Nassau County
Office of the Comptroller
Field Audit Bureau

Financial Audit of
Sanitary District No. 2
Town of Hempstead

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OFFICE OF THE COMPTROLLER

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Background

In Nassau County, the county government is not responsible for collecting or disposing of solid waste from residents and commercial establishments. Instead, garbage collection in Nassau is arranged by the county's towns, cities, villages and, in some unincorporated areas not served by the towns, by a number of local, special "sanitary districts."[1] Local sanitary districts provide services only to residents and commercial establishments within their borders, and district expenses are paid for through local tax levies.[2]

Earlier this year, the County Assessor and others pointed out that the revenue raised and expenditures made by special taxing districts such as these sanitary districts occurred with little public scrutiny or governmental oversight. In response, our office undertook audits of the financial operations of a sample of Nassau's sanitary districts: The Port Washington Garbage District in North Hempstead; the Syosset Sanitary District in Oyster Bay, and Sanitary Districts 1, 2 & 6 in Hempstead. The sanitary districts in the sample generally maintained high tax rates or experienced large tax rate increases from 2004-2005 when compared to districts performing similar functions. Special sanitary district operations vary in size and complexity; some retain independent offices with fully equipped staffs while others share town administrative resources. In a few instances, districts contract with private haulers for refuse collection services.

This audit report reviews the financial operations of Sanitary District No. 2 (district), which employs administrative and operations staff to provide refuse collection services to 15,255 residential and 1,150 commercial parcels. The district provides curbside refuse collection service to residents and commercial properties three days a week. The cost of this service was $8,726,690 and $7,838,872 for the fiscal years ended 2004 and 2003 respectively. The district derives all of its operating revenues, other than interest earned on investments and grants, from real property tax assessments collected by the town of Hempstead and forwarded to the district semiannually.

Audit Scope and Methodology

The scope of our audit was limited to an examination of the district's administrative policies, procedures and expenses; procurement practices and contract monitoring; an analysis of operating costs and the appropriateness of its fund balance for fiscal years 2003 and 2004.

This audit was conducted in accordance with generally accepted government auditing standards. These standards require that the audit is planned and performed to obtain reasonable assurance that the audited information is free of material misstatements. The audit includes examining documents and other evidence to substantiate the accuracy of information tested, including all relevant records and contracts. It includes testing for compliance with applicable laws and regulations and any other auditing procedures

[1]Nassau County sanitary districts are governed by the New York State Town Law, the Nassau Civil Divisions Act, and the Nassau County Charter.
[2] Town Law Article 12 § 198.

necessary to complete the examination. We believe that the audit provides a reasonable basis for the audit findings and conclusions.

District operations are overseen by an active Board of Commissioners (Board) consisting of five commissioners, including the chairman who serves as chief executive officer; and the treasurer who serves as chief fiscal officer. The Board designates the banks or trust companies to serve as depositories for district funds, authorizes investments of district funds and approves claims for payment. In addition, the Board engages a certified public accountant to perform an annual audit and two legal counsels to handle the district's legal matters.

The board appoints the secretary to the board, and the district general supervisor and office manager, all of whom manage the district's day-to-day functions.

Receipts and disbursements are reported at each semimonthly board meeting.

Administrative expenses including, but not limited to, commissioner and administrative salaries and benefits, legal and professional expenses, and insurance totaled $ 1,387,154 for 2003 and $ 1,894,812 for 2004, or 18% and 22 % of total district expenses in 2003 and 2004 respectively. The district operates 19 routes and employs 5 route supervisors, whose base salaries range from $66,500 to $69,050 per year.

Cost Analysis of Operations

In Sanitary District No. 2, residential and commercial property owners paid an average tax levy per parcel of $694 in 2004 and $655 in 2003. Tax levies vary annually, based on district budgeted expenses and estimated use or accumulation of fund balances. The average taxes per parcel were higher than the $605 and $586 levy paid in 2004 and 2003, respectively, by residents and commercial establishments in the Town of Hempstead whose garbage is picked up by the town. The cost per ton for the district was $294 and $272 in 2004 and 2003 respectively compared to $241 and $238 for the Town of Hempstead. Both the Town of Hempstead and the district provide curbside refuse pickup service two times per week and recyclables pickup once per week.

Summary of Significant Audit Findings

Poor Administrative, Financial and Operating Practices – Lack of Internal Controls

The Board of Commissioners does not provide sufficient oversight to ensure that district administration, financial transactions and operations are efficient, appropriate, and in compliance with applicable laws and regulations.

We found that the district:

- does not have formal written policies and procedures for many of its accounting and operating functions; those that do exist are vague and need improvement;

- does not employ personnel with adequate financial or accounting expertise and relies too heavily on its external accountant;
- does not segregate duties, which increases the risk that errors or irregularities may occur and go undetected;
- appears to permit excessive personal or commuting use of district vehicles;
- does not have conflicts of interest rules or code of ethics to guide employees in making appropriate decisions; and
- does not always follow its procurement policy. In addition, its policy is incomplete, and not in compliance with General Municipal Law 103 and 104(b) public procurement requirements. For example:
    a. the policy does not provide adequate guidance or controls for purchases between $500 and $10,000;
    b. the policy contains no procedures for procurement of professional services; and
    c. the district does not maintain documentation of all quotations used as a basis for purchases.

Cash Disbursements

We found the district's manual cash disbursements process controls were poor and contribute to the vulnerability of the district's cash assets. We found payments for other than bona fide district expenses, duplicate payments, lack of supporting documentation, and weak controls over check signing authority.

Role of Insurance Broker

The district spent $2.2 million and $1.8 million for insurance in 2004 and 2003 respectively, which represents approximately 25% and 23% of total expenses for each year. We found that the district relies heavily on the advice and planning of its insurance broker, the Louis Koch Agency (broker). The broker is responsible for contracts relating to liability insurance, health insurance, and financing. The broker prepares the insurance components of the budget used to determine the tax levy, and also serves as administrator for the district's optical and dental insurance, as well as the district's workers compensation risk management program. As a principal of AMS Strategies, LLC, the insurance broker also participated in the transactions pertaining to the district's financing agreement and investment account. The structure of this financing agreement cost the district unnecessary interest expense. We found the district carries more insurance than seems necessary and pays more than necessary for the insurance it does need as a result of its total reliance on the broker. The district paid a $61,500 fee to the broker for its various roles in assessing, brokering and administering the district's insurance needs in 2004. For the two year audit period, the district's health insurance costs were $1.9 million; however health insurance costs would have been approximately $1.3 million if the district had insured with NYSHIP. We estimate that the district could have saved approximately $586,000 during the audit period by joining NYSHIP instead of the carrier selected by the commissioners based upon alternatives presented by the broker.

Personnel

The district's payroll expense for 2004 was $1,532,450 or 18% of total district expenses. Most district personnel are covered by one of three Collective Bargaining Agreements (CBA), but we found inconsistencies in the policies and practices that are applied to the commissioners, attorneys, and four top district management positions that are not covered by the CBA. They, along with district supervisors, are not required to file timesheets and, therefore, there is no validation of the time they spend working at the district. Of the two part-time attorneys, one was paid as both an employee and as an outside consultant. His income was reported to the Internal Revenue Service on both W-2 and 1099 forms. Because the two attorneys keep no time records—either as employees or consultants—it is impossible to conclude how much service they actually provide to the district. Nevertheless, the district's elected commissioners and two legal counsels are treated as full-time employees for the purpose of employee benefits. The district lacks formal employee benefit policies and appears to practice favoritism in the provision of benefits.

Appropriateness of Fund Balance

We found that the district's fund balance as of December 31, 2003 was $1,302,598 (the 2004 fund balance was not available as of the end of our field work) and appeared adequate to cover 7 weeks of expenses from the beginning of the year until the receipt of taxes but may not be sufficient to meet unforeseen expenses. The district does not appear to budget appropriately for expected itemized annual expenses. We found a lack of analyses of expenses from year to year, so that the district relies on its budgeted contingency account and fund balance to cover regular expenses it did not budget for in the proper accounts. Better budget controls are necessary so that the district has a fund balance at year end that is planned and takes into account a cushion for unforeseen district expenses.

Role of External Auditor

Government Auditing Standards, Amendment No. 3, Independence require that audit organizations evaluate the nature and significance of the nonaudit services provided to the audited entity and carefully consider the need to avoid situations that could lead reasonable third parties to conclude that the auditor is not able to maintain independence in conducting audits.

The standard classifies the auditor's role in authorizing and posting entity transactions and developing the draft financial statements as nonaudit services. It requires that the management representation letter include an acknowledgement of the auditor's role in this regard. It states that an external auditor cannot provide these services without impairing its independence to perform the financial statement audit. Further, it stresses the importance of the audited entity to make an informed judgment on the results of an auditor's nonaudit services.

