



Sherrill-Kenwood Water District

Board Oversight

Report of Examination

Period Covered:

January 1, 2010 — October 31, 2011

2012M-100



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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

August 2012

Dear 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 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 Sherrill-Kenwood Water 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 Sherrill-Kenwood Water District (District) provides water services to areas in the City of Sherrill, the City of Oneida and the Town of Vernon. The District is governed by the Board of Water Commissioners (Board) which is comprised of three members and is responsible for the general management and control of the District's financial affairs. The Secretary is responsible for the District's finances, accounting records, and financial reports. There are three clerks that assist the Secretary with fiscal duties. The District's revenues received for the 2011 fiscal year were approximately \$486,000. Revenues for the 2010 fiscal year were approximately \$490,700.

The District contracts with the City of Oneida to purchase its entire water supply. The District's distribution system consists of approximately 25 miles of water main, 168 fire hydrants and provides water service for about 1,250 customers.

The individuals responsible for the District's financial operations (including the Secretary and three clerks) are employees of both the City of Sherrill and the District, and therefore perform tasks for both units of government. Recommendations made in this report relating to physical changes in the office or segregation of duties of office personnel are directed to the Board which will need to work with City of Sherrill officials to implement our recommendations.

Objective

The objective of our audit was to review the Board's oversight of District fiscal operations. Our audit addressed the following related question:

- Did the Board provide adequate oversight of the billing and collection of water rents?

Scope and Methodology

We examined the Board's oversight of the billing and collection of water rents for the period January 1, 2010 to October 31, 2011.

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 are included in Appendix C of this report.

Comments of Local 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 had already or planned to implement corrective action. Appendix B includes our comment on the issue raised in the District's response letter.

The Board has the responsibility to initiate corrective action. A written corrective action plan (CAP) that addresses the findings and recommendations in this report should be prepared and forwarded to our office within 90 days, pursuant to Section 35 of the General Municipal Law. 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. We encourage the Board to make this plan available for public review in the Secretary's office.

Board Oversight

The Board is responsible for overseeing the District's financial affairs and safeguarding its resources. These duties include establishing a system of internal controls to provide reasonable assurance that cash and other resources are properly safeguarded, and that transactions are authorized and properly recorded. The Board must segregate financial duties to ensure that no individual controls all aspects of the financial transactions, or provide for compensating controls that mitigate the risks. In addition, the Board should establish accountability over transactions by requiring separate cash drawers and computer user accounts for employees. The Board should also require the Secretary to prepare accurate monthly financial reports for its review, and should perform, or provide for, an annual audit of the District's records and reports.

The District has not fully segregated duties related to the billing and collection of water rents. District officials told us that they have supervisory review procedures in place to mitigate the risks; however, there was not sufficient documentation on file to substantiate the extent of the supervisory review procedures. Further, the District's procedures do not provide for individual accountability for collections because the three clerks who collect cash use the same cash drawer and the same user name and password in the computerized financial system. In addition, the Board did not receive monthly reports to monitor the District's financial activity and condition, and did not require an annual audit of the Secretary's records and reports. Although we found no exceptions in the billing or collection of water rents, the Board should further strengthen internal controls to reduce the risk that errors or irregularities will occur in the future.

Segregation of Duties - An effective system of internal control provides for the adequate segregation of duties so that no one individual controls all phases of a transaction. In addition, proper division of responsibility should provide that the work of one employee is independently verified in the course of another employee's regular duties. When one person performs all the duties related to billing, cash collections, and record keeping, it increases the risk that cash could be misappropriated and not be detected. At a minimum, the duties of cash custody and record keeping should be separated. If limited resources make it difficult to segregate incompatible duties, District officials must implement compensating controls, such as designating someone outside the cash collection and billing process to regularly review bank deposits, canceled checks, records, and reconciliations and compare them to the transactions recorded in the District's records to verify accuracy.

The Board did not ensure adequate segregation of the duties of the three clerks in respect to billing, collecting and posting customer accounts. The responsibilities of the clerks are as follows:

- Clerk-Typist: preparing and mailing bills, collecting and recording payments, preparing and making bank deposits, and adjusting customer accounts prior to obtaining the Secretary's approval.
- Clerk: collecting payments, performing bank reconciliations, preparing the daily cash reconciliation, and serving as back-up in the Deputy City Clerk's absence.
- Deputy City Clerk: collecting payments, transferring funds among District and City bank accounts, and serving as back-up in the Clerk's absence.

