

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



**Limited Financial Review
of the
Town of Hempstead
Department of Water
and the
East Meadow Water District**

HOWARD S. WEITZMAN

Comptroller

October 17, 2007

NASSAU COUNTY
OFFICE OF THE COMPTROLLER

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EXECUTIVE SUMMARY

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 of the districts 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 taxes² and charges for water, generally based on the gallons used as measured by water meters.

The East Meadow Water District (the "district" or "East Meadow") is run by the Town of Hempstead (the "Town"), not by elected commissioners. The district is one of six component taxing jurisdictions that comprise the Town of Hempstead's Department of Water (the "department").³ Operations of the Town water department are overseen by one Commissioner who is appointed by the Town Board. Resolutions pertaining to any or all six of the component districts of the Town water department are brought before the Town Board. The employees of the Town water department work for all six component districts. Billing and collections for metered water sales is done by the Town water department for each district. The administrative and financial operations of the Town water department are managed by the Town Comptroller's Office.

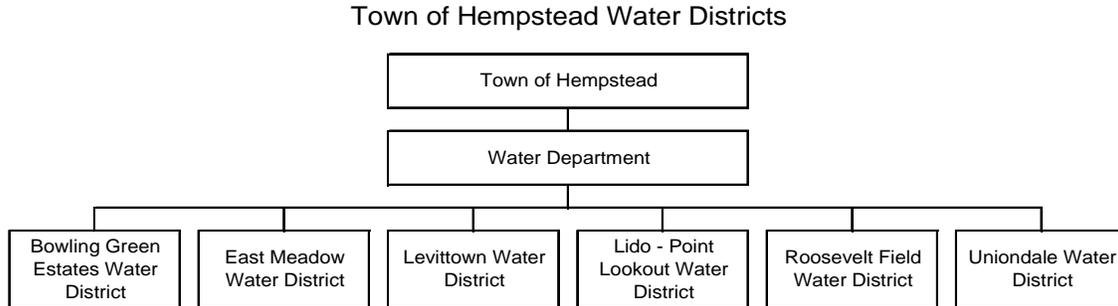
¹ *Nassau County Special Districts: The Case for Reform* (Dec. 19, 2005), www.co.nassau.ny.us/comptroller/auditreports.html

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

² Town Law § 198 (2007).

³ The six component units are: Bowling Green Estates, East Meadow, Levittown, Roosevelt Field, Uniondale and Lido Beach-Point Lookout.

EXECUTIVE SUMMARY



The Town water department provides approximately 6.4 billion gallons of water to a population of 121,000,⁴ operating 27 wells, and 16 pumping stations at plant sites throughout its 13.9 square mile service area. Homeowners in the district paid an average of \$52 in taxes per year⁵ in addition to a water charge averaging \$1 per thousand gallons. For a district homeowner who uses 100,000 gallons per year, the total cost of water was \$151 in 2006.

The Town water department's cost of operations was \$12,603,466 and \$12,747,421 for the years 2005 and 2004 respectively. The Town charged back to each component unit a proportionate share of the water department's operating costs based on the assessed value of property in each district. The apportionment included an allocation of administrative expenses for Town's general fund departments which totaled \$1,604,600 for 2005 and \$1,536,600 for 2004 or about 12 % of the department's total expenses. The department derives approximately 50% of its revenues from charges for water usage, 30% from real property taxes, 10% from an allocation of a portion of the Town's sales tax revenues, with miscellaneous revenues making up the remainder.

Audit Scope and Methodology

The scope of our audit was limited to an examination of the financial operations of the Town's water department as it relates to the district and certain administrative operations of the Town of Hempstead, for the years ended December 31, 2004 and 2005, as reported in the Town of Hempstead's annual financial statements. Each of the six component districts comprising the Town's water department, including East Meadow, derives its administrative and financial infrastructure from the Town and does not issue its own set of financial statements.