We found that the auditor's independence may be compromised because the district relies too heavily on its external auditor to provide nonaudit services. We found that the district does not have adequately maintained books and records to support its financial statements and does not employ personnel with adequate financial and accounting expertise to evaluate and approve nonaudit services, such as the preparation of journal entries, the development of the annual financial statements and notes, and any adjustments or corrections that the auditor proposes. The district relies too heavily on its external auditor to prepare journal entries and develop the annual financial statements and notes without the appropriate oversight by the district. We also noted that the district does not have a policy to rotate its auditor, and that such a policy is designed to identify these issues.

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We recognize the cooperation afforded us by the district and commend it for the steps it is taking to improve and formalize many of its policies and procedures.

Sanitary District No. 2 Response

On August 26, 2005 we submitted a draft report to district officials with a request for comments. The matters covered in this report were discussed with officials of the district during the audit and in an exit conference held on August 29, 2005. The district's comments were received on September 12, 2005. The district's comments and our response to those comments are included as an addendum to this report (Appendix).

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Poor Administrative, Financial and Operating Practices – Lack of Internal Controls

While the district's policies "do not necessarily need to outline in specific detail each and every step of a particular transaction… [they] should provide guidance to help promote and maintain accountability."[3] The district generally lacks these guidelines for the employees and its operations.

Audit Finding (1):

Procurement of Goods & Services

The district's procurement policy lacks clear guidelines for district employees to follow. We found:

a. Lack of Competitive Bidding- Our review disclosed that the district did not comply with General Municipal Law 103 which requires that items costing over $10,000 be procured through competitive bidding. In addition, the district's policy does not clearly define the procurement process for purchases between $500 and $10,000. For example, competitive bidding was not done properly for technology purchases for $38,609.25 in 2003 and $54,543.97 in 2004. The district placed heavy reliance on one vendor to both assess its needs and provide the services. As of the end of field work, the technology purchased was not yet fully utilized. There was no evidence that the districts expenditure of $500 per month for the high speed communication line to transmit data was necessary for district operations.
b. Professional Services - The district's procurement policy does not address the solicitation of professional or specialized services. We found that the district does not attempt to rotate professional service firms and has used the same firms for legal, insurance, auditing, accounting and appraisal services for many years. For example the district has used the same labor counsel firm since 1979; the same insurance broker since 1978; and has been using the same external auditor since at least 1996.
c. Lack of Clearly Defined Roles and Responsibilities for Legal Counsel - The district treats its two attorneys as full time employees even though they maintain private practices, do not have space at the district and are not accountable for their time to the district. The district could not provide current documentation describing the specific duties and responsibilities of its two attorneys. The only documentation that exists is outdated retainer agreements, which support the attorneys' status as independent contractors rather than employees. The outdated retainer agreements were not signed by both parties, and did not include the specific responsibilities of the firm and/or individuals providing services to the district or the related fee structures.

[3] A Study of Cash Internal Control Practices for Local Governments in New York State, State of New York, Office of the State Comptroller, Division of Municipal Affairs , 2000-PS-5, pg.4

Audit Recommendations:

The district should:

a) ensure that all procurement is done in compliance with General Municipal Law Article 5-A sections 103 and §104(b). The district should be using the competitive bidding process for purchases that exceed $10,000. To avoid even the appearance of collusion, it should not permit the vendor assessing its technology needs to bid on technology purchase contracts for equipment it has recommended the district purchase;

b) periodically re-solicit proposals for professional service firms used for legal, insurance, auditing, accounting and appraisal services to allow for rotation and to obtain the best value;

c) require current retainer agreements, contracts and engagement letters for all professional services that detail services to be provided, and contain all the necessary signatures;

d) require an accounting of the hours professionals spend on district business in order to monitor contracted services; and

e) make a determination if the high capacity data transmission line is necessary to conduct the district's business, as opposed to a cheaper alternative, such as cable or DSL service.

Audit Finding (2):

Lack of Segregation of Duties

An effective internal control system requires the separation of duties so that no single individual controls most or all phases of a transaction. Concentrating key duties, such as authorization, recordkeeping and custody, with one individual weakens internal controls and significantly increases the risk that errors and/or irregularities might occur and go undetected and uncorrected in a timely manner. Equally important is that personnel with adequate financial and accounting expertise are employed to perform these duties. In addition to segregation of duties and qualified personnel, written job descriptions are important to establish clear day-to-day roles and responsibilities for each employee.

a) At the time of our review, written job descriptions either did not exist or were vague. The assignment of job duties among the administrative personnel did not provide adequate segregation of duties over financial transactions. We also found that the district does not employ personnel with adequate financial or accounting expertise and it relies too heavily on its external auditor.

b) The secretary to the board and the general supervisor can each individually initiate purchases, sign claim vouchers evidencing receipt, and also have the authority to make payments for goods and services. Although three board

members must also sign the claim voucher, each board member does not review each claim voucher in detail before signing and often relies on the signatures of the secretary to the board and the general supervisor to evidence the validity of the transaction.

c) The district has eight authorized signatories on its main disbursement bank account; these employees also have other approval authority in the purchasing and cash disbursement process.

d) The office manager was inappropriately authorized to sign checks. In addition to writing and signing checks, preparing the general ledger input data sheets, the office manager prepares bank deposits, executes wire transfers, prepares the semimonthly financial report to the board and reconciles the bank accounts.

e) General ledger data is manually entered on input forms by the office manager to be processed by the district's general ledger vendor. The input forms and the subsequent report produced by the vendor is not reviewed or approved by someone other than the office manager to ensure all data entered and reported is accurate and authorized.

Audit Recommendations:

The district should:

a) develop written job descriptions that clearly define roles and responsibilities, establish a proper segregation of duties and assign the duties to personnel with adequate financial and accounting expertise;

b) evaluate the necessity of eight signatories on the district's main disbursement bank account and remove approval authority in the purchasing, receiving and cash disbursements process from authorized signatories;

c) revoke the office managers' authority to sign checks;

d) require an employee other than the office manager to review general ledger input forms prior to submission to the general ledger vendor; and

e) require an employee other than the office manager to review the general ledger report to ensure that all data entered is accurate and authorized.

Audit Finding (3):

Lack of Budgetary Process

The board approved the use of $184,000 of district funds to purchase a building in late 2001. At the time of the purchase the district had a deficit of $330,000 (expenses exceeded tax levy). The building purchase was not in the district's budget as presented to the town and the transaction was posted to the contingency general ledger account. Our review of the board minutes revealed that the board had not noted a need for the building at the time it was purchased in 2001. In 2003, the district converted the building for use as office space for the district's accounting and administrative personnel. We were advised by the secretary to the board that this was done because the administrative and accounting personnel shared the same space with the road supervisors for approximately 3 hours per day (between 5 -7 AM and 12:30-1:30 PM). As of May 2005 the previous office space remains occupied by the 5 road supervisors for approximately 3 hours each day and is underutilized.

Audit Recommendation:

All district expenditures should be based on proper appropriations in the budget as presented to the town, and reported to the taxpayer. The district should not use the contingency general ledger account for other than emergency or unforeseen expenses.

Audit Finding (4):

Lack of Written Policies and Procedures

The district disbursed over $8 million in 2004 without having written policies and procedures for many of its accounting and operating functions and those that do exist are vague and need improvement.

The district lacks written policies and procedures for:

- establishing conflicts of interest and ethical standards;
- cash disbursements. There are no guidelines that define what constitutes proper supporting documentation and no established process to ensure proper review and vendor compliance with contracts, board approval or budgetary constraints. In addition, the district's practices do not include adequate controls to guard against the payment of unauthorized, unsubstantiated or inaccurate payments;
- credit card and petty cash usage;
- reimbursement for travel, meetings and conferences;
- telephone usage, including cellular and land line long distance; and
- inter-municipal agreement for fuel purchased for resale to three local fire departments and the Baldwin school district.