Although each clerk could have the ability to control all aspects of a cash transaction, District officials told us that they have implemented compensating controls to reduce the risk of significant errors or irregularities. For example, the Clerk-Typist maintains a manual water rents receivable control account which she reconciles to the total of the unpaid customer accounts each month and provides to the Secretary for review. In addition, the Secretary periodically reviews the bank reconciliations prepared by the Clerk and customer account adjustments presented to him by the Clerk-Typist after they are made.¹ Although we saw that the Secretary had initialed or signed account adjustments and some of the monthly bank reconciliations during our audit period, many of the reconciliations did not have his initials to indicate they were reviewed. In addition, the Secretary did not document his review of the receivable account reconciliation and he did not have a process in place to verify the Clerk-Typist presented all the account adjustments to him for review.

We examined 30 randomly selected water bills, totaling approximately \$1,388, to determine if they were properly billed and did not identify any discrepancies. In addition, we reviewed all 35 water account adjustments for our audit period, totaling \$783, and all of them were proper account adjustments, supported by adequate documentation. We reviewed select receipts, totaling approximately \$79,800, and traced them to timely deposits into the proper bank account. We also verified that 2011 unpaid water rents were relieved on the 2012 tax rolls. Our review did not disclose any discrepancies in the billing or collection of water rents; however, the risk remains

¹ The Secretary told us that he verbally approves any adjustments that are out of the ordinary before the Clerk-Typist makes them.

that an error or irregularity could occur and go undetected and uncorrected.

User Accountability – Good internal controls require that a separate cash drawer is assigned to each person who collects cash and that a unique user account is created and used by each employee who enters transactions into the computerized financial system to reduce the risk of errors or irregularities through individual accountability.

The Board has not adopted comprehensive written policies and procedures that require the use of separate cash drawers or separate user names and passwords to establish individual accountability of the clerks. The three clerks use a common cash drawer and the same user account when collecting payments and entering them into the computerized financial system. Although each clerk initials the receipt documents related to the moneys they collect, if a problem did arise, District officials would not be able to determine which of the three clerks was responsible for the error or irregularity.

Monthly Reports – It is a good management practice for the Board to receive a monthly report of all moneys collected and disbursed during the month. It is important that these reports also include detailed year-to-date budget to actual comparisons for revenues and expenditures, in addition to fund balance and reconciled cash balances for the District. Complete and accurate monthly reports provide essential financial information that the Board can use to monitor the District's financial condition.

The Board did not receive monthly statements of moneys received and disbursed, budget comparisons, fund balance, or cash balances to review. The Board did receive and approve a list of claims to be paid each month. It is difficult for the Board to effectively oversee District finances and the risk that moneys could be misappropriated without detection increases due to the lack of comprehensive monthly reports.

Annual Audit – In order to meet its fiscal oversight responsibilities, the Board should annually audit, or have an independent public accountant audit, the records and reports maintained on the District's behalf by the Secretary. This annual audit serves as an important internal control over cash receipts and disbursements by providing independent verification that transactions have been properly recorded and that cash has been properly accounted for. It also provides Board members with an added measure of assurance that the financial records and reports contain reliable information on which to base financial decisions.

The Board did not audit, or contract with an independent auditor to audit, the records maintained during 2010. One Board member was unaware that the Board should perform an annual audit and thought that the District may have been included as part of the annual City of Sherrill audit. We found no documentation to support an audit of the District in the City's annual audit report. The failure of the Board to conduct an annual audit of the records and reports precluded the Board from having assurance that the financial resources of the District were accounted for properly.

Recommendations

1. The Secretary should document his supervisory review of the clerks who are involved with cash handling and record keeping.
2. The Secretary should make account adjustments or approve account adjustments made by the Clerk-Typist prior to an adjustment being made and he should periodically generate and review account adjustment reports to verify all adjustments are authorized.
3. The Board, in conjunction with the Secretary and City of Sherrill officials, should establish and implement policies and procedures that require the use of individual user accounts and cash drawers in order to establish accountability over the three clerks in the office.
4. The Board should ensure monthly financial reports are generated in order to monitor the District's financial operations. These reports should include all District cash activity, budget to actual comparisons and cash balances.
5. The Board should perform, or provide for, an annual audit of the District's records and reports.

