



Germantown Fire District Board Oversight

Report of Examination

Period Covered:

January 1, 2013 — March 4, 2014

2014M-166



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

August 2014

Dear Fire District Officials:

A top priority of the Office of the State Comptroller is to help local government officials manage government resources efficiently and effectively and, by so doing, provide accountability for tax dollars spent to support government operations. The Comptroller oversees the fiscal affairs of local governments statewide, as well as compliance with relevant statutes and observance of good business practices. This fiscal oversight is accomplished, in part, through our audits, which identify opportunities for improving operations and Board of Fire Commissioner governance. Audits also can identify strategies to reduce costs and to strengthen controls intended to safeguard local government assets.

Following is a report of our audit of the Germantown Fire District, entitled Board Oversight. This audit was conducted pursuant to Article V, Section 1 of the State Constitution and the State Comptroller's authority as set forth in Article 3 of the General Municipal Law.

This audit's results and recommendations are resources for local government officials to use in effectively managing operations and in meeting the expectations of their constituents. If you have questions about this report, please feel free to contact the local regional office for your county, as listed at the end of this report.

Respectfully submitted,

*Office of the State Comptroller
Division of Local Government
and School Accountability*

Introduction

Background

The Germantown Fire District (District) is a district corporation of the State, distinct and separate from the Town of Germantown and Columbia County. An elected five-member Board of Fire Commissioners (Board) governs the District. The Board is responsible for the District's overall financial management, including establishing appropriate internal controls over District operations and recordkeeping, monitoring the controls to ensure that assets are properly safeguarded and ensuring that financial transactions are executed in accordance with statutory and managerial authorization.

The District Treasurer (Treasurer) is the chief fiscal officer and is responsible for the receipt, custody, disbursement and accounting for District funds and for preparing monthly and annual financial reports. The Treasurer accounts for the District's financial activities in the general fund. The District's 2013 general fund expenditures were \$273,071 and budgeted appropriations for 2014 are \$272,446.

Objective

The objective of our audit was to examine internal controls over the District's operations. Our audit addressed the following related question:

- Does the Board provide sufficient oversight of the District's financial activities?

Scope and Methodology

We examined the District's internal controls over selected financial activities and reviewed its records and reports for the period January 1, 2013 through March 4, 2014. To analyze the District's historical financial condition, we extended our audit period back to the 2011 fiscal year.

We conducted our audit in accordance with generally accepted government auditing standards (GAGAS). More information on such standards and the methodology used in performing this audit is included in Appendix C of this report.

Comments of District Officials and Corrective Action

The results of our audit and recommendations have been discussed with District officials and their comments, which appear in Appendix A, have been considered in preparing this report. Except as specified in Appendix A, District officials generally agreed with our findings and indicated they plan to initiate corrective action. Appendix B includes our comment on an issue District officials raised in their response.

The Board has the responsibility to initiate corrective action. Pursuant to Section 181-b of the Town Law, a written corrective action plan (CAP) that addresses the findings and recommendations in this report must be prepared and forwarded to our office within 90 days. To the extent practicable, implementation of the CAP must begin by the end of the next fiscal year. For more information on preparing and filing your CAP, please refer to our brochure, *Responding to an OSC Audit Report*, which you received with the draft audit report. The Board should make the CAP available for public review in the District Clerk's office.

Board Oversight

The Board is responsible for overseeing the District's financial activities and safeguarding its resources. To fulfill this duty, it is essential that the Board develop and implement a system of internal controls which includes policies and procedures to ensure that transactions are authorized and recorded, and applicable laws, rules and regulations are followed. Where practicable, duties should be separated so that one employee does not control all phases of the financial transaction process. When complete segregation of duties is not possible, active supervision and oversight become even more important components of an effective internal control system. In addition, New York State General Municipal Law (GML) limits the ability of municipal officers or employees to enter into contracts in which their personal financial interests and their public powers and duties conflict.

The Board needs to improve its oversight of District operations. The Board did not properly award a contract for \$4,800 that was determined to be a prohibited conflict of interest, has not adopted key policies and procedures and does not properly plan for reserves or capital expenditures. As of December 31, 2013, the District had \$398,000 in reserves but did not have a formal plan regarding the use of these funds. As such, taxpayers are not properly informed regarding what their taxes are being used to fund. Without adequate oversight, District resources are not properly safeguarded and are at a greater risk of being misappropriated without detection or correction.