As a result we found:

a. payments for items that appeared to be employee gifts, not bona fide district expenses, including:
   - $3,344 for turkeys for all employees at Thanksgiving;
   - $955 for Christmas Breakfast; and
   - $1,358 for floral arrangements for employee bereavement.

b. Double payments:
   - In January 2004 the district paid for three deliveries of diesel fuel. Two of the deliveries were paid on delivery tickets instead of invoices. One of the payments of $3,732 for diesel fuel that was only supported by a delivery ticket was a duplicate payment of an item originally paid on an invoice. The district was unaware of the duplicate payment until the vendor issued a credit.

c. All checks written are not recorded in the general ledger. We found that a check for $2.1 million to transfer funds from one bank to another within the General Fund was not included in General Fund's list of checks written. In addition to the check not being recorded properly, it was not properly authorized because the check and the voucher did not contain sufficient signatures. The district's informal practice requires at least three commissioners sign all vouchers and that checks contain two authorized signatures. The office manager, who is responsible for all cash receipts and disbursements, was the only one that signed the check and only one commissioner signed the voucher.

d. no supporting documentation, or inadequate documentation, for meal, travel and miscellaneous expenses. These expenses appear unreasonable, lack a stated business purpose or are in excess of comparable state and county limits including:

   - $3,202 of various delicatessen food disbursements for board meetings;
   - $3,195 in travel expenses for a conference to New Orleans in 2003;and
   - $249 to a beverage distributor; and
   - Payments made on credit card purchases without detailed documentation such as the stated business purpose for the purchase of tables, chairs, and holiday decorations.

e. the distribution of cell phones to commissioners allowing for the use of 1,000 minutes per month;

f. payments for unexplained long distance charges that increased 47% from 2003 to 2004; and

g. fuel purchases for resale to other municipalities, when there is no contractual obligation for the municipalities to purchase the fuel from the district.

h. The following district policies lack clear guidelines for employees to follow:

- Procurement (see Audit Finding 1)
- The district's business meal policy is vague and does not cap expenses when the board adjourns to restaurants. For example, there was a $600 board meal at a restaurant in December 2004. This amount exceeded state and county spending limitations based on the number of normal attendees at the district's board meetings.
- Personal use of district vehicles (see Audit Finding 5)
- Investments

Audit Recommendations:

The district should:

a) adopt written, fiscally responsible policies and procedures to ensure that the district only spends taxpayer revenues on reasonable and necessary district expenses;

b) formalize a conflicts of interest policy and code of ethics as part of the district's operating procedures to guide employees in making appropriate decisions, deter wrongdoing and to encourage honest and ethical conduct;

c) promulgate cash disbursement policies and procedures to include the specific steps that must be performed when reviewing a claim voucher for accuracy, completeness, and compliance with contractual, board approval and budgetary requirements. The procedures should include descriptions of what constitutes acceptable supporting documentation, as well as how to document the steps that were done, by whom and when;

d) make payments only when supported by an original invoice to prevent duplicate payments;

e) maintain a vendor history file and file their paid invoices by vendor to avoid duplicate payments to vendors. Filing by vendor enables the district to research prior payments;

f) ensure that all required approvals and check signatures are obtained on checks written to transfer funds between bank accounts;

g) require adequate documentation and review vouchers to ensure that the expense is reasonable and necessary to the operation of the district; and

h) set limits for what it will spend on bona fide district travel expenses.

Audit Finding (5):

Personal Use of District Vehicles

The district's Vehicle Usage Rules date back to 1984 and permit eight district vehicles to be used by certain employees for commuting to and from work, and three district vehicles to be used by three management staff for personal use. The district imputes a taxable income value to its employees for the use of all 11 vehicles. The district pays for all fuel, repairs, maintenance and insurance. For the eight vehicles used by the supervisors (five sanitation, one automotive and two code enforcement) the district permits the personal use of district vehicles to commute to and from work only. The district imputes a taxable income value of $3 per day commuting cost, for each day the employees report to work. Base salaries of the district supervisors, including the two code enforcement supervisors, range from $66,501 to $69,049; seven are given the use of pick-up trucks and one code enforcement supervisor is given the use of a Ford Explorer. The district justified this policy as follows:

- Supervisors are on call all day and night;
- Supervisors respond to urgent problems at any time; and
- Supervisors monitor stops, collection points at night, during weekends and holidays.

We requested the district's documentation evidencing the dates and hours worked by supervisors during nonbusiness hours to support the need for use of district vehicles. The district provided memorandums prepared by one code enforcement supervisor that documented his activities during nonbusiness hours. The district also provided copies of "Week-End Work Chits" for the other code enforcement supervisor, which detailed dates and hours worked, but which did not include any details as to the nature of the work performed. Our review disclosed that the code enforcement supervisors worked nonbusiness hours about one day per month. There was no evidence that full-time commuting use of the vehicles by supervisors was warranted.

In 1992, the Board granted personal use of three additional district vehicles, to the secretary to the board, the recycling coordinator and the general supervisor, in lieu of a raise as "a course of action that would enable the Board to keep any future budget increases to a minimum" (1992 Board minutes). The district imputed taxable income of $6,100 per year to these three employees' gross wages for personal use of these vehicles. The total gross wages for these three positions includes the imputed value for the use of a Ford Explorer by each and ranges from $103,819 to $126,215. (The base salary component of the total gross wages for these three positions range from $83,467 to $99,857.)

Our review disclosed that:

a) There are no controls in place to monitor the gas usage or the mileage for these vehicles to ensure compliance with district policy;

b) All vehicles have removable identifying magnetic district seals. The removal of the seal by the operator hinders the ability of the district to monitor compliance with policy;

c) The charge of $3 per day likely undervalues the benefit to the employee. The lack of monitoring of gas and mileage for these vehicles makes it undeterminable if the imputed cost is appropriate for the nonbusiness related usage of the vehicles by employees;

d) The district does not monitor the actual cost of personal and business use of vehicles granted to the Secretary to the Board, Recycling Coordinator and the General Supervisor and therefore an analysis that supports the premise that "budget increases will be kept to a minimum" by granting personal use of district vehicles cannot be done;

e) The imputed value of $6,100 per year for personal use and $3 per day for commuting use of district vehicles was determined by the external auditor based upon vehicle depreciation only and may be understated. It does not include gasoline, maintenance, repairs and insurance expenses also paid by the district; and

f) The necessity of the use of district vehicles by all these employees is questionable.

Audit Recommendations:

The district should:

a) Impute value to the employees based on a formula that takes into account all vehicle related costs.

b) Establish procedures to monitor the gas usage and the mileage for personal use of district vehicles to ensure:
   - compliance with district policy;
   - the premise that budget increases are kept to a minimum by the granting of personal use of district vehicles is valid; and
   - the accurate determination of imputed value.

c) Reevaluate its policy of allowing supervisors to use district vehicles for commuting and personal use within the district.

d) Affix permanent district seals to all district owned vehicles to facilitate district monitoring and allow district residents to observe how the vehicles are being used.

e) Develop and implement a formal process to record and track the nonbusiness hours worked, as per the memorandums submitted by the two code supervisors.

Audit Finding (6):

Role of Insurance Broker

The district spent approximately $2.2 million and $1.8 million for insurance in 2004 and 2003 respectively, which represents approximately 25% and 23% of total expenses for each year. We found that the district relies heavily on the services of its insurance broker, the Louis Koch Agency (broker) without apparent benefit. The broker also appears to have a conflict of interest in the services it provides to the district: the broker assesses the insurance needs of the district, creates the district's insurance budget, brokers all policies and administers some of the district's insurance plans. The policies are not periodically bid out so that the district is ensured of getting the best value. Moreover, the district may be over insured or insured for risks that do not exist in the district. For example:

- District policies note $50,000 coverage for damage or loss of fine arts and $50,000 coverage for installment or deferred sales. We did not observe fine arts at the district, and the district does not have any installment or deferred sales.
- Lesser of actual loss sustained for 30 days or $100,000 coverage for websites and communications services. The district's website is not integral to the district's operations. It was not clear what type of communications services that were covered or an event that would give rise to a claim under this line of coverage.

The higher the district's premium, the higher the fee paid to the broker from the carrier.

In addition to any commissions paid by the insurance carriers, the broker was paid fees by the district totaling $61,500 in 2004 as follows:

- $12,000 administration fee for dental plan and $3,000 administration fee for optical plan-No bidding was done to determine the nature and cost of administrative services available elsewhere. In 2004, the $3,000 administrative fee for the optical plan exceeded reimbursements to employees of $2,700. As administrator, the broker maintains district check stock to reimburse the employee or pay providers directly and does not issue reports on the insurance activity to district management as specified in the contract.
- $40,000 risk retention fee for worker's compensation plan-the broker is responsible for monitoring and reducing risk associated with worker's compensation claims for the purpose of keeping premiums down. Instead, the district's worker's compensation premium costs increased 53% from 2003 to 2004.
- $6,000 administration fee for worker's compensation plan in addition to the $40,000 risk retention fee.
- $500 administration fee on Employment Practices Liability Insurance-it is not usual for the broker to collect a fee from the insured; fees are usually received from the carrier.