APPENDIX A

RESPONSE FROM LOCAL OFFICIALS

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

SHERRILL-KENWOOD WATER DISTRICT

377 Sherrill Road
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Sidney Thirumulpad, Chairman
Gordon Silsby, Board Member
Charles Vallee, Board Member

Robert A. Comis, City Manager
Michael D. Holmes, Secretary
Christopher M. Dunn, Superintendent

August 8, 2012

Chief Examiner Rebecca Wilcox
Office of the State Comptroller
State Office Building, Room 409
333 East Washington Street
Syracuse, New York 13202

Re: Draft Report Sherrill-Kenwood Water District July 31, 2012

Dear Ms. Wilcox:

The Sherrill-Kenwood Water District Board (Board) is responding to information contained in the document titled *Draft Report of Examination* (Draft), received July 17, 2012 revised July 31 and provided at exit conference (EC) held on July 24, 2012. We would like to thank the Comptroller's representatives, who were on site periodically during the four-month period, for the professional manner in which their review was conducted, resulting in a thorough audit of District procedures for the period of January 1, 2010 – October 31, 2011.

Overall the Comptroller's audit confirmed the Board's expectations that there are not any significant issues relevant to the oversight of finances of the Water District. It also reconfirms our confidence in the staff that manages and performs the day-to-day functions of the Water District. It continues to be our goal to improve the policies, procedures, means and methods to provide services to District customers efficiently and cost effectively.

We do however have the following comments relative to the July 31st Draft.

- In the first paragraph of the DRAFT it states that the Board "provide reasonable assurance that cash and other resources are properly safeguarded". In the fifth paragraph it is stated that "District officials told us that they have implemented compensating controls." A reader without broader understanding of the District's process could interpret that compensating controls were "implemented" as a result of the audit and that supporting documentation was not provided. We believe it should be acknowledged that these controls have long preexisted the audit period and continue presently. In addition, the supporting documentation was provided by District officials to support its assertion that controls existed. One goal of the Board as stated earlier is to improve procedures; it is the opinion of the Board that the existing controls met the intention to provide reasonable assurance.
- In the first paragraph of the DRAFT it states "The Board must segregate financial duties to ensure that no individual controls all aspects of the financial transactions, or provide for compensating controls that mitigate the risks". Our response is to suggest that at the beginning of the paragraph User Accountability the word "Good" be replaced by "Stronger internal controls than currently exist would". This language would reinforce to a reader that while full segregation of duties does not exist compensating controls are present.

In addition the Board is providing, as required, the following a corrective action plan (CAP).

Corrective Action Plan

The Office of the New York State Comptroller (NYSOSC) performed an audit on the Sherrill-Kenwood Water District (SKWD) from January 1, 2010 through October 31, 2010. The *Draft Audit Report*, dated July 31, 2012, noted five (5) recommendations that this corrective action plan (CAP) will address.

Recommendation Item #1: The Secretary should document his supervising review of the clerks who are involved with cash handling and record keeping.

The Board agrees that despite the fact that the district Secretary has the duty and responsibility for cash handling and record keeping and is in fact performing the oversight, the documentation to document this oversight could be improved. In addition the cash handling process could be even more strengthened if the secretary performed some daily duties on a periodic random basis.

The Board will look to implement within the next thirty (30) days a process by the Secretary to formally document these oversight procedures he already has in place. Additionally the Secretary will look to periodically perform some of the cash handling procedures on a periodic unannounced random basis.

Recommendation Item #2: The Secretary should make account adjustments or approve account adjustments made by the clerk typist prior to the adjustments being made and he should periodically generate and review account adjustment reports to verify all adjustments are authorized.

The SKWD areas that such a modification would decrease the risk of fraud and help prevent financial losses. The SKWD plans to implement such prior approval procedures in accordance with the recommendation within the next thirty (30) days. The Secretary will follow through with the implementation and document the steps of approval going forward.

Recommendation Item #3: The Board, in conjunction with the Secretary and City of Sherrill officials, should established and implement policies and procedures that require the use of individual users accounts and cash drawers in order to establish accountability over the 3 clerks in the office.

