



Town of Jay

Internal Controls Over User Charges

Report of Examination

Period Covered:

January 1, 2011 — March 31, 2012

2012M-128



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

November 2012

Dear Town 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 Town 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 Town of Jay, entitled Internal Controls Over User Charges. 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 Town of Jay (Town) is located in Essex County and has approximately 2,500 residents. The Town is governed by an elected five-member Town Board (Board), which consists of the Town Supervisor (Supervisor) and four council members. The Board is responsible for the general oversight of the Town's operations and finances, including establishing appropriate internal controls to safeguard Town assets. The Supervisor is both the Town's chief executive and chief financial officer and is elected for a four-year term.

The Town provides various services to its residents, including road maintenance and improvements, snow removal, public improvements, recreation and cultural activities, water, sewer, and general government support. The Town's budgeted appropriations for the 2012 fiscal year are approximately \$2.32 million, funded primarily with real property taxes and user charges.

The Town has three water districts (Au Sable Forks, Jay, and Upper Jay) and one sewer district (Au Sable Forks-Jay), which provide water and sewer services to approximately 590 and 235 customers, respectively. The Town recorded water rent revenues of \$55,110 and sewer rent revenues of \$64,533 during the 2011 fiscal year.

Objective

The objective of our audit was to review the Town's internal controls over user charges. Our audit addressed the following related question:

- Are internal controls over user charges appropriately designed and operating effectively to adequately safeguard Town assets?

Scope and Methodology

We examined the Town's financial records and reports related to user charges for the period January 1, 2011, to March 31, 2012.

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 B of this report.

Comments of Local Officials and Corrective Action

The results of our audit and recommendations have been discussed with Town officials and their comments, which appear in Appendix A, have been considered in preparing this report. Town officials generally agreed with our recommendations and have initiated, or indicated they planned to initiate, corrective action.

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 Town Clerk's office.

User Charges

A well-designed system of internal controls over user charges requires that the Board establish written policies and procedures that provide guidance for individuals involved in billing users, collecting and depositing moneys received, adjusting user accounts, and reconciling outstanding user charges between control account balances and detail accounting records. The Board also must provide sufficient oversight of those officers and employees involved in these processes and ensure that an adequate level of segregation of duties exists between the employees involved with the billing, collecting, and recording functions related to user charges.

The Town did not have comprehensive written policies and procedures to provide adequate guidance and internal controls over water and sewer user charges and the Board provided only minimal oversight. As a result, we identified internal control weaknesses in the Town's billing procedures, account adjustments, deposits, and the reconciliation process for water and sewer user charges. For example, the Board has not formally adopted the water and sewer rates, adjustments are made to accounts with no support for the changes, collection dates for cash receipts are not documented, deposits are not made in a timely manner, and no one is performing a reconciliation of the water and sewer billing control accounts and the detail records. This increases the risk that the Town is not collecting all the user charge revenues it is owed, along with the possibility of fraud, abuse, and professional misconduct.

Billings, Adjustments and Deposits

The Board is responsible for formally establishing rates for all user charges. Also, the Board must establish written procedures to address the approval and documentation process for when billing adjustments are necessary. Each adjustment must be approved by the designated official who should adequately document its origination, justification, amount, and date approved. Additionally, when Town officials receive payments, it is important that they record the date of receipt. Good business practice requires cash and checks to be deposited daily, or as quickly as possible, to prevent the loss or misuse of cash. Furthermore, it is critical that Town officials deposit cash receipts intact¹ to reduce the risk of fraud and concealment.

The Town charges a flat rate to customers for water and sewer services. The Town bills for water services annually in August and for sewer services on a quarterly basis. Although the duties for billing and collecting user charges were adequately segregated, we found

¹ In the same amount and form (cash or check) in which they were received

other deficiencies in the Town's billing and collecting procedures. For example, Town officials could not provide us with documentation during our review that the Board had formally approved the water and sewer rate schedules that were being used. We also found adjustments to customer accounts are generally not approved by the Board and in numerous instances there was inadequate documentation to allow us to determine if the adjustments were for legitimate purposes. Furthermore, we found instances where deposits were not made timely or we were not able to determine if deposits were made timely due to the Town Clerk's failure to record when the collections were received for water and sewer billings.

We reviewed all 35 adjustments totaling \$5,706 that were made to customers' accounts during our audit period to verify that they were approved by the Board and supported by adequate documentation. We found that 34 of the 35 adjustments totaling \$5,663 were not approved by the Board. Additionally, for seven of the 35 adjustments totaling \$313, we could not determine if they were for appropriate purposes because they were not supported by adequate documentation. The failure to approve adjustments and include adequate documentation to justify the need for an adjustment creates a risk that customers may receive adjustments to their water and sewer billings to which they are not entitled.