Although the district compensates its broker to oversee its insurance needs, the district was unaware that it is entitled to offer its employees health insurance under the New York State Health Insurance Plan (NYSHIP). For the two year audit period, the district's health insurance costs were $1.9 million; however health insurance costs would have been approximately $1.3 million if the district had insured with NYSHIP. We estimate that the district could have saved approximately $586,000 during the audit period by joining NYSHIP. It is common practice for private health insurers to pay brokers commissions; however NYSHIP does not pay commissions.

Audit Recommendations:

The district should:

a) issue a request for proposals for a consultant to review the district's insurance coverage. The consultant should review the coverage, insurance administration and the broker's recommendations for, among other things, possible conflicts of interest.

b) obtain a better understanding of its insurance policies and coverage and contracts with the broker;

c) evaluate the use of alternative insurers, such as NYSHIP, for health insurance coverage;

d) request an accounting of all expenses paid out of the dental and optical plans, along with the cumulative total by employee for each check run. This will provide the district with assurance that total payments for services do not exceed the maximum benefits for the year; and

e) require the broker to supply the management reports specified in the dental and optical insurance contracts and management should review them to ensure that insurance is efficiently obtained and administered.

Audit Finding (7):

Broker's Role in Lease/Purchase Agreement

The district's insurance broker's principal is also the principal of Advanced Management Strategies, LLC (AMS), the company the district used to obtain its $1,000,000 Equipment Lease/Purchase Agreement. AMS was paid $20,000 to obtain and evaluate financing proposals. Proper procurement procedures were not followed. The district relied too heavily on its vendor to determine the district's need for financing.

Further, the Lease/Purchase Agreement was disadvantageously structured for the district. The Lease/Purchase Agreement called for the full $1,000,000 to be drawn down at inception and invested through an escrow account until funds were needed. The district was therefore paying for the loan unnecessarily before using the proceeds. The net effect of the interest on the loan and the interest income from investments was an interest expense. Although the initial investment decisions for the loan proceeds were made by the district, all subsequent investment decisions were made by the broker. The Lease/Purchase Agreement was entered into in 2002 and as of March 17, 2005, the district was still paying interest on $131,999 that it had not used to acquire assets. The district may also have misled the lessor as to the purpose of the financing. The district specifically stipulated in the lease that the funds would be used to finance building improvements that would not be affixed to the building or be permanent. Neither of these warranties was true. Instead the district purchased a delicatessen and converted it into office space, a permanent conversion.

Audit Recommendations:

The district should:

a) request financial institutions to bid on financing proposals and discontinue the use of an outside firm to obtain bids for a fee;

b) exercise budgetary restraint and borrow funds only when needed;

c) should not hide the true nature of a purchase;

d) review its funding needs and consider negotiating a partial prepaying of the lease if the unused funds are unneeded and financially advantageous terms can be negotiated; and

e) ensure that all investment decisions are made by district management.

Personnel

Audit Finding (8):

Time Records are Not Kept for All Employees

The district does not keep a daily record of the hours worked, including starting and ending times, for any of its 20 managerial and supervisory employees. These employees include the district's five commissioners, two legal counsel, four managers and nine supervisors. Daily time records are necessary for the district to determine the employees' regular and overtime hours. The time records should encompass each employee's entire workday, including starting times and ending times. This lack of proper time records inhibits the ability of the district's management to oversee district operations.

The Collective Bargaining Agreements define sanitation workers' work day as 10 hours per day, four days per week. It also states that the sanitation workers shall work until the sanitation routes are completed, unless otherwise directed by management. The district maintained time records for these workers and a review of time clock records revealed that the average work day is four to five hours per day, not 10. We also observed that most Unit II supervisors were not at the district for the 10 hours that their CBA requires. Many of them leave the district after 6-7 hours. Based upon hours worked, we found that sanitation workers were being paid an effective rate of about $58 per hour and supervisors were being paid about $62 per hour.

Audit Recommendations:

The district should require all employees, including management to record their time daily, including starting and ending times, in order to provide more accurate oversight of district operations.

Since sanitation workers are working only four days a week and completing their routes after only four or five hours, the district should consult with labor counsel about extending or combining routes.

Audit Finding (9):

Improper Reporting of Certain Employees for New York State Retirement System, Internal Revenue Service, Civil Service and Employee Benefits Purposes

a. The district reports four of its five commissioners as full-time district employees to the New York State and Local Retirement System (NYSERS). The only record of time spent on district business by the commissioners is the record of their attendance at the district's semimonthly board meetings. We saw no other evidence to substantiate full-time employment. Two commissioners reported as full-time to NYSERS are also full-time employees of the Baldwin Fire District. The commissioners are paid $7,500 per year.

b. The commissioners and the two attorneys also receive health insurance benefits as if they were full-time employees at a cost of $108,300 during the audit period. Neither the commissioners nor the attorneys have a defined work week, are not required to, and do not, report their time worked, and do not have offices at the district. District practice for all other employees is that part-time employees do not receive benefits.

c. The district is required by Civil Service Law to obtain civil service approval to establish and fill each position at the district. In addition, the district is required to file a salary plan, for approval from the Nassau County Civil Service Commission (Commission), for each position. Annually the district is required to certify its payroll to the Commission. The Commission then reviews the district's submitted, certified payroll to ensure that the salaries agree and fall within the range on the approved salary plan filed with the Commission. The district reported some remuneration to its labor counsel on an IRS form W-2 and some on an IRS form 1099. Since the civil service payroll certification only reflects moneys that were paid through the payroll system, and therefore reported on the W-2, it will not reflect the additional amounts reported on the 1099. The additional amounts reported on the attorney's 1099 fell outside the salary plan submitted to the Commission and circumvented civil service approval.

d. The district did not establish a justification for reporting payments to the labor counsel as both an employee and a consultant on IRS forms W-2 and 1099. The outdated agreement between labor counsel and the district does not make clear what services are as an employee and what services are as a consultant.

e. We found that the board did not comply with civil service law when the board established an in-house recycling coordinator position in 1986 to help create its recycling unit.

    1. The board minutes reflected that the in-house recycling coordinator position created in 1986 was temporary and would report through the general supervisor. The position was not submitted to the Commission for approval, was not covered under the union contract for recycling workers and was not

posted; a sanitation supervisor was appointed to the in-house position by the board.

As of December 31 2004, 18 years later, the in-house recycling coordinator position was still being reported to the Commission as a sanitation supervisor at an annual base salary of $83, 967, which is approximately $15,000 over the maximum salary per the union contract.

2. In January 2005, we were advised by the current secretary to the board that the temporary recycling coordinator position that existed for 18 years at an annual base salary of $83, 967 as of December 31, 2004 was no longer needed and was eliminated.

Audit Recommendations:

The district should:

a) maintain time records for district commissioners and attorneys in order to substantiate full-time status of district commissioners and document time worked as reported to NYSERS;

b) reevaluate the practice of providing health benefits to attorneys and commissioners;

c) follow IRS regulations in determining whether its labor counsel should be considered an employee and receive a W-2 or a consultant and receive an IRS form 1099 for IRS reporting purposes;

d) formally establish and document work week and time reporting requirements for all nonunion workers and employees not covered by a CBA;

e) require all employees of the district to record their time on a daily basis; and

f) follow Civil Service Law in the establishment and hiring for all district positions.

Audit Finding (10):

Lack of a Formalized Benefits Plan for all Employees

The district provides health, dental and optical insurance to all full-time employees and some part-time employees. Under Federal law, it is also obligated to offer continuation of health coverage under the Consolidated Omnibus Budget Reconciliation Act (COBRA). We found that the district does not have a formal policy on employee fringe benefits and its current practices suggest favoritism in the provision of benefits. For example:

- The district's practice is to provide group term life insurance to all full-time employees and to end coverage upon retirement. However, the district provides group term life insurance coverage to its commissioners and its two attorneys who do not work full-time at the district. With the exception of one commissioner who receives a $5,000 policy, all commissioners and attorneys receive a $50,000 policy at a total cost to the district of $3,600 per year. In addition, the board resolved in 2004 that the district assume the life insurance payments for the former Secretary to the Board upon his retirement in 2005.

- Although the district's policy requires that employees hired after 1986 contribute toward benefits coverage, one commissioner and one attorney hired after 1985 did not contribute. This resulted in an unnecessary cost to the district of $5,300 during the audit period.

- The district's former labor counsel was allowed to remain on COBRA for 36 months until his death in 2003, 18 months more than the federal allowable guidelines.

We were unable to perform a review of the employees' personnel records to determine the accuracy of the records because we were denied access by the current secretary to the board on the advice of counsel.

Audit Recommendations:

The district should establish and adhere to a written, evenhanded policy that does not permit favoritism for:

a) the provision of life insurance to district employees;

b) enrollment of employees in health benefits and the contributory nature of the enrollment; and

c) provision of COBRA coverage.