Conflict of Interest

GML limits the ability of municipal officers and employees to enter into contracts in which both their personal financial interests and their public powers and duties conflict. Unless a statutory exception applies, GML prohibits municipal officers and employees from having an interest in a contract with the municipality for which they serve when they also have the power or duty – either individually or as a Board member – to negotiate, prepare, authorize or approve the contract; to authorize or approve payment under the contract; to audit bills or claims under the contract or to appoint an officer or employee with any of those powers or duties.

The Board did not properly award a contract for cleaning services for \$4,800 when it renewed its contract with a Commissioner's spouse in 2013. The contract was originally awarded in 2011 for \$4,800 and was properly bid and awarded based on the lowest cost. The Commissioner disclosed his interest and recused himself from voting. Because the contract was properly bid and awarded to the

lowest bidder, the Commissioner did not have a prohibited interest at that time. However, when the District renewed the contract in 2013, it did not use a competitive process and had no process to indicate that the 2013 agreement was the lowest dollar offer. Further, there was no indication that each Board member had an opportunity to approve the contract. Therefore, the Commissioner had a prohibited interest in this contract. When a district pays officials for services, the payment can raise questions as to the propriety of the transactions. This is especially true when proper disclosures are not made.

Policies and Procedures

It is essential that the Board establish a system of internal controls which include policies and procedures to ensure that transactions are authorized and properly recorded in a timely manner; that financial reports are accurate, reliable and filed timely; and that the District complies with its bylaws and applicable laws, rules and regulations.

The District does not have policies and procedures for key financial functions including reserves, budgeting, cash receipts and disbursements, computer and internet use and travel. In addition, the District's policies for procurement and investments were not effective. These policies were adopted in 1995 and actual procedures used are not documented and are not consistent with the adopted policy. For example, the policy requires employees to obtain two verbal quotes when making purchases valued between \$250 and \$2,999. However, employees do not obtain the required quotes when making such purchases. Key District officials and Board members were also unaware of the existence of policies.

Because the District does not have effective policies and procedures outlining expectations for managing District resources, there is an increased risk of abuse.

Segregation of Duties

Segregation of duties is the division of key tasks and responsibilities among various employees. No one individual should control all key aspects of a transaction. By separating tasks and responsibilities, such as receiving, recording, depositing, disbursing and reconciling assets, management can reduce the risk of error, waste or wrongful acts occurring or going undetected. However, in cases where tasks cannot be effectively separated, management can substitute increased supervision as an alternative control activity that can help prevent or reduce these risks.

During the audit period, the Board implemented multiple procedures to ensure adequate segregation of duties or provide for compensating controls. Previously, the Treasurer handled all aspects of financial transactions. In October 2013 (prior to our onsite fieldwork), District officials implemented new procedures such as having a

Commissioner pick up, open and review the mail, including bills and bank statements. The Commissioner also reviews canceled checks, deposits and transfer activity. In addition, at the Board's monthly meeting, the Board approves a list of bills for payment, and discusses major purchases and their timing.

We tested a randomly selected sample of 25 disbursements totaling \$32,103 out of 198 general disbursements totaling \$225,070 and reviewed 22 disbursements totaling \$1,401 to key officials or related parties. All disbursements appeared to be properly authorized and for proper District purposes. We also reviewed the check sequence within and between the abstracts to ensure that all checks were accounted for. We found two missing items: one check was properly voided and retained; a second check was not available for review and did not clear the bank during our audit period. In addition, we reviewed all 15 non-check disbursements totaling \$589,958, including such items as wire transfers or payments made using an automated clearing house. We confirmed these charges were for proper District purposes.

Reserves

Saving for future projects, acquisitions and other allowable purposes is an important planning consideration for local governments. Reserve funds provide a mechanism for legally saving money to finance all or part of future expenditures for infrastructure, equipment and other requirements. These reserve funds provide resources for both unanticipated events and other identified or planned needs.

