to your letter of August 1, 2007, attached please find our responses to your audit findings and recommendations:

Audit Finding (1) – Lack of Board Oversight – Inadequate Control of District Finances

“The Board did not accurately budget revenues and expenses”...“...under budgeted revenues by not including known revenue sources, such as payments in lieu of taxes ...”

The 2004 budget includes \$210,000 budgeted for Unclassified Revenue sources – this includes the 2004 PILOT revenues of \$41,968 and hydrant rentals of \$47,400 as well as other miscellaneous revenues that the District may receive.

The 2005 budget includes \$265,000 budgeted for Unclassified Revenue sources – this includes the 2005 PILOT revenues of \$49,974 and hydrant rentals of \$47,400 as well as other miscellaneous revenues that the District may receive.

“...the District consistently over budgeted expense categories such as Source of Power, Supply and Pumping, Transmission and Distribution and Hospital and Medical Insurance...”

The budget category Source of Power, Supply and Pumping pertains to the operations and maintenance of the wells, pumps and plants that supply water to the consumers of the District. Repairs and maintenance and improvements are budgeted each year to allow funds to be available for repair and improvement projects, if needed. These projects cannot always be anticipated in advance, tend to be costly, usually have to be done immediately and pertain to the health and safety of the consumers of the District. If these funds are not utilized or encumbered during the year, the excess is transferred to the Repair Reserve Fund to be utilized for projects or major repairs when needed in the future.

The budget category Transmission and Distribution pertains to the operations and maintenance of meters, mains, valves and hydrants in the District. During 2004, anticipated budget expenditures were not expended for personal services (did not hire anticipated employee), operating equipment and meters (did not purchase anticipated equipment). During 2005, the original budget for this category was \$821,011 and the actual expenditures were \$807,781 showing an unexpended budget of \$13,230 or 1.6%.

The budget category for Hospital and Medical Insurance includes allowances for family hospitalization policies for employees who, at the time of budget, are choosing not to participate in the District's hospitalization plan and are offered an alternative buyback payment from the District in lieu of coverage. Since this buyback payment is much less costly to the District

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(\$3,000 per employee per annum for five employees) and the employee has the option at the beginning of each new year to participate in the District's hospitalization plan, there is extra money budgeted in the category.

Auditor's Follow-up Response:

We stand by our finding. A two year surplus of \$807,970 as compared to a budgeted surplus of \$250,000 demonstrates that the Board has not budgeted accurately.

With regard to health insurance, we recommend that the District survey its employees annually as to whether they will take the buy-back for the following year so that it can accurately budget for health insurance costs.

The District's response states that PILOT payments were included in planned revenues. Our audit comment was based a list of revenues provided by the Superintendent. He told us that the list, which did not include PILOT revenues, had been used as a basis for the budgeted Unclassified Revenue. The District's uncertainty as to the components of its budget further illustrates the need for a formalized budget approval process to ensure accuracy.

“The District transferred \$600,000 of the surplus to the repair reserve and did not designate any purpose for the remaining \$322,541 surplus.”²¹

Because of the method that Nassau County uses to collect the tax levy on a semi-annual basis and the forty day grace period granted to the mortgage holders and residents, in order for the District to meet cash flow needs, the District needs to carry over general fund surplus each year to operate. Since the District's fiscal year starts January 1st and a large portion of their revenue (over 50%) is derived from the tax levy of which the first half is not received from the Town until two months later, the District requires a carryover fund balance each year to meet their payroll and pay their bills currently. In addition, because the majority of the water revenue from metered water sales is billed to consumers in the fall, after the summer watering season, and expenses are heavy during the watering season (especially LIPA to power the wells), the District needs general fund balance to operate efficiently. The second half of the tax levy is also not received from the Town until two months after July 1st, which begins the District's second half of the fiscal year.

Auditor's Follow-up Response:

Tax revenues are collected and disbursed by the Town of North Hempstead's Receiver of Taxes,

²¹ The draft report sent to the District for comment showed \$322,541 as the undesignated portion of the District's two year surplus. That amount was derived from the Town of North Hempstead Annual Budget's disclosure of the District's actual results for 2004 and 2005. The final audit report was revised to reflect an amount of \$207,970 derived from the District's 2004 and 2005 audited financial statements.

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not by Nassau County.

As of year end 2005, the District had \$2,437,333 in its general fund, an amount more than ample to meet short term funding needs. The District, however, may have created liquidity issues by permitting unapproved transfers to restricted portions of the general fund. The District had \$1,864,117 of cash on hand of which \$1,664,562 was restricted for the purposes of repairs and inventory. This left cash balances of only \$199,555 available to fund operating expense and current liability payments. The Board should have required its approval before restrictions were placed on general fund balances and should consider cash flow needs in determining appropriate levels of reserved fund balances.

The District's response does not address our findings that the Board did not:

- adopt the budget; review and approve or reject budget transfers, monitor financial transaction, or require the Treasurer to provide periodic financial reports;*
- establish policies and procedures for essential functions;*
- establish a written code of ethics and a conflict of interest policy;*
- expand its Board minutes to include all significant matters discussed and/or resolved;*

We reiterate our recommendations with regard to these findings.

Audit Finding (2) – Life Insurance Policies

The District did not have any response to this finding.

Audit Finding (3) – Commissioner's Pay and Benefits

The Board is very much aware of the law concerning the prohibition of Fire District Commissioner's receiving any compensation. Per Diem compensation applied for by the Board is solely for Water District business.