We also examined a non-biased judgmental sample of 15 water rent and 15 sewer rent collections² totaling \$2,397 during our audit period to verify that they were deposited timely and intact. We found that all 30 collections were deposited intact. However, we could not determine if 28 of the 30 collections were deposited timely because the Town Clerk did not record the date the payments were received on the billing stub. For the two collections that the billing stub documented the date that the payment was received, we determined that the deposits were not made timely. Specifically, one payment was received on January 12, 2011 and was not deposited until 16 days later on January 28, 2011, and the other was received on January 14, 2011 and was not deposited until 33 days later on February 16, 2011. When the Town Clerk does not record the date that payments are received, Town officials cannot ensure she is depositing cash receipts in a timely manner.

Reconciliation of Control and Detail Accounts

An effective system of internal controls dictates that all individual user charges billed are posted to a receivable control account when billed; these control accounts, typically referred to as Water/Sewer Rents Receivable will contain a balance reflecting the total amount of unpaid water and sewer billings owed to the Town by customers.

² Appendix B contains our sampling methodology

It is important that, on a monthly basis, these control accounts be reconciled to the amounts billed, the amounts collected, and the remaining unpaid bills. This process provides a timely means to detect and correct posting errors, verify adjustments, account for returned checks, and verify that the Town's accounting records are in agreement with the detailed water and sewer billing and collection records. Without accurate and complete reconciliations, Town officials cannot have a reasonable level of assurance that the billings, collections and accounting records are accurate.

We found that the Clerk to the Supervisor did not properly maintain receivable control accounts in the Town's accounting records for the Town's three water districts and one sewer district. Specifically, when we compared the Town's water and sewer control account balances with supporting detail records from the water and sewer billing and collection software for a judgmental sample³ of three months during our audit period we found that:

- The water control accounts did not reconcile with the detail records for one month in our sample in which the control accounts had balances.⁴ Specifically, the combined total balance of the three water control accounts was a negative \$25,838 at month end September 2012, while the detail records had a positive balance of \$27,475, resulting in a variance of \$53,313.
- The Town's sewer control account did not reconcile with the detail records for any of the three months in our sample. For example, the sewer control account balance was \$18,549 more than the detail records at month end February 2012.

Because the Clerk to the Supervisor did not properly maintain water and sewer control accounts, she could not reconcile these accounts with supporting detail records from the water and sewer billing and collection software on a monthly basis. Instead, at year-end, the Clerk to the Supervisor adjusted the control account balances in the accounting records to agree with the listing of re-levied water and sewer accounts that was sent to Essex County. As a result, Town officials are not using the water and sewer control accounts as a means to ensure that billings and collections are properly recorded, which increases the likelihood that errors and omissions could occur and remain undetected.

³ Our judgmental sample consisted of the selection of May 2011, September 2011, and February 2012. Appendix B contains details of our sampling methodology.

⁴ The Town bills for water user charges on an annual basis in August, and thus the water control accounts did not have balances for two of the months in our sample (May 2011 and February 2012).

Recommendations

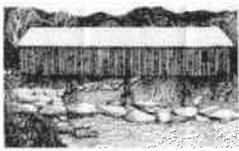
1. The Board and Town officials should establish written policies and procedures to provide adequate guidance and internal controls over billing, collecting, adjusting, and depositing user charges, and reconciling user charges between control account balances and detail accounting records.
2. The Board should formally establish and approve a schedule of water and sewer rates to be charged to customers for water and sewer services.
3. The Board should review and approve all adjustments made to customers' accounts and ensure that they are adequately documented, or designate someone independent of the billing and collecting of user charges to perform these functions.
4. The Town Clerk should record the date on the billing stubs when payments are received.
5. Town officials should ensure that collections are deposited in a timely manner.
6. The Supervisor should ensure that the Clerk to the Supervisor properly maintains water and sewer receivable control accounts in the Town's accounting records and that Town officials perform monthly reconciliations of these accounts with the supporting detailed records ensuring that any discrepancies are promptly investigated and resolved.

APPENDIX A

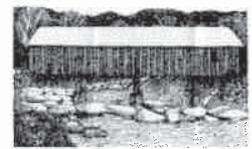
RESPONSE FROM LOCAL OFFICIALS

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

The Town's response letter refers to attachments that support the response letter. Because the Town's response letter provides sufficient detail of its actions, we did not include the attachments in Appendix A.