This audit examined the revenues and direct expenses unique to the district's water operations, the allocation of Town administrative costs to the water department, the administrative and operating expenses of the Town water department as a whole, and the

⁴“Annual Drinking Water Quality Report for the Bowling Green Estates, East Meadow, Levittown, Roosevelt Field and Uniondale Water Districts 2005”

⁵ The average assessed value for homes in the District was \$350,000 in 2006. The average assessed value was calculated by dividing the total assessed value of all class 1 properties in the district by the number of class 1 parcels in the district. The water district tax on a home with an assessed value of \$350,000 was \$52.

EXECUTIVE SUMMARY

department's operations,. Since the administrative policies and procedures (such as payroll and benefits), procurement practices and contract monitoring are controlled at the Town level, we examined the Town's processes and controls and the water department's compliance therewith.

Summary of Significant Findings

Townwide Finding

Reliance on Manually Intensive Payroll and Time and Leave Processing Systems

Time and leave, payroll preparation and overtime recording are processed using undocumented, manually based processes that are not efficient and increase the risk for human error. We found that the payroll clerk entered all time worked and leave time taken onto a series of handwritten input sheets that are then forwarded to the Town Comptroller's office for data entry.

Water Department Findings

Inadequacy of Timekeeping for Administrative Staff

Proper internal controls dictate that time records should detail the exact time an employee starts and finishes their workday. We found that the department had approximately 20 administrative employees, none of whom were required to keep any record of the number of their hours worked or their starting and finishing times. The department relies on a weekly summary sheet prepared by a supervisor of the hours worked by the department administrative employees each day. There is no attestation by the employees to certify that the recorded time is correct.

Unauthorized Adjustments to Customer Billing

Controls over adjustments to customer accounts failed to ensure that the adjustments are adequately documented and formally approved by a senior official who is not involved in the billing or collection function.

Integrity & Accuracy of Billing System's Water Usage Data

Our review disclosed that input/output controls are not in place to ensure that water usage billed per the billing system agrees with the supporting meter reading records and supporting records are not retained as required by New York State Records Retention guidelines.

EXECUTIVE SUMMARY

Lack of Formalized Receiving Process

The department did not have a formalized receiving process to document that the goods received agree to the purchase order and also match the invoice and shipping documents. The person certifying on payment claim forms that goods were received is not always the recipient of the items ordered and cannot attest to the receipt of items received by other employees.

Inadequate Departmental Control over Supplies

We found that supplies are not inventoried to track their usage by commodity to help ensure that the materials are used only for the reasons acquired, and pre-set re-order points have not been established for supplies to ensure that quantities purchased are re-ordered before levels get too low.

Lack of Unique User Identifiers and Passwords

We found no evidence that the water billing and accounts receivable system incorporates user access profiles that limit system access only to the level required for employees' area of work. This increased the possibility that users could inadvertently and/or inappropriately access systems, programs and/or data, thereby compromising the integrity of the water billing and accounts receivable.

We also found that employee passwords were not safeguarded. Some employees shared passwords and some employees kept their passwords taped to their desks in open view. Employee passwords were known to the Town's Department of Information Technology because the password holders were unable to change the passwords themselves.

EXECUTIVE SUMMARY

Inaccurate Departmental Fixed Assets Inventory

The department did not perform a periodic physical inventory of fixed assets and did not reconcile the departmental records to the fixed asset records maintained by the town's comptroller.

We found that the inventory listing provided to us by the department's inventory custodian did not include 31 vehicles currently in use by the department, and it erroneously included eight vehicles that had been disposed of according to other departmental records.

The matters covered in this report have been discussed with officials of the Town Department of Water during this audit. On June 1, 2007 we submitted a draft report to the Town Department of Water with a request for comments. The Town Department of Water's comments, received on June 13, 2007 are included as an addendum to this report (Appendix).

