



Town of Berlin

Internal Controls Over Water District No. 2 Operations

Report of Examination

Period Covered:

January 1, 2013 — November 30, 2014

2015M-51



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

June 2015

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 Berlin, entitled Internal Controls Over Water District No. 2 Operations. 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 New York State 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 Berlin (Town) is located in Rensselaer County and has approximately 1,880 residents. The Town Board (Board) is the legislative body, which comprises an elected Town Supervisor and four elected members who are responsible for managing Town operations, including establishing internal controls over water operations. The Supervisor serves as the chief executive officer and chief fiscal officer, responsible for disbursing and maintain custody of Town money. The Board is responsible for the general management and control of the Town's financial affairs and has the authority to set the rates for water user fees. The Board, along with the Supervisor, share the responsibility for ensuring that internal controls over the Town's water districts¹ are adequate and working properly.

Water District No. 2 (District) includes 232 water customers² who are billed user charges based on the number of fixtures³ in their homes. The Water District clerk (clerk), who is appointed by the Board, is responsible for maintaining the Town's water customer accounts and for billing, receiving and recording payments, making bank deposits and making adjustments to water customer accounts. For the 2015 fiscal year, budgeted appropriations for the District totaled \$83,015.

Objective

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

- Are internal controls over District billings and collections adequately designed and operating effectively?

Scope and Methodology

We examined internal controls over District operations for the period of January 1, 2013 through November 30, 2014.

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.

¹ The Town has two water districts. Water District No. 1 is seasonal, operating from April through October and customers are billed for associated services on their property tax bills. Water District No. 2 operates throughout the year.

² According to the clerk's records

³ Such as the number of faucets

**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 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.

Water Operations

The Board is responsible for designing an adequate system of internal controls to safeguard Town resources. To meet this responsibility, the Board must implement policies and procedures that include adequate segregation of financial duties and must ensure that water user fees are properly billed, collected, recorded, deposited and accounted for. The Board is also responsible for annually auditing the clerk's records and reports.

The Board did not establish adequate internal controls over District operations. There is a lack of sufficient policies and procedures to guide employees in the performance of their jobs. The duties related to billings, collections and recordkeeping were not adequately segregated. In addition, the Board did not approve water billings or customer account adjustments or perform an annual audit of the clerk's records and reports. Furthermore, the clerk did not maintain adequate customer records or records of billings and collections. As a result, the Town may not be collecting all the revenue to which it is entitled.

Water Charges

A well-designed system of internal controls over water charges requires that the Board establish procedures that provide guidance and oversight for employees involved in the billing and collection of water charges to ensure water rents are accurately billed for, collected and deposited. This requires the segregation of incompatible duties or implementation of compensating controls when it is not feasible to segregate duties. Policies and procedures should require the maintenance of accurate and complete billing, collection and deposit records and a master list of water customers to be maintained independent of the clerk's records. In addition, the Board is responsible for approving all water billings and adjustments to water bills prior to the adjustments being made by the clerk.

The Town did not have comprehensive procedures to provide adequate guidance and internal controls over water charges and the Board provided minimal oversight of water operations. As a result, we identified significant internal control weaknesses in the Town's billing and collection procedures for water charges.

Segregation of Duties – Proper segregation of duties ensures that no one person controls all phases of a transaction and provides for the work of one employee to be verified by another employee in the course of his or her duties. Concentrating key duties with one individual (i.e., maintaining customer records, billing, collecting,

cash custody and reconciliations) with little or no oversight weakens internal controls and significantly increases the risk that errors or irregularities might occur and go undetected. If it is not feasible to segregate duties, Town officials must institute compensating controls such as enhanced management oversight.

There is a lack of segregation of duties over the billing, collection and maintenance of records for water charges. The clerk is solely responsible for the maintenance of customer records and the billing and collection process. Her duties include preparing the bills, collecting payments, preparing and making deposits, issuing and recording receipts, making billing adjustments, and creating, deleting and amending customer account files. The clerk performs her duties with no oversight from the Supervisor⁴ and does not provide the Supervisor with adequate documentation to support the deposits she makes for water collections. Instead, she provides him with duplicate receipts for amounts equal to the deposits she makes with no detail or support for the amount of the deposits. Furthermore, although the bookkeeper for the Supervisor records the District billing and collection activity in the centralized accounting records and reconciles the water fund bank account, the information used to perform these duties is based solely on information the clerk provides.

The lack of segregation of duties associated with the billing, collection and maintenance of records for water operations, coupled with the Supervisor's lack of oversight, significantly increases the risk that errors or irregularities might occur and go undetected. For example, the clerk could receive payment from customers and conceal the collections by making changes to the customers' water bills and water accounts without the knowledge of the Supervisor or Board members.