TOWN OF JAY



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September 18, 2012

Overall, the Town of Jay is pleased with the following Report of Examination conducted by the New York State Comptrollers Office for the period covered January 1, 2011 – March 31, 2012.

Our auditor was professional and thorough in their investigations as well as approachable and willing to lend his expertise.

Since becoming Supervisor of the Town of Jay, I have read numerous Audits conducted on various towns, villages and cities in an attempt to insure we are in full compliance of the New York State standards of the Comptrollers Office. Over the last nine years as Town of Jay Supervisor, I have worked alongside my Town Board and Administrative/Financial staff to make the Town more transparent and accountable to the taxpayers we represent.

In my opinion, the "Report of Examination(s)" tends to publicize the negative results of an audit, rather than highlighting all the day to day operations that are being done correctly. For example, the following information that the Town of Jay was initially required to provide to the NYS Comptrollers Office for thorough review were as follow:

Minutes

Annual Financial Reports

Records, Policies, and Other Documents

- Cash Receipts Journals
- Cash Disbursement Journals
- General Journals
- Revenue Ledgers
- Appropriation Ledgers
- Inventory Records for Gas, Fuel & Other Commodities
- Property and Equipment Inventory Records
- Bank Statements
- Canceled Checks
- Copies of Deposit Slips
- Bank Reconciliation
- Investment Policy
- Security and Custodial Agreements
- Confirmation of Pledged Collateral
- Duplicate Receipt Forms
- Purchasing Policy
- Code of Ethics
- Vendor Listing
- Purchase Requisitions/Orders
- Paid Vouchers or Claims
- Abstracts, Audits or Warrants
- Bid Specifications or Folders
- Record of all Indebtedness
- Payroll Records
- Certified Payroll
- Employee Time Cards
- Leave Time Records
- IRS Forms and Reports
- State Tax Forms and Reports
- Retirement Reporting
- Tax Cap Records
- Dump Ticket Sales

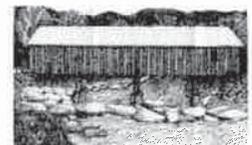
Electronic Information/Reports

- Payroll Data Fields
- Cash Disbursement Data

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- Cash Receipts
- Employee Master List
- Vendor Master List
- Customer List

Seven Departments were pre-audited in total; Supervisor, Highway, Justice, Town Clerk, Tax Collector, Code Enforcement, Water and Sewer. Each department was required to provide some of the above information that applied to their department and their daily duties.

Once the initial pre-audit of all departments and above material was conducted, the "Internal Controls Over User Charges" was the area that the auditor chose to further examine. The concerns that were expressed in the audit were similar concerns that were reported in an examination back in 1989 by the NYS Comptrollers Office.

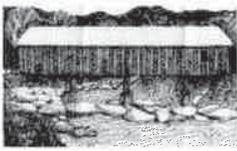
The Town of Jay Board was aware of the issues expressed in the current audit and had been making efforts over the last few years to correct and update the current policy on water/sewer charges and daily operations. These policies had been in place since the Water/Sewer Systems were built in the 1980's and 1990's.

We have made numerous changes but had not yet completed this department. Unfortunately, 2011 was a tough year for the Town of Jay and so many of the projects we were working on to improve were put on hold due to four disasters in our Township, including the devastation of Tropical Storm Irene.

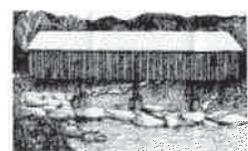
The Town of Jay Board's Response and Corrective Action Plan in regards to the current audit at hand is to establish updated written policies and procedures to provide adequate guidance and internal controls over billing, collecting, adjusting and depositing user charges and reconciling user charges between control account balances and detail accounting records at the January 2013 Organizational Meeting.

- The Town of Jay Sewer Committee Members, Town Supervisor, Clerk to the Supervisor, DPW Director and Water/SS Collector and Biller all met to discuss the Corrective Action Plan to review the above mentioned and to establish and approve a schedule of water and sewer rates to be charged to customers for water and sewer services beginning in 2013. (See attached sewer resolutions; 1A, 1B & 1C)
- The Town of Jay Water & Sewer Department has also developed a Property Owner Request for Change form which will be presented to the Town Board at their monthly meetings for approval starting January 2013. (see attached form; 2A) In the meantime, in order to make any adjustments residents or business owners must submit a request letter to be approved at the Town Board Meeting before any changes can be made. (see attached sample resolution, request letter & original bill; 3A, 3B & 3C)

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As suggested by the Comptrollers Office; the Board should review and approve all adjustments made to customers' accounts and ensure that they are adequately documented, or designate someone independent of the billing and collecting of user charges to perform these functions.