A governing board that establishes and finances reserve funds should develop a written policy that communicates to taxpayers why the money is being set aside, the board's financial objectives for the reserves, optimal funding levels and conditions under which the assets will be used. Boards should also periodically assess the reasonableness of the amounts accumulated in their reserves. Local governments should balance the desirability of accumulating reserves for future needs with the obligation to ensure taxpayers are not overburdened by these practices. There should be a clear purpose or intent for reserve funds that aligns with statutory authorizations.

The District had four reserve funds with balances totaling \$398,000 as of December 31, 2013, as indicated in Figure 1. District officials could not locate the original documentation for the establishment of the reserves and there are no written procedures for their funding and use. The District's reserve funds increased from \$142,836 as of December 31, 2009 to \$398,000 as of December 31, 2013 – approximately \$64,000 per year – because the Board overestimated budget appropriations. The overestimated appropriations resulted in operating surpluses, which increased surplus cash. District officials then placed the surplus cash into reserve funds.

Figure 1: Reserves and Cash Balances

Fiscal Year	2009	2010	2011	2012	2013
Truck Reserve	\$40,727	\$65,824	\$108,740	\$149,150	\$189,548
Building Reserve	\$102,109	\$107,267	\$107,729	\$108,087	\$108,357
Radio Reserve	-	-	\$8,025	\$12,081	\$20,088
Personal Protective Equipment	-	-	-	-	\$80,007
Total Reserves	\$142,836	\$173,091	\$224,494	\$269,318	\$398,000

Funding reserves with excess cash resulting from operating surpluses did not provide the taxpayers with an accurate picture of what their taxes were actually being used to fund. A more transparent and appropriate method of funding reserves would be to estimate overall appropriations more accurately and include a specific budgetary appropriation for the intended purpose of funding reserves. By including an accurate estimate of the amount the Board intends to set aside in the reserves at the time the budget is prepared, officials can provide voters the opportunity to decide whether they concur with this use of their tax money. Without written plans, there is no assurance that the Board followed the proper procedures to establish reserve funds or that the funds set aside will be used as intended.

Capital Planning

An important Board oversight responsibility is to plan for the future by setting adequate long-term priorities and goals. To address this responsibility, it is important for District officials to develop comprehensive multiyear financial and capital plans to estimate the future costs of ongoing services and capital needs. Effective multiyear plans project operating and capital needs and financing sources over a three- to five-year period and allow District officials to identify developing revenue and expenditure trends, set long-term priorities and goals and avoid large fluctuations in tax rates. Long-term financial plans work in conjunction with Board-adopted policies and procedures to provide necessary guidance to employees on the financial priorities and goals set by the Board. In addition, the Board should monitor and update long-term financial plans on an ongoing basis to ensure that its decisions are guided by the most accurate information available.

The District has no formal plans to use the \$400,000 in reserve funds to replace trucks and radios. The radio replacement is a result of a Columbia County change in the emergency radio system and, therefore, may be paid for by the County. Further, the District has not formed a plan for making essential improvements to its facilities and equipment.

While the Board received monthly cash reports, it did not review them. As such, it was unaware that the general fund checking account had a cash balance totaling \$192,000 at December 31, 2012. The Chairman said that, when the Board became aware that the checking account had a substantial cash balance, it used \$44,000 to purchase a compressor needed for self-contained breathing apparatus gear for the firefighters and \$80,000 to establish a personal protective equipment reserve in 2013.

When District officials budget for future needs, it places a burden on District taxpayers. Therefore, it is essential that District officials adopt long-term capital and financial plans to ensure reserved amounts are realistic and real property taxes are not higher than the amounts needed to fund District capital needs.

Recommendations

1. District officials should ensure that all officials and employees are familiar with the requirements of the District's Ethics and Disclosure Policy as they relate to conflicts of interest.

The Board should develop policies and procedures over:

2. The procurement process to ensure that goods and services are procured in a transparent and competitive way.
3. Cash receipts and disbursements that adequately segregate duties and provide oversight. If it is not practical to segregate duties, the Board should establish compensating controls.
4. Reserves that clearly communicate to District taxpayers the purpose and intent for establishing each reserve fund, the manner in which the Board will fund and maintain each reserve fund, and the optimal or targeted funding levels and conditions under which each fund's assets will be used or replenished.
5. Capital planning by developing a comprehensive multiyear capital and financial plan to establish long-term objectives for funding long-term needs.