TABLE OF CONTENTS

Findings and Recommendations	Page Number
Section 1 – Townwide Finding.....	1
Reliance on Manually Intensive Payroll and Time and Leave Processing Systems.....	1
Section 2 – Water Department Findings.....	2
Inadequacy of Timekeeping for Administrative Staff	2
Unauthorized Adjustments to Customer Billing and Revenue.....	2
Integrity and Accuracy of Billing System’s Water Usage Data	4
Lack of Formalized Receiving Process.....	5
Inadequate Departmental Control over Supplies	5
Lack of Unique User Identifiers and Passwords.....	6
Inaccurate Departmental Fixed Assets Inventory	7
Appendix - Town of Hempstead Department of Water’s Response and Auditor’s Follow-up.....	8

AUDIT FINDINGS AND RECOMMENDATIONS

Section 1 – Townwide Finding

The townwide finding relates to the processes administered by the town government.

Audit Finding (1):

Reliance on Manually Intensive Payroll and Time and Leave Processing Systems

Time and leave, payroll preparation and overtime are dependent on manual data entry, increasing the risk for human error. We found that:

- the computerized payroll system did not allow for distributed data processing. The payroll clerk must enter all time worked and leave time taken onto a series of handwritten input sheets that are then forwarded to the Town Comptroller's office for data entry. Transcribing data onto handwritten input sheets could be avoided if the department inputted time and leave directly into the system;
- the Town's official time and leave system uses individual handwritten cards to track each employee's accrual and use of leave time. An annual report of unused leave balances has to be manually prepared from these cards and forwarded to the Town's Human Resources department for the purposes of calculating the Town's liability for unused leave time for the Town's annual report; and
- there are no written procedures for employees to follow in preparing payroll, overtime payments or maintaining time and leave balances.

Audit Recommendations:

The Town should consider:

- a) fully automating and integrating its payroll and time and leave system, so that manual recordkeeping and the transcription of information to input sheets will no longer be required;
- b) reporting leave earned, leave used, and leave balances to employees periodically so that they can validate their leave balances; and
- c) documenting procedures that are used to track leave time and to prepare both regular and overtime payrolls.

AUDIT FINDINGS AND RECOMMENDATIONS

Section 2 – Water Department Findings

Water Department findings are those that relate to the processes administered by the water department on behalf of the six water districts. While our examination was limited to an examination of the financial operations of the Town's water department as it relates to the East Meadow water district, these findings and recommendations are applicable to all six water districts.

Audit Finding (2):

Inadequacy of Timekeeping for Administrative Staff

The Town of Hempstead Water Department had 78 employees, in 2004 there were 19 administrative employees, and in 2005 there were 21 administrative employees. All employees who are members of the Civil Service Employees Association are required to work a 40 hour week. Proper internal controls dictate that time records should detail the exact time employees start and finish their workday.

We were informed by the Town comptroller that administrative employees are not required to keep any record of the number of hours worked or starting and finishing times. The department relies on a weekly summary sheet prepared by a supervisor of the hours worked each day. There is no affirmative attestation, signed by the employees to certify that the hours recorded as time worked were correct. A record of the exact hours worked, including the times employees began work and ended work, attested to by the employee could be useful to resolve disputes over hours worked or protecting the town against fraudulent claims, such as on-the-job injuries. During the audit period, the department paid \$2,858,342 in salaries for hours that while certified to by the supervising personnel, were not attested to by the employees.

Audit Recommendation:

The Town should institute an appropriate time record control system requiring a record of the actual time and hours worked, signed and attested to by the employee and supervisor.

Audit Finding (3):

Unauthorized Adjustments to Customer Billing and Revenue

The department made 822 adjustments to the District's customer account balances and revenue amounts, decreasing revenue by a net of \$128,259 during the audit period. These adjustments were generally made to reflect meter reading corrections, penalties, interest, insufficient funds fees and to transfer water billing between town districts to reflect the source of water. We tested 35 adjustments that reduced certain customer

AUDIT FINDINGS AND RECOMMENDATIONS

billings by \$9,511 and increased others by \$3,913. We found that 28 of the 35 were not approved by a supervisor.