- The Town of Jay was in the practice of appointing two members of our Town Board to be on the Water/Sewer Committee at each year's Organization Meeting and whenever adjustments were made, one or both of the committee members were asked to review. However, our error was in not taking this procedure one step further by approving these adjustments by formal resolution as to document the procedure we had in place.
- The Town of Jay Board has been issued monthly reports from the Water/SS Biller since June 14th, 2012. The Town Board has made it their monthly practice to review and accept by formal resolution the following reports :
 - ❖ Billing Summary of Water/Sewer
 - ❖ Adjustment Summary of Water/Sewer
 - ❖ Penalty Summary of Water/Sewer
- The Town of Jay has also worked diligently with their Water/Sewer Software Programmer to develop reports suggested by our auditor. We can now generate penalty reports, journal entry reports by district, unpaid balance reports, receivables reports by date, district, etc. and adjustment reports by billing cycle. The system now automatically (versus manually) applies penalties to unpaid balances after 30 days.

The Town Board has asked the Town Clerk to record the date of when payments are received on the billing stubs, as suggested by the auditor.

The Clerk to the Supervisor has worked in conjunction with the Water/SS Biller and Collector on reconciling the control accounts to their receivable accounts to ensure that any discrepancies are promptly investigated and resolved. The new reports generated and updated from the Water/SS Software Program assist in this task.

In closing, the Town Board and I feel certain that the internal controls we had in place at the time of our audit and the ones recently implemented for "User Charges" per the NYS Comptrollers Office are adequately safeguarding the Town of Jay assets. Bottom line, with the continual changes in New York State practices of governmental accounting and policies; we feel that the Town of Jay has done an excellent job in effectively managing operations and in meeting the expectations of our constituents.

Sincerely,

Randall T. Douglas, Town of Jay Supervisor

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APPENDIX B

AUDIT METHODOLOGY AND STANDARDS

Our overall goal was to assess the adequacy of the internal controls put in place by officials to safeguard Town assets. To accomplish this, we performed an initial assessment of the internal controls so that we could design our audit to focus on those areas most at risk. Our initial assessment included evaluations of the following areas: control environment, accounting records, financial condition, budgeting, cash receipts and disbursements, deposits and investments, purchasing and claims processing, payroll, capital projects, and information technology.

During the initial assessment, we interviewed Town officials, performed limited tests of transactions, and reviewed pertinent documents such as Town policies, Board minutes, and financial records and reports. After reviewing the information gathered during our initial assessment, we determined where weaknesses existed and evaluated those weaknesses for the risk of potential fraud, theft and/or professional misconduct. We then decided upon the reported objective and scope by selecting for audit the area most at risk. We selected user charges for further audit testing.

To accomplish our audit objective and obtain relevant audit evidence, our procedures included the following:

- We interviewed Town officials, reviewed the Board minutes, the Town's Local Laws, and various financial records and reports related to user charges to gain an understanding of the internal controls over the billing, collecting, adjusting, depositing, and reconciling of user charges, and any associated effects of deficiencies in those controls.
- We reviewed all 35 adjustments that were made to customers' accounts during our audit period to verify that they were approved by the Board and supported by adequate documentation.
- We examined a non-biased judgmental sample of 15 water rent and 15 sewer rent collections during our audit period to verify that they were deposited timely and intact. We selected our sample of 15 water rent collections by starting with the first payment listed on the Au Sable Forks Water District paid report and then selecting every 25th payment, which we continued with the Jay Water District and Upper Jay Water District paid reports to obtain our sample. We selected our sample of 15 sewer rent collections by starting with the first payment listed on the first sewer district paid report for the 2011 fiscal year and then selecting every 54th payment, which we continued with the subsequent sewer district paid reports during our audit period to obtain our sample.
- We compared the Town's water and sewer control account balances with supporting detail records from the water and sewer billing and collection software for a judgmental sample of three months during our audit period to determine if they reconciled. We selected our sample by dividing the 15 months during our audit period by three, which would result in us selecting every fifth month during our audit period as our sample. As a result, we selected the fifth month during our audit period (May 2011) as the first month in our sample. However, we then selected September 2011 as the second month in our sample, instead of the next fifth month

(October 2011), because it fell within the middle of the only water collection period (August 1, 2011 to October 31, 2011) during our audit period. We then selected February 2012 as the third month in our sample because it was the fifth month after September 2011.

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.

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