



Town of Red House

Internal Controls Over Financial Records

Report of Examination

Period Covered:

January 1, 2009 — April 10, 2012

2012M-107



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

September 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 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 Red House entitled Internal Controls Over Financial Records. 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 Red House (Town) is located in Cattaraugus County and has a population of 38 residents. For the 2012 fiscal year the Town has an adopted budget of \$159,871, to be funded primarily with real property taxes and Justice Court fees.

The Town is governed by an elected Town Board (Board) comprised of four Board members and a Town Supervisor (Supervisor). The Board is responsible for oversight of Town functions, including fiscal and departmental activities. The Supervisor serves as the Town's Chief Fiscal Officer, and is responsible for maintaining financial records for the Town and for filing required reports timely.

Objective

The objective of our audit was to review internal controls over the Supervisor's records and reports. Our audit addressed the following related question:

- Are internal controls over the Town's financial records implemented properly and operating effectively?

Scope and Methodology

We examined controls over the Supervisor's financial records and associated reports for the period January 1, 2009 to April 10, 2012. We also reviewed the Town's 2008 annual report.

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 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 indicated they plan to take corrective action. Appendix B includes our comment on an issue in the Town'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 Town Clerk's office.

Financial Records

The Board is responsible for developing internal controls to help ensure that Town assets are adequately safeguarded and accounted for. The Supervisor is responsible for maintaining a complete set¹ of the Town's financial records in a manner that ensures the accuracy of the information for reporting and auditing purposes. The Supervisor is also required to file with the Office of the State Comptroller (OSC) a detailed report of all financial activity for the preceding year. This report provides the Board, OSC, residents, and others with a tool for monitoring the Town's financial activity. It is the responsibility of the Board to ensure that procedures have been properly implemented to provide assurance that the report is accurate and that it is submitted to OSC by the deadline. Additionally, the Board is required annually to audit, or cause the audit of, all departments which receive and/or disburse funds on behalf of the Town, including the Supervisor.

There is a lack of internal controls over the Town's financial records. Due to the Supervisor's lack of adequate record keeping, cash and bank balances do not agree, and the annual financial report has not been completed since 2008. In addition, the Board's inadequate annual audit of the Supervisor's records failed to note the inconsistencies.

Records and Reports — The Supervisor accounts for Town activity using electronic spreadsheets. A complete set of accounting records is not maintained, including a means by which to readily compare actual revenues and expenditures with budgeted amounts. In addition, only a check register is maintained to record trust and agency fund activity.

The Supervisor could not locate her records for the 2009 fiscal year. During our review of the records that were available, we found that the December 31, 2008 cash balances from the last annual report filed with our Office did not agree with the bank statements. We also found that her recorded cash balances² were approximately \$6,000 to \$14,000 less than the adjusted bank balances for the period reviewed. The Supervisor indicated that cash in the bank and the balances in her books had never agreed. Due to the lack of an adequate accounting system and the lack of 2009 financial records we could not determine the cause of all of the differences. We also found that the 2008 annual report filed with our Office did not include balances from the trust and agency fund.

¹ Financial records should include general and subsidiary ledgers and cash receipt and cash disbursement books.

² Adjusted for errors and omissions that we found while reviewing the Supervisor's records

While comparing recorded disbursements to canceled checks, we found six checks, dated between March and May of 2011, totaling \$18,390, payable to the Federal government, likely for payroll withholdings.³ However, that amount did not agree with available payroll information for 2010 or 2011.⁴ Some of the difference may be attributable to penalties that could have been imposed for untimely reporting or remittance to the Federal government. In addition, we found ten checks to a bank, all dated November 30, 2009, totaling \$6,570. The Supervisor failed to provide us with any documentation to support the purpose for these payments, including the Employer's Quarterly Federal Tax Return (Form 941), after repeated requests.

Further, we found that since the Town began filing its monthly Justice Court reports electronically, the Supervisor remitted payment to OSC more than 30 days after the date of the invoice from OSC for 11 of the 32 remittances we reviewed.

Annual Financial Reporting — As of the completion of field work on April 10, 2012, the Supervisor had not filed the required annual report for the fiscal years 2009, 2010, and 2011. When questioned why the report had not been filed in a timely manner, the Supervisor indicated that she encountered difficulties when attempting to file. Due to the Supervisor's employment commitments, her schedule did not allow us to assist her with questions that she had in filing the reports.

The lack of adequate accounting records and an adequate audit of her records by the Board could result in undetected errors and misstatements. Furthermore, not filing annual reports creates a risk that the financial condition and activity of the Town is not being properly monitored by the Board for indications of fiscal stress and/or improper activities.

Annual Audit — The minutes indicate that the Board audited the records of the Supervisor on an annual basis and note that they were found to be "in order." However, the minutes did not indicate the extent of the Board's audit. Board members stated that they compared check registers to bank statements.

³ We found no payments to the State for withholdings in 2010 and 2011, even though \$38 was withheld from Town employees' paychecks. Also, in 2009 a payment was made for State taxes in the amount of \$19; however, the total withholdings for the year were \$34.

⁴ 2011 Federal withholdings, Social Security and Medicare deductions totaled approximately \$3,700. This, along with the employer's share of Social Security and Medicare of approximately \$3,200, should have been the amount remitted to the Federal government.