Controls over adjustments to customer accounts failed to ensure that the adjustments were adequately documented and formally approved by a senior official who is not involved in the billing or collection function. We found that:

- written procedures do not exist governing adjustments to customer accounts;
- an audit trail does not exist to accurately identify the employee who enters each adjustment in the system; and
- a monthly report is generated of all adjustments; however it is not reviewed or signed off on by a supervisor on a consistent basis.

Audit Recommendations:

- a) Customer adjustment procedures should be formalized to ensure that adjustments to customer account billings and balances are adequately explained, reviewed and approved prior to processing by a supervisor not involved in the billing or collection functions.
- b) Evidence of management's review and approval should appear on the supporting documentation and the monthly reports. Management may want to consider establishing a reasonable threshold amount above which a supervisor's approval is needed.
- c) Steps should be taken to improve the audit information trail, including accurate identification of both the preparer and the individual who enters the adjustment in the system.

AUDIT FINDINGS AND RECOMMENDATIONS

Audit Finding (4):

Integrity and Accuracy of Billing System's Water Usage Data

Our review disclosed that input/output controls were not in place to ensure that water usage billed per the billing system agreed with the supporting meter reading records and supporting records were not retained as required by New York State Records Retention guidelines.⁶ We found that:

- file control totals, such as hash totals⁷, were not generated for use in validating that all data has been correctly input and accepted by the system;
- water meter readings were taken and recorded electronically, and then uploaded into the customer billing and accounts receivable system to produce water bills. Customers' meter reading data was not compared on a test basis to the data uploaded into the system to validate the accuracy of the customer billings; and
- source documents relating to customer meter readings are only retained for six months and not six years as required by the New York State Records Retention guidelines. We have been advised that the department has taken measures to comply with these guidelines.

Audit Recommendations:

The department should:

- a) develop and implement input/output control procedures to ensure the completeness and accuracy of the water usage quantity information that appears in the billing system. A reconciliation of the input file control totals to the billing system's output control totals should be performed and reconciling items should be researched and resolved;
- b) develop an output review procedure to verify the accuracy of customer level data in the billing system prior to generating bills; and
- c) maintain records in accordance with the New York State Records Retention guidelines.

⁶ N.Y. Arts and Cultural Affairs Law §57.25 Schedule MU-1

⁷ A hash total is a validation check in which an otherwise meaningless control total is calculated by adding together numbers (such as the sum of the account numbers of the customers being billed) associated with a set of records. The hash total is compared to the data input to ensure that no entry errors have been made.

AUDIT FINDINGS AND RECOMMENDATIONS

Audit Finding (5):

Lack of Formalized Receiving Process

Purchases of fixed assets and supplies are shipped directly to the water department. The department did not have a formalized receiving process; receiving reports are not prepared as part of the cash disbursements process to document that the goods received agree to the purchase order and also match the invoice and shipping documents. Our review disclosed that the shipping documentation is attached to the town's claims form by the water department's accounts payable clerk. The clerk signs the "received by" certification section of the claim form and forwards it to the Town Comptroller's Office for payment. The accounts payable clerk is not always the recipient of the items ordered and cannot attest to the receipt of items received by other employees.

Audit Recommendation:

A formalized receiving process should be put in place for all supplies and equipment received by the department. The employee receiving the goods from the vendor should match the goods received and shipping documents with the purchase order and complete a receiving report to verify the proper receipt of the goods ordered.

Audit Finding (6):

Inadequate Departmental Control over Supplies

We found that the only formal inventory process in place relates to the town-wide requirement for inventory of fixed assets. Supplies are not inventoried.

The department has not established:

- a perpetual inventory system for supplies to track their usage by commodity to help ensure that the materials are used only for the reasons acquired, and
- pre-set re-order points for supplies to ensure that quantities purchased are re-ordered before levels get too low.

Audit Recommendation:

The department should establish inventory controls for the supplies it uses in the normal course of business. A perpetual inventory system should be established and the usage of supplies should be reviewed for reasonableness as to quantities. Pre-set re-order points should be established to monitor inventory levels to help avoid out of stock conditions.