Audit Finding (11):

Appropriateness of Fund Balance

The Office of the NYS Comptroller conducted a study of unreserved and unappropriated fund balances in selected water, fire and sewer districts in Nassau County for the period January 1, 1998 through December 31, 2000. The study indicated that "recent changes in state Law and prudent budgeting practices allow a "reasonable" amount of unreserved fund balance to be retained to ensure the orderly operation of the district and continued provision of services."

We found that the district's failure to establish adequate budgetary controls and exercise appropriate levels of fiscal restraint has led to an unreserved and unappropriated fund balance of $1,302,598 at December 31, 2003 that appeared inadequate. (2004 financial statements were not available as of the end of field work). This is because the district's average monthly expenses were $730,910 from January through April 2004 and the fund balance at December 31, 2003 represents the equivalent of only seven weeks expenses, which coincides very closely with when the district receives its share of the tax levy each year (around February 25). Therefore, while the fund balance at December 31, 2003 might be enough to meet the district's existing spending levels until the tax revenues are received, it may not be sufficient to meet unforeseen expenses.

The district does not appear to budget appropriately for expected itemized annual expenses. We found a lack of analyses of expenses from year to year, so that the district relies on its contingency account and fund balance to cover regular expenses it did not budget for. The district posts expenses to accounts in a surplus position, or directly to the contingency general ledger account, rather than to the appropriate general ledger account to avoid showing individual expense types as exceeding budget. Better budget controls are necessary so that the district has a fund balance at year end that is planned and takes into account a cushion for unforeseen district expenses.

Audit Recommendations:

The district should develop a formal budgetary control policy which:

a) includes the maintenance of a sufficient fund balance to meet its operating expenses for the first six weeks of the following calendar year (due to the timing of tax receipts) and any unforeseen increase in district expenditures;

b) requires all budget transfers be formally reviewed and approved by the board;

c) revisits the need for a contingency general ledger account, and if still deemed necessary, that it only be used for non routine emergency expenses, which are formally approved by the board in advance. The budget for this account should be justified and the nature of the actual expenses reported in this account should be fully explained in the audited financial statements;

d) requires that expenses can only be paid after a review is done and documented to indicate that budgetary limits are not exceeded, including a notation of the general ledger account where the funds are budgeted; and

e) prohibits the practice of posting expenses to a general ledger account in a surplus position, or directly to the contingency general ledger account, rather than to the appropriate general ledger account in order to minimize over budget conditions.

Audit Finding (12):

Role of External Auditor

Government Auditing Standards, Amendment No. 3, Independence [issued January 25, 2002] require that audit organizations take a “substance over form” approach and consider the nature and significance of the services provided by the external auditor and carefully consider the need to avoid situations that could lead reasonable third parties to conclude that the auditor is not able to maintain independence in conducting audits.

The Standard classifies the auditor’s role in authorizing the client's transactions, posting transactions to an entity’s financial records or to other records that subsequently provide data to an entity’s financial records, and developing the draft financial statements as nonaudit services. It requires management's representation letter to include an acknowledgement of the auditor's role in this regard. The standard states that an auditor cannot provide this service without impairing its independence to perform the financial statement audit. Further it stresses the importance of the audited entity to make an informed judgment on the results of the auditor's nonaudit services. The audit organization must ensure that the management-level individual designated to oversee the nonaudit services has the necessary qualifications to conduct the oversight needed.

The apparent lack of independence of the external auditor and its possible impact on the value of the audited financial statement, combined with the lack of financial expertise of employees, raises concerns that there may be insufficient fiscal oversight of district operations.

We found that the district does not have adequately maintained books and records to support its financial statements and does not employ personnel with adequate financial and accounting expertise to evaluate and approve nonaudit services, including any adjustments or corrections that the auditor proposes. The district relies too heavily on its external auditor to prepare journal entries and develop the annual financial statements and notes without the appropriate oversight by the district. As a result, the district was not aware that the 2003 financial statements compiled by the auditor contained errors, such as the undervaluation of fixed assets by $104,000. We also found that neither the audit engagement letter nor the management representation letter states the role the auditor performed in providing these services.

We also noted that the district does not have a policy to rotate its auditor, and that such a policy is designed to identify these issues.

Audit Recommendations:

The district should:

a) employ personnel with adequate expertise to coordinate and understand the audit work performed and oversee and evaluate the nonaudit services provided;

b) adopt a policy to rotate its external auditor periodically; and

c) require that the engagement letter and management representation letter cover all audit and nonaudit services to be performed by the auditor. The roles of the district and the auditor with respect to nonaudit services should be clearly defined to prevent a lack of independence on the part of the external auditor.

Audit Scope and Methodology

District Response:

The scope of audit went well beyond the stated "focus" in the letter from the Comptroller dated February 24, 2005 at which time you indicated you intended to examine the District's "administrative and operating expenses, procurement practices and fund balances". There was no mention that there would be an all-encompassing procedural audit that included requests ranging from what time does the mail arrive and who opens the mail, to requests for personnel files, and protected OSHA logs. The audit which included thirty six (36) full days of an on site field audit, on occasion employing more than ten auditors, unknown staff support and approximately seventy (70) days to prepare a draft must have cost the County an enormous amount of money and man hours.

The District's daily operations vary from day to day and season to season. On a normal day the District deploys eleven (11) route trucks; one (1) municipal truck, which picks up schools, churches, synagogues, apartment house, post offices, etc; two (2) compost trucks; and one or two special item bulk trucks. In addition the District, on a daily basis, deploys four (4) recycling route trucks, one (1) plastics truck, one (1) or two (2) special metal pick up trucks. During the fall months, several additional compost trucks are deployed enabling the district to provide unlimited leaf collection. Likewise in the spring, extra special bulk items trucks are utilized to facilitate spring cleanups.

Auditor's Follow-up:

During the course of the audit, the audit team explained to the district that the goal of a financial audit is to obtain reasonable assurance that the financial reports being audited are reliable. The Government Finance Officer's Association publication Government Accounting, Auditing, and Financial Reporting states that "Auditors use a variety of means to obtain the evidence they need to provide such assurance. Auditors inspect relevant documentation, observe employee performance, inquire concerning policies, procedures, transactions, and events; confirm balances and transactions with outside parties; and perform analytic procedures to determine the reasonableness of transactions and balances. Personnel files were requested as part of our test of payroll expenses and we did not request protected OSHA information; the information we requested was part of our review of workers' compensation expenses. For most of our fieldwork, the audit team consisted of a maximum of four auditors. The time it takes to perform an audit depends on several factors, including auditee cooperation, availability of documentation, degree of computerization of data, and access to personnel. Our first consideration is performing a quality audit that produces reliable information.

Cost Analysis of Operations:

Tax levies are calculated, by each entity, on budgeted expenses and applied fund balances, and are also based in a large part on monies available to the taxing entity from taxable property valuations. Two Districts with identical budgets but with different

taxable property valuations will have different tax levies. The District with higher taxable property valuation will have a lower tax rate. The audit findings in regard to per ton costs do not identify collection districts serviced by the Town of Hempstead nor does it indicate if the taxable valuation is comparable to our District. The comparison to the differing tax rates of the Town of Hempstead and the District is certainly misleading and in our view beyond the stated scope and purpose of the audit. The audit finding also incorrectly implies that the level of service provided by the Town of Hempstead and the District are the same.

Auditor's Follow-up:

This information was provided as background rather than as an audit finding. The background information did not compare the district's tax rates to those of other districts; rather it compared the average tax levy (the average amount paid by the property owner) for property owners in the district to the average tax levy paid by those property owners serviced by the Town of Hempstead. The cost of picking up and disposing of each ton of refuse is a measure of the efficiency of the district. These costs can be compared and are independent of property values. The levels of service are not a significant factor in causing cost differences because in the district and the Town of Hempstead the level of service is similar.

Summary of Significant Audit Findings

The Board of Commissioners disagrees with the statement that it does not provide sufficient oversight to financial and operation concerns. There were absolutely no findings by the auditors of any fraudulent, intentional, or malicious misappropriation of any District funds. A Senior Account Clerk, a Nassau County Civil Service competitive title and two competitive accounts clerks oversee the District's finances, and report to the Secretary to the Board. This audit does not take into account that the concept of reasonable assurance recognizes that the cost of a system of internal accounting should not exceed the benefits derived and also recognizes that the evaluation of those factors necessarily require estimates and judgment by management. The District does acknowledge that improvements can be made in certain policies and procedures especially in the area of segregation of duties and will take the audit recommendations under advisement and make the necessary changes where applicable.