During our review of the Supervisor's records, we found numerous instances where the records maintained by the Supervisor differed from activity noted on the bank statements. Therefore, we question the adequacy of the Board's audit of the Supervisor's records.

Recommendations

1. The Supervisor should establish and maintain an appropriate accounting system to properly record the Town's financial activity.
2. The Board should adopt policies and related procedures establishing an appropriate level of oversight with respect to the Supervisor's financial responsibilities.
3. The Board should review reports and payments to the Federal government to ensure that they are accurate and timely, to avoid errors in filing and late filing penalties.
4. The Supervisor should file annual financial reports with OSC for 2009, 2010 and 2011. The Board should consider obtaining assistance if the Supervisor is unable to complete them on her own.
5. The Board should refer to the OSC publications entitled *Local Government Management Guide* (specifically the section on Fiscal Oversight Responsibilities) and *Conducting Internal Audits of Cash Collection Activities* for guidance on performing the annual audit of the Supervisor's records.

APPENDIX A
RESPONSE FROM LOCAL OFFICIALS

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

TOWN OF RED HOUSE

Lonkto Road, Salamanca, NY 14779
716-354-5052

Town of Red House
Internal Controls Over Financial Records, Report of Examination
2012M-107

The following is a combined audit response letter and CAP in a single document.

The Town Board does agree with the findings stated in the audit for the Town of Red House covering 1/9/09-4/10/12. We do agree the Board has not conducted adequate internal controls to ensure our assets are safeguarded and accounted for. The Board has not conducted a complete annual audit of all departments which receive and/or disburse funds.

We also understand our Supervisor has not been maintaining a complete set of financial records, has not filed the annual financial reports for 2009, 2010 and 2011, has not reconciled records to bank statements, deposited monies timely or made payments to the Federal government.

Audit Recommendation

1. The Supervisor should establish and maintain an appropriate accounting system to properly record the Town's financial activity.
2. The Board should adopt policies and related procedures establishing an appropriate level of oversight with respect to the Supervisor's financial responsibilities.
3. The Board should review reports and payments to the Federal government to ensure that they are accurate and timely, to avoid errors in filing and late filing penalties.
4. The Supervisor should file annual financial reports with OSC for 2009, 2010 and 2011. The Board should consider obtaining assistance if the Supervisor is unable to complete them on her own.
5. The Board should refer to the OSC publications entitled: *Local Government Management Guide* (specifically the section on Fiscal Oversight Responsibilities) and *Conducting Internal Audits of Cash Collection Activities* for guidance on performing the annual audit of the Supervisor's records.

Implementation Plan of Action

The Board has planned to hire Tamara Booth to establish an appropriate accounting system to properly record the Town's financial activity.

Mrs. Booth will create a schedule for monthly use by the Board to review reports and payments to the Federal government and the Town's properly recorded financial activity.

Mrs. Booth will also attempt to recreate the financial records for 2008, 2009, 2010 and 2011 and properly file the required annual reports with OSC.

See
Note 1
Page 10

Mrs. Booth has requested and/or printed the recommended publications entitled: *Local Government Management Guide* and *Conducting Internal Audits of Cash Collection Activities*. A procedure will be created for annual reports audited by the Board. She will also make deposits and prepare payments in a timely manner.

Implementation Date:

Starting August 22, 2012 when all information is provided by the Supervisor to Mrs. Booth.

Person Responsible for Implementation:

Tamara Booth, reporting progress to the Town Board monthly.

Melissa Sipko
Supervisor

8/21/12

Date

Rita Sienkiewicz
Councilman

August 21, 2012

Date

Veronica Weber
Councilman

8-21-2012

Date

Brian Booth
Councilman

8-21-2012

Date

Tamara Booth
Councilman

8/21/12

Date

APPENDIX B

OSC COMMENT ON THE TOWN'S RESPONSE

Note 1

There are a number of potential problems with either contracting with a Board member or employing them directly. The Board should consult with counsel prior to taking this step.

APPENDIX C

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 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: financial condition, cash receipts and disbursements, Supervisor's records and reports, purchasing and claims processing, and payroll and personal services.

During the initial assessment, we interviewed appropriate Town officials, performed limited tests of transactions and reviewed pertinent documents such as Board minutes, bank statements, and available financial records.

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 on the reported objective and scope by selecting for audit those areas most at risk. We selected internal controls over the Supervisor's records and reports for our audit scope.

During this audit, we examined the Board's monitoring of selected financial operations and the filing and reporting by the Supervisor for the period January 1, 2009 to April 10, 2012. We extended our review to the report filed with OSC for the fiscal year ended December 31, 2008.

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

- We reviewed applicable laws governing the actions of the Town Board and specific report filing requirements.
- We interviewed Town officials to gain an understanding of policies and procedures related to the audit objective.
- We interviewed the Town Supervisor to gain an understanding of the process followed for maintaining records and filing required reports.
- We reviewed Board minutes and interviewed Board members to gain an understanding of the process conducted for the annual audit of the Supervisor's records.
- We reviewed annual activity reports prepared by the Supervisor, as well as associated bank activity and check registers.
- We reviewed payments filed with the Office of the State Comptroller for the remittance of Justice Court Funds.

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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DIVISION OF LOCAL GOVERNMENT
AND SCHOOL ACCOUNTABILITY

Andrew A. SanFilippo, Executive Deputy Comptroller
Steven J. Hancox, Deputy Comptroller
Nathaalie N. Carey, Assistant Comptroller

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