Billing Records – Town officials should maintain a master list of water district customers independent of the records maintained by the clerk to ensure that all water customers' accounts are accurately accounted for. The clerk is responsible for maintaining complete records of water rent billings as well as customer files. To become a District customer, a resident must complete and submit to the Town an application for water services. The application requires customers to document their name, address and the number and type of fixtures⁵ in their residences. The Town bills customers based on the number and type of fixtures reported to the Town on the customer applications.

⁴ For example, the Supervisor does not review changes to customer accounts (i.e., changes in the status of a property or changes in the number of fixtures located at a residence), billing registers, records of receipts and deposits or billing adjustments.

⁵ Such as the number of faucets, washing machines, etc., located on the property

The Board did not approve the master list of water customers and did not approve the addition to or removal of customers from the District. As a result, Town officials do not have a master list of water customers and the amount to be billed to each customer, independent of the clerk's records. Also, the clerk did not have applications on file for all customers who were billed. We found a total of 45 customers who were billed a total of \$9,280 in 2014 without an application for water services on file. The clerk could not explain why applications were not on file for these 45 customers but told us that, when properties receiving water services changed hands, she used the amounts previously billed to former property owners to bill the new owners. However we could not verify this practice because she did not adequately document such billings by maintaining records of notices sent to new property owners, documentation of a new owner's failure to return a completed application and the prior owner's application which she used to bill the new owner. Additionally, we compared the 2013 assessment rolls to the 2014 assessment rolls to determine whether the property owners changed for these 45 customers and found that the same residents owned the properties in both 2013 and 2014.

Furthermore, the Town does not have a process to verify the accuracy of the number and type of fixtures reported by customers, thus creating an opportunity for customers to not accurately report the number and type of fixtures in their residence, which would result in some customers paying less than what they should for water services.

We compared the clerk's records to the customer applications on file to determine whether customers were billed accurately. We reviewed 25 customers in 2013 who were billed a total of \$3,937 and 25 customers in 2014 who were billed a total of \$5,108. Except for minor variances, we found that 40 customers were billed accurately, based on their customer applications. However, for 10 customers who were billed a total of \$1,169, applications were not on file and, as a result, we could not verify if they were billed correctly. By not maintaining complete water applications for all customers, the Town lacks assurance that customers were billed accurately. Additionally, by not having an independently maintained list of District customers and amounts to be billed, we and the Town cannot verify that the clerk billed the full population of customers in the District.

Board Approval and Adjustments – Requiring prior Board approval of water billings and adjustments ensures that adjustments are made consistently and for appropriate purposes and reduces the opportunities for unauthorized adjustments or reductions in billings. Recording (in the minutes) the total amount billed not only informs the Board of amounts expected to be collected, but also provides the

basis for establishing accountability to those charged with collecting and reconciling amounts billed.⁶ It also helps prevent unauthorized changes to billing totals from occurring after bills are sent out.

The clerk did not provide the Board with a copy of the District's billing register for each of the quarterly billing cycles,⁷ which totaled \$51,691 in 2014. Also, the Board did not approve water billing adjustments made by the clerk or authorize her to make adjustments. The clerk adjusted water bills for various reasons, such as for a water main line that was shut off or for vacant properties.⁸ The clerk did not request Board approval prior to making the adjustments or provide the Board with a list of adjustments she made, and the Board did not request information related to adjustments. We reviewed 10 adjustments⁹ totaling \$1,253 that the clerk made to customer water accounts and, based on information provided by the clerk, the adjustments appeared to be for appropriate purposes. Without prior Board review and approval of all water account adjustments, there is a risk that customers may receive water account adjustments to which they are not entitled.

Collections – The clerk is responsible for maintaining adequate cash receipt records, which document the amount and form of payment received (e.g., cash or check) and the collection date. The clerk should use a detailed duplicate deposit slip to document that money collected was deposited intact. Such detailed receipt and deposit records should be maintained to ensure that all money collected is deposited timely¹⁰ and intact.¹¹

When residents pay water bills, they return a portion of their bill to the Town with their payment. The clerk used this portion of the bills to document the receipt of payment for the bills. However, when water payments were received, the clerk did not document the form of payment or the date of collection on the portion of the bill retained by the Town. Instead, she documented the date that she batched

⁶ In a small municipality with few people involved in the financial operations, the total amount to be billed for each quarterly period should be recorded in the Board's proceedings.

⁷ The Town bills its water customers quarterly in January, April, July and October.

⁸ The properties for which the water line was shut off were adjusted to \$0 and the vacant properties were adjusted to the minimum charge per the Town's water rules and regulations.

⁹ Random sample of adjustments made January 1, 2013 through November 30, 2014

¹⁰ New York State Town Law (Town Law) requires the Supervisor to deposit money received no later than 10 days after receipt. While the Clerk made deposits, the Supervisor is responsible for ensuring that they are made timely.