At this current time the SKWD and City of Sherrill have no immediate plans to implement individual cash accounts or cash drawers. The SKWD will however continue to enhance the control procedures already in place over the cash receipts process. The board will strive to build on the already individualized initialing process that all 3 clerks go through before they input the cash receipts into the computer system. Additional cross-check procedures will be considered within the next thirty (30) days such as notations of cash amounts received and or change given to further individualize the cash receipt process.

See
Note 1
Page 13

Recommendation Item #4: The Board should ensure monthly financial reports are generated in order to monitor the District's financial operations. These reports should include all District cash activity, budget to actual comparisons and cash balances

The SKWD agrees that receipt of such financial data reporting would enhance its oversight over the water district's financial position. The Board has the confidence in the Secretary's oversight and has periodically received such reports. To further ensure the Boards' management and oversight of the district's finances the district's Secretary will on a regular basis provide the Board with profit-loss statements showing budget to actual status of all accounts, revenue and expenditure. Additionally, copies of cash balances and bank reconciliations will be available formally for the Board's review on a monthly basis. The Secretary will

implement these new formal report provision steps within the next thirty (30) days and document the Boards receipt of them at their required regularity.

Recommendation Item #5: The Board should perform, or provide for, an annual audit of the District's records and reports.

The Board feels that it has already in place strong internal controls and mitigating procedures via the Secretary's oversight of the financial records. This recent NYSOSC audit goes further to confirm this fact through their audit testing and reconciling. However, the Board continually tries to strengthen in fact and in perception its required fiscal oversight of the Water District's affairs. In doing so it will consider implementing an independent public accountant's review of the districts records and discuss with the firm any perceived shortcomings (if any) and how to strengthen them or audit portions of the financial records if necessary. The Board will look to implement this independent public accountant's review at the end of the current fiscal year and perform such tasks on the 2012 financial statements.

In conclusion, the Sherrill-Kenwood Water District Board continues to be committed to the delivery high quality affordable potable water effectively and efficiently to its customers. We again thank the Office of the State Comptroller for its thorough review of District records and procedures. The Sherrill-Kenwood Water District Board looks forward to implementing the corrective actions listed above, thereby reinforcing oversight.

Sincerely

Sidney Thirumulpad
Chairman

PC. Michael Holmes Secretary
Robert Comis City Manager

APPENDIX B

OSC COMMENT ON THE DISTRICT'S RESPONSE

Note 1

User accountability is an integral part of internal controls and is virtually impossible to implement without separate user accounts and cash drawers. Assigning a separate cash drawer to each collector provides individual accountability over the cash received by that person. If an employee is stealing, separate cash drawers and individual accountability make it easier to trace the theft to the responsible party.

APPENDIX C

AUDIT METHODOLOGY AND STANDARDS

To achieve our audit objective and obtain valid audit evidence, we performed the following audit procedures:

- We interviewed District officials to obtain an understanding of the organization and the accounting system and to identify key personnel.
- We evaluated internal controls, including management oversight and segregation of duties, to determine whether duties and responsibilities had been established for officials and employees involved with maintaining the accounting records and collecting cash.
- We interviewed District officials and reviewed records and documents to determine whether adequate records were available, whether the Secretary provided monthly financial reports to the Board; and whether the Board annually audited or caused to be audited the records and reports of the water district.
- We examined customer billings, testing a random sample to determine that the billings are correctly prepared and supported. A sample of 30 water bills was randomly selected from the January 2011 and February 2011 billing cycles, totaling approximately \$1,388.
- We examined the tax roll of the City of Sherrill, selecting a judgmental sample of 50 properties to verify that all customers are being billed for water.
- We examined all 35 water account adjustments for January 1, 2010 through October 31, 2011 to determine whether the adjustments were appropriate.
- We reviewed journal entries, accounts receivable records and the trial balance detail for January and February 2010, and for May and June 2011.
- We examined daily water rent collections, bank statements and deposits for December 2010 and September 2011 to determine whether deposits were made timely.
- We reviewed the collection process of unpaid water rents and we verified that unpaid water rents for 2011 were relieved appropriately onto taxes for 2012.

We conducted this performance audit in accordance with generally accepted government auditing standards (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.

APPENDIX D

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