Auditor's Follow-up Response:

While the District maintains that the commissioners are compensated for Water District business only, the District did not have any documentation to support this statement. Commissioners have claimed reimbursement for approximately 3 ½ days a week spent on Water District business throughout the year. The need to keep records is even greater when the same Commissioners are presumably spending an equivalent amount of time on non-payable Fire Commission business. In addition, two of the three Commissioners were self employed during the audit period.

The District's response does not address our finding that the Board has not established any policies requiring Board members to attest to their time worked or that a record be maintained of the work done on days when the Board did not meet.

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The District's response does not address our recommendations that it:

- *comply with NYSEERS regulations and establish a standard workday to be used as a basis for commissioners retirement reporting; and*
- *consider terminating health insurance coverage and buy-back options for commissioners.*

Audit Finding (4) – Employee Compensation

The District did not have any response to this finding.

Audit Finding (5) – Personal Use of Business Vehicles

The District did not have any response to this finding.

Audit Finding (6) – Non Compliance with General Municipal Law 103 and District Procurement Policy

Procurement of Goods

The District purchased water meters through May of 2004 under a public bid awarded in 2001. The vendor held the bid price on all meters until a new bid was awarded in February 2006.

Auditor's Follow-up-Response:

The contention that the vendor held the price on water meters after the contract expired is not an indication that the District received the best price after May 2004. It should have re-bid the contract upon the expiration of the previous contract.

Due to a volatile market and the lack of a New York State Contract, the District was forced to purchase caustic soda for a period of time on the spot market. The District did, however, award a public bid for caustic soda in February 2006.

Auditor's Follow-up-Response:

We found no evidence that the District requested bids for caustic soda during the audit period and that vendors did not respond.

Asphalt paving repairs were the direct result of an unusually large amount of water main breaks that required immediate repair without adequate time to publicly bid the work.

Auditor's Follow-up-Response:

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We recommend that the District bid out a requirements contract for asphalt paving. A requirements contract would benefit the District by locking in a price and having a paving company available on demand.

It is our belief that lab services for the testing of water, as a professional service, do not require public bidding.

Auditor's Follow-up-Response:

Whether required or not, the District should engage in a competitive procurement process for services. As long as there are multiple vendors who provide the same services meeting testing standards, the District should use a competitive procurement process to ensure that it is obtaining the lowest price.

Procurement of Services

We believe that our present hiring practices comply with the appropriate sections of New York State Law. We will review our procedures with regard to the obtaining of and the content of retainer agreements.

Auditor's Follow-up-Response:

We reiterate our recommendation that the District request proposals for all professional services on an annual or other routine basis. Without this practice, the District cannot be assured that it is receiving the best possible service at the lowest price.

The District's response did not address our recommendation that it reconsider its practice of having its outside counsel review claim vouchers submitted to the Town of North Hempstead for payment from capital funds.

Insurance

The District's long time insurance broker retired in 1998 and not during the audit period as stated in the report. At the June 17, 1998 meeting of the Board of Commissioners, the Board reviewed a proposal by Carbone & Molloy Insurance and determined that the premium costs would be cheaper and in the best interest of the District.

Auditor's Follow-up-Response:

The report was corrected to delete references to the prior broker's retirement. The Board's review of one proposal in 1998 does not provide a basis of comparison to conclude that the

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District is obtaining the best price for insurance today.

We reiterate our recommendation that the District engage in a competitive procurement practice for insurance.

Audit Finding (7) – Oversight of External Auditor and Audited Financial Statements

During 2004, the amount of the accounting work done by the former auditor was de minimis. All proposed journal entry adjustments were reviewed and approved by management and then given to the account clerk to record on the books and records, which are maintained by the District on their computer system. The accountant did not retain custody of any of the District's accounting records, but did retain her original work papers.

Auditor's Follow-up-Response:

We found no evidence of review and approval of journal entries by District management. When we requested District accounting records, such as year end adjusting entries, GASB 34 fixed asset work papers and budget transfers, the accountant had to bring them to the District from her office.

Sales of materials and services by the District are recorded in the general ledger under one budget category "Water Service Charges". Even though, as stated in the report, \$6,642 of materials may have been incorrectly posted to service revenues, there is no effect on the audit report.

Auditor's Follow-up-Response:

We reiterate our recommendation that the District properly classify transactions in its general ledger in accordance with the District's chart of accounts.

The District's response did not address our recommendations that it properly account for the life insurance policies and that it comply with IRS regulations with regard to the issuance of Forms 1099-MISC to its auditors and law firm.

Audit Finding (8) – District Acting as Vendor

The District did not have any response to this finding.

Audit Finding (9) – Affiliation between the Westbury Water and Fire District

The District did not have any response to this finding.

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Audit Finding (10) – Purchasing and Receiving

The District did not have any response to this finding.

Audit Finding (11) – Approval of Payment Warrants

The District did not have any response to this finding.

Audit Finding (12) – Weak Internal Controls over Cash Receipts

The District did not have any response to this finding.

Audit Finding (13) – Lack of Management Review of Original and Revised Customer Invoices

The District did not have any response to this finding.

Audit Finding (14) – Lack of Bank Reconciliations and Lack of Controls over Check Stock

The District did not have any response to this finding.

Audit Finding (15) – Inadequate Fixed Asset Controls

The District did not have any response to this finding.

Audit Finding (16) – Non-Compliance with Civil Service Reporting

The District did not have any response to this finding.

We will continue to review our operation in light of your findings and recommendations and will make appropriate modifications or changes where necessary as circumstances and events dictate.

We sincerely appreciate your consideration in this matter.