APPENDIX A

RESPONSE FROM DISTRICT OFFICIALS

The District officials' response to this audit can be found on the following pages.

Germantown Fire District
P.O. Box 331
181 Main Street
Germantown, New York 12526

August 4, 2014

Office of the State Comptroller
Newburgh Regional Office
33 Airport Center Drive
Suite 103
New Windsor, NY 12553

Attention: Tenneh Blamah
Chief Examiner

On behalf of the Germantown Board of Fire Commissioners, we appreciate your detailed review of our policies and procedures as it relates to the Commissioners oversight of the Fire District. The Commissioners are committed to improving operations and board governance which ultimately provides better accountability for tax dollars spent to support Fire District operations. The Board of Commissioners respectfully request that this response also be considered our corrective action plan for the purposes of statutory compliance.

Conflict of Interest. Although we dispute your findings under conflict of interest and the improper award of a cleaning services contract for \$4800.00, we do agree and have already implemented a new "Ethics" policy as it relates to conflicts of interest and prohibited interest in awarded contracts and we will provide more details in our monthly meeting minutes.

See
Note 1
Page 13

Policies and Procedures. Based on your offices recommendations during your review visit in 2013, the District was already in the process of updating our policies and procedures prior to your 2014 audit. All but one of these policies has now been adopted by the Board of Fire Commissioners and the last one will be in place by the end of the year.

Segregation of Duties. As you point out in your audit, the Board of Fire Commissioners made changes in 2013 to better segregate the duties of individuals for better control and accountability. And based on our conversations during the audit process, we have already instituted more oversight with bank transfers and deposits. The Board is committed to better accountability of all its public funds and will continue to refine our roles and responsibilities and document them in our policies.

Reserves. We understand the need to establish reserve accounts for future purchases of vehicles and equipment and as you know the district has several already established. Based on your recommendations from your 2013 review, funds have already been

transferred and reserve accounts have been established to provide funding for future truck and equipment purchases. The District will work to establish more details in writing for the timing of vehicle and equipment expenditures for our reserve accounts before the end of 2014.

Capital Planning. The District does not dispute your findings under capital planning. The District will put into writing a long-term financial plan, in conjunction with our current reserve accounts, to provide the necessary guidance on future financial priorities and goals established by the District. This plan will be in effect before the end of 2014.

The Germantown Board of Fire Commissioners views your audit and report as an opportunity to improve public accountability of our policies and procedures and the expenditure of public funds.

Best regards,

Roy D. Brown, Chairman
Germantown Board of Fire Commissioners

Cc: Board of Fire Commissioners, Germantown Fire District

APPENDIX B

OSC COMMENT ON THE DISTRICT'S RESPONSE

Note 1

Under GML, an agreement between the District and a Commissioner or spouse must be awarded through a competitive process approved by the Board. In this instance, the Commissioner with the conflict of interest should have recused himself from awarding the contract.

APPENDIX C

AUDIT METHODOLOGY AND STANDARDS

The objective of our audit was to assess the Board's oversight of the District's financial activities and to examine the internal controls over selected financial activities for the period January 1, 2013 through March 4, 2014. To achieve our audit objective and obtain valid audit evidence, we performed the following audit procedures:

- We interviewed District officials to gain an understanding of the District's policies and procedures.
- We reviewed the minutes of the Board's proceedings to obtain an understanding of the District's policies and procedures.
- We reviewed the District's financial records and reports.
- We obtained and reviewed bank statements, canceled checks and claims packets. We tested the accuracy and validity of selected claims.
- We reviewed purchases made from or by District officials and Fire Company members for conflict of interest.
- We tested a random sample of 25 out of 198 general disbursements and a judgmental sample of 22 disbursements to key officials or related parties.
- We reviewed the check sequence within and between the abstracts to ensure that all checks were accounted for.
- We reviewed all non-check disbursements, including such items as wire transfers or payments made using an automated clearing house.
- We requested original documentation for the establishment of the reserves and written procedures for their funding and use.

We conducted this performance audit in accordance with GAGAS. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

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