Auditor's Follow-up:

It is the responsibility of the Board of Commissioners to provide effective oversight over the operations of the district. This includes establishing and maintaining a proper internal control environment to provide the reasonable assurance that the district's resources are safeguarded and that transactions are executed in accordance with management's authorization and properly recorded. We found that district procedures were insufficient to permit testing of controls and therefore we have no confidence that adequate controls exist. While it may be true that we did not find evidence of fraud, we did find intentional use of public funds for inappropriate expenses. We note that one of

the three positions the district cites as having oversight of the district's finances is not an account clerk, but a clerk typist position which does not require an accounting background. In addition, the senior account clerk, on several occasions, acknowledged that she did not have an understanding of basic accounting functions such as bank reconciliations.

Cash Disbursements

The District will review its cash disbursement policy and take into consideration the recommendations of the audit, particularly the area of those persons authorized to sign checks. The District acknowledges that the audit showed one (1) duplicate payment, which was discovered and corrected by our staff, which was paid to a vendor incorrectly. The auditors were given over two thousand vouches to examine and question.

Auditor's Follow-up:

We concur with the corrective actions taken by the district but emphasize that it is the lack of controls over the cash disbursements process and lack of written policies and procedures, not the number of errors found, that puts the district at risk for unauthorized transactions and misuse of funds.

Role of the Insurance Broker

The audit conclusions and criticism of the role of the District's insurance broker is distorted and seemingly deliberately misleading. The District disputes the fact that it carries too much insurance or that it pays more than it should. During the audit, the District and the broker provided the auditors with documentation which clearly indicated the administration of the self insured Optical and Dental has saved the District money. In the case of the Worker's Compensation the audit fails to mention, although the auditors were provided both written and a face-to-face meeting with the broker, the fact over a nine-year period the broker saved the District 1.2 million dollars by his management of our Risk Retention Program and Worker's Compensation. The audit statement on the District's Health Insurance is again distorted and misleading. As explained to the field auditors at the time the District selected its current health care carrier, several other carriers were considered. The major consideration, aside from cost, was that the carrier chosen provide benefits equal to or greater than those agreed to, by the unions and the District. At the time the selection was made, the program referred to was Empire Blue Cross and Blue Shield and it did not meet the District's requirements.

Auditor's Follow-up:

During the course of the audit, we discussed the choices the district made regarding its insurance coverage and the role of its broker. The district acknowledged that it has not bid out its insurance needs since 1998; therefore, they cannot be certain that they are not overpaying or carrying unnecessary coverage. The only documentation provided to us regarding savings from the self-insured optical, dental and worker's compensation risk

management program were summaries presented by the broker. There was no evidence of analysis performed to substantiate the broker's claimed savings for self-insurance. In addition, we note that the administrative fees for the optical plan exceeded the amounts reimbursed.
The district was unable to provide us with any documentation evidencing which insurance carriers were considered for its health insurance coverage. Our audit compared the district's current coverage to the New York State Health Insurance Plan, not to Empire Blue Cross/Blue Shield.

Personnel

District Response:

As stated, most employees are covered by Collective Bargaining Agreements and, as is the case in most municipalities, persons charged with managerial or confidential duties are not. The Board of Commissioners are elected officials whose salary is set by the New York State Legislature, and are recognized by the New York State Employee Retirement System as full time employees. The attorneys' positions are Nassau County Civil Service certified full time positions. The District disputes the appearance of favoritism. All salary and benefits for employees not covered by one of the CBAs are a result of a Board resolution or motion made at a regular meeting of the Board of Commissioners.

Auditor's Follow-up:

The fact that Board members are elected does not automatically entitle them to recognition as full-time employees by the NYS Retirement System. The NYS Retirement System has specific guidelines and requirements for the reporting and recording of days worked by elected and appointed officials. See NYS & Local Retirement System, Employer Guide, June 2004, pp.1021-05 (available at http://www.osc.state.ny.us/retire/employers/index.html).
The attorneys' positions are not certified as full-time based on documentation provided to the Civil Service Commission; instead, the documentation states that attorneys' hours are "as required by the Board of Commissioners." The attorneys maintain private practices, do not maintain office space, and are not accountable for their time spent on district business. We acknowledge that benefits were granted through Board resolutions to employees not covered by the CBAs; however, Board approval does not preclude favoritism. The Board had not established appropriate standards or criteria that are applied uniformly to all employees. Again, there is an inconsistency here because if the district claims that the attorneys are full-time they must be reported to the NYS Retirement System as required. This is another indication that the district's policies are inconsistently applied, which can lead to the appearance of favoritism.

Appropriateness of Fund Balances

District Response:

The District does take into consideration the possibility of unforeseen expenses when preparing the budget and has been prudent in the transfer of surplus funds to be applied to new budgets. The District has not floated a bond or been forced to borrow money. The audit criticism seems to be based on their understanding of the District's purchase of a piece of real property in 2001. The property in question was the building, which is contiguous to the District's main building and was put on the market in 2001. The Board of Commissioners at that time was considering options regarding the allocation of space and needs of the District and felt that it would be in the best interest to purchase the property while it was available. The building was converted into administrative offices and New York State required record retention area. The area, which previously was shared by the administrative and operational supervisory staff, is now fully utilized by the supervisory staff.

Auditor's Follow-up:

The district's contention that they did not borrow money is incorrect. The district borrowed $1 million to finance, in part, the purchase of the building as well as the acquisition of equipment.

Role of External Auditor

District Response:

The District disagrees with the audit findings suggesting that the District auditor's independence may be compromised. The non-audit services that are provided by the external auditor are without any monetary cost to the District. The individual who performs the questioned non-audit services is not involved in the actual audit of the District, which is conducted by an independent audit team.

Auditor's Follow-up:

The fact that nonaudit services were provided at no cost is irrelevant.
The district and the auditor failed to take steps required by Government Auditing Standards to maintain the auditor's independence. They did not:

- *outline nonaudit services in the engagement letter along with the roles and responsibilities of the auditee and the auditor.*
- *document the rationale that nonaudit services do not include management functions or decisions or result in the external auditor auditing its own work; and*
- *designate a management-level individual responsible and accountable for overseeing the nonaudit service.*

Audit Finding (1):

Procurement of Goods & Services

District Response:

Lack of Competitive Bidding: The District takes exception to the audit stating that we do not comply with the General Municipal Law 103. The stated example is both misleading and incorrect. The figures stated include service contracts for software development, hardware equipment, Internet access fees and repairs. The District acknowledges that it relies on a vendor, which has developed, trained and provided support for our computer needs. Technology needs are somewhat proprietary and the District feels that we have been served well and fairly by the vendor in question. There is no other occasion that we know of that you question our compliance with General Municipal Law 103.

Auditor's Follow-up:

We stand by our finding that the technology purchases, where the total purchase is anticipated to exceed $10,000 should have been formally bid. The district did, on occasion, obtain informal bids from three vendors, two of whom were recommended by the district's technology vendor. We noted that for other types of purchases, quotes were not retained as required by the district's procurement policy. The district's external auditor noted in his management letter that written quotes and formal bids were not received. The auditor recommended that the district follow the guidelines for written quotes and formal bids in accordance with its purchasing policy and General Municipal Law §103.

Professional Services

District Response:

The District's selection of professional services is based on the individuals, firms or companies, who in our consideration provide the best and cost effective services. It is our opinion all three examples cited fill that requirement.

Auditor's Follow-up:

The district's procurement policy does not address professional services. Again, we note that the district has used the same firms for many years. Therefore, they have no objective basis for stating that their current firms offer the best and most cost-effective services.

Lack of Clearly Defined Roles and Responsibilities for Legal Counsel

District Response:

The District treats its two legal counsels as full time employees, which is in accordance with Nassau County Civil Service titles. The District, has since the audit findings, requested that both attorneys submit fully executed updated retainer agreements.

Auditor's Follow-up:

There is no evidence that the district's attorneys are functioning as full-time employees, since the attorneys maintain private practices, do not maintain office space, and are not accountable for their time spent on district business. Retainer agreements would be recommended for the attorney positions if they are considered consultants, job descriptions should be on file for employees. If the district can substantiate the full-time status of its attorneys, it should be consistent in its treatment of them as such. The district does not report the attorneys to the NYS Retirement System and is required to report all full-time employees, unless they are already collecting retirement benefits.

Audit Finding (2):

Lack of Segregation of Duties

District Response:

Although there has been no finding of criminality, fraud or attempt to defraud, the District acknowledges that because of the lack of a clearly defined segregation of duties, the opportunity for all could exist. However, the District is confident that the people that are currently employed are honest, competent and ever increasingly aware to be on the lookout for any type of fraudulent activity. The District is taking into consideration suggestions made by the auditors and will take the necessary steps to correct any deficiencies in its job descriptions and responsibilities, and those persons authorized to sign checks. The District will begin to use an approved computer program, one suggested by the audit team, to replace manual general ledger entries, in January 2006. The Secretary to the Board, as he does now, will review all general ledger postings. As far as the conclusion that board members don't go over vouchers in detail, that can only be an assumption on part of the audit team.