AUDIT FINDINGS AND RECOMMENDATIONS

Audit Finding (7):

Lack of Unique User Identifiers and Passwords

It is a standard element of internal control that all users of shared electronic data processing systems have user access profiles that limit their system access only to the level required for the work that they are performing.

We found no evidence that user access security controls were in place to limit the nature and extent of user access for the water billing and accounts receivable system. The Town's Department of Information Technology did not generate unique user profiles that document, authorize and control user access within the system. This increased the possibility that users could inadvertently and/or inappropriately access systems, programs and/or data, thereby compromising the integrity of the system and its data.

We also found that some employees did not properly secure their user identification numbers and passwords, increasing the risk of unauthorized access, which could jeopardize the integrity of the data and the audit trail since data entry could not be reliably identified with a particular individual. For example:

- An employee who was required to enter data did not have a unique user identification number or password and instead shared another employee's user identification number and password.
- Some employees kept their passwords taped to their desks in view of other employees.
- The Town's Department of Information Technology issued unique user passwords that could not be changed by the user. The fact that the passwords are known to the Information Technology employees increases the risk that the passwords could be misused. The inability of the user to change passwords increases the risk that they will become known to other employees.

Audit Recommendations:

The Town's Department of Information Technology should:

- a) issue each user's identification number with an initial password that must be changed by the user before access to any system is allowed;
- b) provide for passwords that expire and require that they be changed by the users prior to expiration;
- c) issue a formal reminder to all employees that User IDs and passwords are not to be shared or kept out in the open; and
- d) develop unique user profiles that document, authorize and control user access to the system. These profiles should limit the level of access (data entry, view only, approve, etc.) within each system and the functions that can be performed (billing,

AUDIT FINDINGS AND RECOMMENDATIONS

revenue, cash disbursements, general ledger, none, etc.) depending on the employee's assigned tasks and responsibilities.

Audit Finding (8):

Inaccurate Departmental Fixed Assets Inventory

The department is required to enter all equipment costing \$1,000 or more into the town-wide inventory of fixed assets. We found that the inventory provided to us by the department's inventory custodian included 66 vehicles, however it did not include 31 vehicles currently in use by the department and it erroneously included eight vehicles that had been disposed of according to other departmental records. The inventory custodian could not explain the discrepancies. It should be noted that a revised vehicles inventory was provided to us before the end of our field work.

The department's inventory process is not adequate to ensure the accuracy of its records. They do not perform a periodic physical inventory of fixed assets and do not reconcile the departmental records to the fixed asset records maintained by the Town's comptroller.

Audit Recommendation:

The department should develop written fixed assets procedures to ensure that all eligible assets are accurately reflected, including additions and disposals.

Appendix
TOWN OF HEMPSTEAD DEPARTMENT OF WATER'S RESPONSE
AND AUDITOR'S FOLLOW-UP

Audit Finding (1):

While time and leave, payroll preparation and overtime are prepared manually, all data is reviewed and approved by the Commissioner of Water before transmittal for payment to the Comptroller's office.

Auditor's Follow-up Response:

We reiterate our recommendation that the Town consider automating and integrating its payroll and time and leave system and formally document the processes used.

Audit Finding (2):

Although systems vary among departments, time and leave accounts are kept for all employees. In some cases, attendance is recorded using time clocks. In others, records are maintained by town employees charged with the responsibility of physically observing the daily attendance of workers. To modernize town practice in this regard, the administration is currently working to implement the installation of modern technology – including hand scanning – to track the arrival and departure time of personnel.

With respect to the Water Department, and prior to your audit (in January, 2006), the procedure was modified to require a supervisor to monitor and attest to each person's daily attendance and record same on a weekly time sheet. At the end of each week, the supervisor is required to certify the time sheet's accuracy.

As a result of your suggestion, and until such time as more modern technology is deployed in the Water Department, each employee will be required to add his or her certification to that of his or her supervisor that his or her time sheet is accurate.

Auditor's Follow-up Response:

We concur with the corrective actions taken by the department.