¹¹ Money deposited in the same order and form (cash or check) in which it was received

the payments to be deposited. Also, the clerk did not use duplicate deposit slips. As a result, we reviewed bank compositions for three bank deposits¹² totaling \$4,926 to determine if the deposits were made timely and intact. Because the clerk did not document the date of collection, we compared the date of the checks from customers to the bank deposit date.¹³ We found 40 checks totaling \$3,993 that were deposited between 10 and 56 days after the check dates and nine checks totaling \$479 that were deposited under 10 days after the check dates. The three deposits included six cash payments totaling \$454 for which we could not trace the date the cash was collected to the deposit date due to the clerk's failure to record the date of collection. Additionally, although we were able to trace the amount of customers' checks to their associated water bills for the six customers who paid with cash, we were unable to verify that their payments were deposited intact due to the clerk's failure to record the form of payment in her records.

Because the clerk did not record the dates payments were received, Town officials lack assurance that deposits were made timely. Moreover, by not recording the form of payments received and by not using detailed duplicate deposit tickets, the Town cannot ensure that collections are deposited intact.

Annual Audit

The Board is required to annually audit, or cause an audit of, the clerk's records and reports. The audit is an important internal control to verify that the records are maintained in accordance with established procedures, transactions are properly recorded and cash is 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 cause an audit of the clerk's financial records during our audit period. The clerk stated that the Board has never audited or caused an audit of her records. We spoke to one Board member who stated that no annual audit of the clerk's records has been performed and did not know that this should have been completed. Had the Board audited the clerk's record, they would have detected that the deposits were not timely. The Board's failure to perform the required annual audit diminishes its ability to monitor the Town's water operations and increases the risk that errors and irregularities could occur, go undetected and remain uncorrected.

¹² Selected randomly from January 1, 2013 through November 30, 2014

¹³ While the dates of the checks written by customers may not represent the dates that the clerk received the payments, because the clerk did not document the dates of receipt, we reviewed the check dates to gain perspective on the dates customers wrote checks to the clerk.

Recommendations

The Board should:

1. Establish policies and procedures to provide guidance to employees involved in the billing and collection of water charges.
2. Establish compensating controls to mitigate the risk associated with the lack of segregation of duties. The controls, at a minimum, should provide oversight procedures designed to reduce the risk of errors or fraud not being detected.
3. Institute procedures to ensure water customers' applications for water service are accurate, particularly the number and type of faucets reported on the application.
4. Implement billing adjustment procedures that require approval for all adjustments and that require written documentation of the reasons for such adjustments.
5. Ensure that Town officials create and maintain a list of water customers and amounts to be billed independent of the clerk's records.
6. Review and approve water district quarterly billing registers received from the clerk.
7. Perform an annual audit of the clerk's records and reports.
8. Ensure deposits are made timely in accordance with Town Law.


The clerk should:

9. Ensure that a water application is on file for each customer being billed.
10. Provide a quarterly billing register to the Board.
11. Maintain cash receipt records that document the date of receipt and form of payment.
12. Ensure that water billing adjustments are approved by the Board.
13. Prepare duplicate deposit slips to document the composition of each deposit.

APPENDIX A
RESPONSE FROM LOCAL OFFICIALS

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

May 27, 2015


NYS Office of the State Comptroller
Division of Local Government and School Accountability
One Broad Street Plaza
Glens Falls, NY 12801

Dear 

In response to your draft report titled Internal Controls Over Water District No. 2.

The Town Board will respond to this report and strengthen the controls of this operation, this will accomplished by creating written policy procedures .

Segregation of duties is not an option since the entire clerical budget for Water District No.2 is \$1,100 per year. Instead of segregation of duties we will implement compensating controls. It needs to be clearly recognized that the majority of our staff are part time workers.

The Town has just switched financial institutions and now has remote capture for checks which will provide for more timely deposits. It also provides detailed deposit accounting.

An annual audit will be performed by the Town Board.

Sincerely,

~~Robert C. Jaeger~~
Supervisor
Town of Berlin

Cc: Town Board

APPENDIX B

AUDIT METHODOLOGY AND STANDARDS

To accomplish our audit objective and to obtain valid audit evidence, our audit procedures for water operations included the following:

- We interviewed Town officials to gain an understanding of water operations; determine if the Town had adopted policies and procedures over water billing, collection and recording; and determine whether the water operation functions were adequately segregated.
- We randomly selected 10 water billing adjustments (five from 2013 and five from 2014) to determine if the adjustments were for proper purposes and authorized by the Board.
- We interviewed Town officials in order to gain an understanding of the reports provided by the clerk to the Board pertaining to water operations. We also interviewed Town officials to determine if Town officials had an independent list of water customers to compare against the clerk's records.
- We tested a total of 50 water customers (25 from 2013 and 25 from 2014) to determine if the amounts billed were correct compared to the customers' water applications.
- We obtained the deposit composition information for the deposits dated February 18, June 10 and August 26, 2014 from the Town's bank and compared the amounts billed and deposited to the clerk's collection report, the portion of the bills retained by the Town, the clerk's billing register, the deposit tickets and the bank statements to determine whether deposits were made intact and the timeliness of the deposits made.

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.

APPENDIX C

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