Auditor's Follow-up:

We concur with the district's corrective action with respect to segregation of duties. It is irrelevant to rely on the honesty of employees as a substitute for an adequate internal control environment. We concluded that "board members don't go over vouchers in detail" because commissioners approved vouchers with inadequate or incomplete supporting documentation. This was also confirmed in an interview with the senior account clerk. We did not "approve" any particular accounting program, but suggested

that the district look into purchasing any one of a number of readily available, off-the-shelf software accounting programs. The same type of program was suggested by the District's external auditor.

Audit Finding (3):

Lack of Budgetary Process

District Response:

As described earlier, the District disputes the findings and conclusion drawn by the audit concerning the purchase of the building. The office space has, from the first day, been occupied by the supervisory staff and is utilized on a daily basis and is vital to our day-to-day operations. Although the auditors arrived early each day, to the best of our knowledge they never witnessed what takes place in the questioned office space. All daily assignments, attendance recordings, accident reports, complaint compliance reports, end of the day collection of weight tickets take place in that office.

Auditor's Follow-up:

The finding relates to the fact that the district did not budget for the purchase of this building and the district should only be spending what it has budgeted for.

Audit Finding (4):

Lack of Written Polices and Procedures

District Response:

The District has reviewed the findings of the audit in regard to policies and procedures. While all policies are under review and/or revision, the District has adopted some of the recommendations of the audit team and forwarded them to your office. Specifically, long distance and cell phone polices drafts have been sent to you for approval. Expenditures deemed inappropriate will be discontinued. The District does have a detailed investment policy, which was provided to the auditors. As explained during the field audit and again at the exit conference, the agreements with the school district and the various fire departments save thousands of taxpayer dollars. We do not consider these agreements to be of a so-called "resale" nature since they pay whatever we are charged. All districts utilizing our state contract do so upon their written request, which we produced to the field auditors. We have never experienced any problems with reimbursement and do not anticipate any district not taking advantage of such a cooperative program, which saves the taxpayers money. With regard to the check for 2.1 million dollars, we dispute that a voucher would be required for a bank transfer. The changes in the delegation of duties and responsibilities will prevent such an occurrence in the future.

Auditor's Follow-up:

We commend the district for making improvements to its written policies. It is not our practice to approve district policies. We reiterate our recommendation that the district have inter-municipal agreements for the resale of fuel. Government entities should document all their contracting arrangements, even those that are with other governmental entities. With respect to the check for $2.1 million, all cash disbursements should follow district policy and be approved by three Board members regardless of purpose.

Audit Finding (5):

Personal Use of District Vehicles

District Response:

The District does monitor gas usage and the field auditors were shown gas tickets filled out by the supervisors each time they fueled up and computer print outs of every time some one fueled up. These printouts identify the vehicle, the amount of product taken and the time and date of the transaction. The Motor Repair Supervisor records monthly mileage for all District vehicles and any extraordinary discrepancy would be reported. Logs for the Code Enforcement Supervisors, who occasionally work weekends or nights, were supplied to the auditors. In addition to the logs supplied, the field auditors inspected the notice of violation and summons books of both Code Enforcement Supervisors. These books, which are duplicates of the actual notice of violation or summons and contain the day, date and on some occasions the time that they were written. The District believes that given that information, the auditor should clearly be able to determine the nature of their work performed on any given date. The audit incorrectly concludes that imputed value of $6,100 per year and $3 per day for commuting and personal use of district vehicles was determined by the District's auditor and was based on depreciation only. The District's policy regarding the Secretary to the Board and the General Supervisor are based on IRS regulation Reg 1.61-21(d)(3) which states "this method takes into account the value of insuring and maintaining the auto, but not the value of fuel, which if provide in kind can be valued on all facts and circumstances, or alternatively at 5 1/2 cent per mile for all miles driven (in the U.S. Canada or Mexico) by the employee". The District, as it was pointed out to the field auditors, did not depreciate the full value charged to the Secretary to the Board, General Supervisor or the Recycling Coordinator. All three were charged full value to take into consideration fuel usage beyond District business.

Auditor's Follow-up:

We concur that the district maintains tickets for fuel pumped; however, we saw no evidence that an analysis is performed to determine if the miles driven and fuel used is reasonable.
The district's external auditor informed us that the $6,100 rate was based on depreciating the vehicles over five years. We stated in our finding that the income

imputed by the district may be insufficient; the district did not add the value of fuel to the $6,100 per year. The district's response does not address the adequacy of $3 per day or our concern that personal use of the vehicles may be unnecessary. The district only provided us with documentation that related to the code enforcement supervisors, which only addresses two out of the eleven employees that have personal or commuting use of district vehicles.

Audit Finding (6):

Role of the Insurance Broker

District Response:

The District disputes the finding that the insurance broker "creates the district's insurance budget" when in fact he assists the District by providing the necessary insurance cost projections for the coming year. The District acknowledges that it does not have a fine art collection. However, that particular coverage is part of a package of fifty items, which pertains to the District's needs. Likewise, the coverage regarding our website also includes, although not stated in the audit, coverage for our telephone system, two way radio communications system and email system. The audit is misleading when its states that there is a 53% increase in workers compensation premium, without acknowledging that the 2004 premium reduction due the District has not yet been processed. The District will require, as recommended, that the broker supply the management reports specified in the dental and optical insurance contracts and will review them to ensure they are being efficiently administered. The District will require the broker, as has been the practice in the past, to provide written quotes when pricing out renewals.

Auditor's Follow-up:

In our interview with the secretary to the board, we were advised that the budget for the insurance was provided to the district by the insurance broker. We stand by our finding that there is a conflict of interest with respect to the role of the insurance broker. The district acknowledged that it has not bid out its insurance needs since 1998; therefore, they cannot be certain that they are not overpaying or carrying unnecessary coverage. There was no recognition in any of the financial information provided for 2004 that there was an anticipated premium reduction related to the district's 2004 workers' compensation premium. In addition, we found no evidence that the district retained any written quotations when pricing out insurance renewals.

Audit Finding (7):

Broker's Role in Lease /Purchase Agreement

District Response:

The District asserts that it does make all of its own investment decisions. The District disputes the conclusion that investment decisions were made by the broker. We may have relied on advice provided by the broker, but ultimately the Board of Commissioners made the decision. The District did not mislead the lessor or violate any warranties under the lease agreement. The Lessor acknowledged that the District would make building and automotive improvements and facilitated their needs through the Security Agreement within the lease.

Auditor's Follow-up:

Our conclusion that investment decisions were made by the broker was based on three factors:

1) *The bank's written comments on the escrow statements consistently reference telephone calls from the bank to the broker for investment instructions and responses from the broker that provided the instructions.*
2) *We requested the documentation authorizing the broker to make investment decisions and authorizing the bank to accept instructions from the broker. The district did not respond to this written request or indicate that the broker did not have any investment authority role.*
3) *Board minutes did not contain any evidence that escrow investment decisions were made by the Board.*

On February 6, 2002, The Board of Commissioners resolved to execute the lease agreement because a "true and very real need exists for the reimbursement of building improvements and the equipment. . . ." and detailed a reimbursement as $184,400 for building improvements. A letter from the district's counsel to the bank provided the bank with an opinion that the equipment leased under the Equipment Lease/Purchase Agreement "constitutes personal property and when subjected to use by the Lessee will not become fixtures under applicable law." The letter made no mention of the purchase of real property. The district purchased a building on December 10, 2001 for $182, 379 (including closing costs) and the district requested reimbursement through a requisition request issued to the bank on September 24, 2002. The district's requisition request did not make any mention of a building; instead, it authorized the lessor to fund the acquisition of equipment in the amount of $184,000. The district eventually made improvements to the building in the amount of $84,995, but not until April 2003, one and a half years later. We stand by our conclusion that the $184,000 drawn down under the lease was not used to acquire equipment or to make building improvements. In addition, we stand by our finding that the district did not follow proper procurement procedures in obtaining the lease/purchase agreement and relied too heavily on its insurance

broker/vendor, to determine its financing needs. This lease agreement resulted in unnecessary interest expense to the district.