Audit Finding (3):

Based upon the draft's recommendation, the department's existing procedure will be formalized to ensure that an audit trail exists.

In addition, your suggestion that a reasonable threshold amount, above which a supervisor's approval is needed, will be implemented.

Appendix
TOWN OF HEMPSTEAD DEPARTMENT OF WATER'S RESPONSE
AND AUDITOR'S FOLLOW-UP

Auditor's Follow-up Response:

We concur with the corrective actions taken by the department to develop and implement input/output control procedures and to establish a threshold for adjustments above which supervisory approval is required. We reiterate our recommendation that the monthly report of all adjustments be reviewed and signed by a supervisor.

Audit Finding (4):

Working with our Office of Comptroller and software vendor, we will develop and implement input/output controls, such as the use of computerized "hash totals" to assure the accuracy of usage information and to verify billing system data prior to bill generation.

We dispute the draft's observation that "source documents relating to customer meter readings are only retained for six months and not six years as required by the New York State Records Retention guidelines." Although the draft acknowledges that the department has taken steps to comply with these guidelines, I would point out that the records referred to, at all times, have been maintained for the legally required period in electronic form and were, at all times, capable of being printed on a moment's notice.

Appendix
TOWN OF HEMPSTEAD DEPARTMENT OF WATER'S RESPONSE
AND AUDITOR'S FOLLOW-UP

Auditor's Follow-up Response:

We concur with the corrective actions taken by the department to implement input/output controls.

We were informed during field work that the original meter reading files, electronically recorded in the meter reading device and then uploaded, are not retained after six months. While the customer billing information was retained, we were unable to verify it back to the data gathered by the meter reading devices because the original data was not retained. We reiterate our recommendation that this original data be stored in an electronic or hard copy format in compliance with the New York State Records Retention guidelines.

Audit Finding (5):

The department is developing a formalized receiving process for all supplies and equipment which will be implemented immediately.

Auditor's Follow-up Response:

We concur with the corrective actions taken by the department.

Audit Finding (6):

Plans for an improved inventory control process, being developed for the last few months, has been implemented and two employees have been specifically assigned to this process. A perpetual inventory system – to monitor and assure adequate supply levels – is now being developed and will be implemented shortly.

Auditor's Follow-up Response:

We concur with the corrective actions taken by the department.

Appendix
TOWN OF HEMPSTEAD DEPARTMENT OF WATER'S RESPONSE
AND AUDITOR'S FOLLOW-UP

Audit Finding (7):

Following review of your recommendations, we will be consulting with our software vendor regarding the updating of our system to permit system access at differing levels based on user profiles. In reviewing your recommendations in this regard with the town's Department of Information Technology, I have been made aware that the town already has plans to modify the system to require individuals to create (and periodically change) their passwords. As part of this modification, employees with computer access will be required to sign documents accepting personal responsibility for the security of their individual machines.

Finally, employees will be directed not to share their passwords, not to allow them to be displayed and otherwise to secure their passwords.

Auditor's Follow-up Response:

We concur with the corrective actions taken by the department.

Audit Finding (8):

The delivery of an outdated vehicle listing to your representative resulted from a miscommunication within the Department of Water and haste on the part of departmental personnel to furnish the document which your office requested. In fact, an accurate listing did exist at the time you requested same and, as you indicate, it was provided to you promptly. We regret the error.

In fact, in tracking fixed assets, the department *exceeds* comptroller requirements in that it includes items under the \$1,000 townwide threshold.

The above being the case, we would respectfully urge that this item be deleted from the report.

Appendix
TOWN OF HEMPSTEAD DEPARTMENT OF WATER'S RESPONSE
AND AUDITOR'S FOLLOW-UP

Auditor's Follow-up Response:

The fixed asset listing was corrected after we brought the discrepancies to the department's attention. While the Assistant to the Deputy Commissioner's vehicle listing was correct, the fixed asset inventory custodian's official listing was not up to date.

The department's response does not address our recommendation that the department develop written fixed asset procedures. These procedures should address our finding that periodic fixed asset inventories are not taken.