Audit Finding (8):

Time Records are Not Kept for All Employees

District Response:

Commissioners are elected officials and are not required to keep daily hours. Daily attendance is recorded for all employees. The District supervisors meet with the General Supervisor, or in his absence the Secretary to the Board each day prior to leaving on the road and at the end of each day, however the practice of supervisors not signing time sheets is under review. It should be noted that several of the field auditors were shown and tested the District procedures for recording daily attendance, which includes several redundancies to assure its accuracy. To our knowledge there were no errors found. Although the second recommendation concerning collective bargaining issues goes beyond the scope of the audit, the proposal, to the unions, for consolidation of routes was made before the issuance of this report, and for that matter before the audit was conducted.

Auditor's Follow-up:

We concur with the district's decision to review its timekeeping practices, which do not currently require detailed time records or that supervisors sign timesheets. The district states that no errors were found, but we were unable to test district procedures for the recording of time and leave because the district denied us access to employee personnel files. We consider route consolidation a good first step, but note that route consolidation alone will not address the impractical—and unenforced—four-day, ten-hour day workweek currently stipulated in the CBA for positions that require a substantial amount of physical labor. We found that District sanitation workers work an average of 4-5 hours a day for four days (Monday, Tuesday, Thursday & Friday) but get paid for a forty-hour workweek.

Audit Finding (9):

Improper Reporting of Certain Employees for New York State Retirement System, Internal Revenue Service and Employee Benefit Purposes

District Response:

The audit incorrectly indicates that the District reports four of the five Commissioners as full time employees to the New York State and Local Retirement System (NYSERS). The District reports three, not four, Commissioners as full time employees to NYSERS. The audit fails to recognize that NYSERS has accepted them as full time employees for the purpose of additional salary reporting. The total cost to the District for the

Commissioners reported as full time, is less than $350 per year. The fact that two of the Commissioners work for the Baldwin Fire District is immaterial and beyond the scope of the audit and, in our opinion, reported for political purposes. The attorneys, as stated in the executive summary, are recognized by Nassau County Civil Service as full time positions. As stated in our response in the Executive Summary of this audit, the District disagrees and takes exception with audit finding regarding the assertion that in some way the District tried to circumvent or deceive the Nassau County Civil Service Commission in regard to the District's Labor Counsel. As explained during the audit and again at the exit conference, the Labor Counsel performed all his regular duties as Labor Counsel and represented the District in several on-going Ad Valorem tax cases. As explained, the Labor Counsel was the attorney of record for these cases. The auditors were given and inspected the voucher explaining the cost and hours and subsequent payment concerning these cases. The District properly reported payment to the IRS on a 1099 form. The District did establish an in house title of Recycling Coordinator 1985. As explained to the field auditors, the District was the first municipality on Long Island to institute a curbside recycling program. There was no title available at that time from Nassau County Civil Service. As stated his salary change was reported to and accepted by the Nassau County Civil Service Commission. This title is no longer in use by the District. The General Supervisor as a cost saving measure has assumed the responsibilities of the Recycling Coordinator.

Auditor's Follow-up:

We confirmed with the NYSERS that four of the five Commissioners are being reported as full-time employees. Until NYSERS performs an audit of an individual employee's retirement record, it accepts the employee's employment status as it is reported by the district, but may reject this status as a result of performing a detailed audit. We did not observe the District commissioners working anything like a full-time schedule, and it strains credulity to believe they are doing so for a salary of $7,500. Without any evidence of the time worked by the commissioners, it is difficult to assume full-time employment for a $7,500 salary. In addition, according to the Retirement System, local employers such as the District should determine the average time worked by elected officials, issue a resolution to that effect and report that time to NYSERS; NYSERS recommends that the local employer revisit this determination periodically. See NYSERS Employer Guide, June 2004, pp. 103-05.
We understand that there may have been a board resolution approved July 2nd, 1986 concluding that the Commissioners should be considered full-time employees; as NYSERS recommends, the District should revisit this conclusion We stand by our finding that the additional amounts reported on the attorney's IRS form 1099 fell outside of the salary plan submitted to the Civil Service Commission and circumvented the civil service approval process. Although the district is entitled to two full-time attorney positions by Nassau County Civil Service, in practice the two attorneys at the district do not appear to work full-time. They maintain private practices, do not maintain office space at the district, and are not accountable for their time spent on district business. We are not questioning the value of employing the recycling coordinator, but rather the circumvention of process, especially civil service regulations, in originally establishing

this position and in maintaining it for 20 years. We stand by our finding that the district employed a Recycling Coordinator for almost 20 years without civil service approval and paid him in excess of his union title wage scale.

Audit Finding (10):

Lack of Formalized Benefit Plan for all Employees

District Response:

The District, for reasons as stated before, considers the Commissioners and attorneys to be full time employees. Therefore, we disagree with the audit finding. The requirement for contribution to health care benefits covers employees who are covered by the collective bargaining agreements. The Board at a regular meeting granted the former Secretary to the Board the insurance benefit in appreciation for his thirty-five years of service to the District. The audit finding regarding the former labor counsel is incorrect. He was billed and reimbursed the District legally, as a retiree.

Auditor's Follow-up:

While the district is permitted to have five Commissioners and two attorneys, they should not automatically be considered full-time when the hours they spend reflect a part-time status. We reiterate that the attorneys maintain private practices, do not maintain office space, and are not accountable for their time spent on district business. We were informed that employees that are not covered by a collective bargaining agreement receive the same benefits as those covered under the Unit II CBA, which includes a provision for contribution to health insurance, the termination of health insurance after the age of 65, and does not provide for the payment of life insurance after termination of employment. We stand by our findings and recommendations in this area.

Audit Finding (11):

Appropriateness of Fund Balance

District Response:

The District endeavors to treat fund balances in a manner that allows us to operate comfortably until tax revenues are received in February-while still applying surplus funds to the new budget, in order to keep the tax rate down. In September 2004, when the District prepared its budget projections for 2004, it estimated the New York State Retirement System bill to be $384,000. In October 2004, the New York State Comptroller announced a huge increase in all billings (this affected all municipalities in the system). The District's bill was increased to $583,000, an increase of $199,000. The District had options but it chose to pay the entire amount in December 2004 and be economical in its spending in the New Year. The District chose not to pay in February additional interest and not to amortize, and by doing so avoided additional costs of

$52,000 on the retirement billing for the next five years. As far as budget preparations are concerned, the District does thoroughly prepare its budget, but acknowledges that the backup materials sought by the auditors can be improved. The District will incorporate those recommendations stated in the audit relevant to contingency and identifying overspent accounts.

Auditor's Follow-up:

The district's response does not address our finding that the district does not appear to budget appropriately for expected annual expenses. We reiterate our recommendation that budget transfers be formally reviewed and approved by the board, that expenses be charged to the appropriate account, and that expenses should only be paid after it is determined that budgetary limits are not exceeded.

Audit Finding (12):

Role of External Auditor

District Response:

The District, as stated in its reply in the Executive Summary, does not agree that the auditor's role is inappropriate or in any way compromised. Whatever advice or assistance given during the year is done without cost to the District. As to the finding that the District made an error in reporting fixed assets in its 2003 financial statement, as explained by the District auditor during the audit, the District disagrees with the audit conclusion. The District had not adopted Government Auditing Standard Board's Statement Number 34 for the year ending December 2003. Therefore, capital assets were not audited, but submitted for information only. The District did adopt Government Auditing Standard Board's Statement Number 34 for the year December 31, 2004, and capital assets have been presented accordingly. The District management letter, supplied to the field auditors, dated March 19, 2004 contains some of the same recommendations that this audit contains. The District is presently reviewing and adopting many of these recommendations. The District auditing firm has conducted hundreds of municipal audits, including several Long Island school districts, whose published New York State audits have been fine. The District is not required to rotate auditors and knows of no other municipality that does.

Auditor's Follow-up:

The district did not address the finding that it relies too heavily on its auditor, therefore compromising the external auditor's independence. In addition, the district should ensure that it employs individuals with adequate financial and accounting expertise to ensure that the information the district provides in its annual report is free of obvious errors. The fact that nonaudit services were provided at no cost is irrelevant. The district and the auditor failed to take steps required by Government Auditing Standards to maintain the auditor's independence. They did not:

- *outline nonaudit services in the engagement letter along with the roles and responsibilities of the auditee and the auditor;*
- *document the rationale that nonaudit services do not include management functions or decisions or result in the external auditor auditing its own work; and*
- *designate a management-level individual responsible and accountable for overseeing the nonaudit service.*

Our recommendation that the district rotate auditors is based on good business practice, to promote objectivity and to minimize complacency. We note that Nassau County and New York City, with much more complicated financial records than the district, making rotating auditors more burdensome, periodically issue a request for proposals to obtain auditing services. In addition, we note that General Municipal Law Section 104(b) requires written procurement procedures for obtaining professional services, and that recent New York State legislation will require school districts to competitively procure audit services, at a minimum of every five years.