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STATE OF NEW YORK
OFFICE OF THE STATE COMPTROLLER

February 15, 2000

Mr. John P. Cahill
Commissioner
Department of Environmental Conservation
50 Wolf Road
Albany, NY 12233-1550

Re: Report 99-F-28

Dear Mr. Cahill:

Pursuant to the State Comptroller's authority as set forth in Article V, Section 1 of the State Constitution, Article II, Section 8 of the State Finance Law, and Section 72-0303 of the Environmental Conservation Law, we have reviewed the actions taken by officials of the New York State Department of Environmental Conservation (Department), as of December 9, 1999, to implement the recommendations contained in our audit report, *Costs and Revenues of the Title V Operating Permit Program Regulating Industrial Air Pollution* (Report 95-S-107). Our report, which was issued on February 19, 1998, examined the Department's administration of the Title V Operating Permit Program for the period April 1, 1993 through December 31, 1996.

Background

In 1970, Congress passed the Clean Air Act (Act) to promote public health and welfare. Congress amended the Act in 1990 to require the states to meet air quality standards developed by the Federal Environmental Protection Agency (EPA). Title V of the amendment requires the individual states to establish an operating permit program regulating the amount of pollutants emitted by industrial sources. As such, the states are responsible for issuing operating permits to regulated facilities, and collecting the corresponding fees each facility is assessed according to its respective emissions level. The Act also requires that permit fee revenues be sufficient to cover all reasonable direct and indirect costs of the program. If an individual state does not establish this program in accordance with the mandated requirements, the EPA may assume operation of that state's program.

To comply with the 1990 amendment to the Act, the New York State Legislature enacted the Clean Air Compliance Act of 1993. In accordance with this legislation, the Department formally established New York's Title V Operating Permit Program (Program), which was

approved by the Federal EPA in 1996. The Department is required by the Clean Air Compliance Act to:

- identify New York's major stationary air pollution sources (Title V facilities);
- collect fees from these facilities based on the amount of pollutants each emits;
- set up an account for the deposit of Program fees to cover Program costs; and
- report annually on Program costs, revenues, and progress during the preceding fiscal year.

Summary Conclusions

Our prior audit found that, contrary to Federal requirements, permit fee revenues had not been sufficient to cover Program costs. As a result, the cost of the Program had been subsidized by other State and Federal funds. We also found that reported Program revenues could not be verified because of serious weaknesses in Department procedures for billing, collecting, and accounting for fee revenue. We further determined that reported Program costs were not entirely accurate, in part because of weaknesses in the Department's cost accounting practices. We recommended that the Department seek a change in the State law governing the permit fee to ensure that the fee could generate enough revenue to cover Program costs. We also recommended that the Department improve its internal controls over fee revenue and its cost accounting practices.

In our follow-up review, we found that the Department has made significant progress in implementing the recommendations contained in our prior audit report. The Department requested and received an increase in the Title V Permit fee ceiling, and has improved its system of allocating applicable personal service costs to the Program. However, Department officials have not taken steps to reconcile the cash receipts reported by its contracted billing and collections agent, nor have they issued the Program's annual reports by the mandated annual due date.

Summary of Status of Prior Audit Recommendations

Of the 13 prior audit recommendations, Department officials have implemented 8 recommendations, partially implemented 3 recommendations, and have not implemented 2 recommendations.

Follow-up Observations

Recommendation 1

Develop a system that accurately accounts for and allocates Program personnel costs throughout the fiscal year, rather than accumulating the cost information after the year ends.

Status - Partially Implemented

Agency Action - In January 1998, the Department's Division of Air Resources developed a personal service time and activity tracking system to help ensure that all Program staff time cards are submitted within the established time frames, thereby enabling Program officials to prepare quarterly time allocation reports for management review. The information from this system is periodically reconciled to the Department's official time card data, maintained by its Division of Management and Budget Services, to ensure that the official time card data is up-to-date and complete. However, the Department's system, which provides the applicable cost data and is used for official reporting purposes, is still unable to provide allocated program costs within a reasonable period of time (less than one month) after each quarter.

Recommendation 2

Ensure that all identified Title V facilities are billed annually for permit fees.

Status - Implemented

Agency Action - Department officials use an independent contractor to bill Title V facilities and have taken steps to ensure that all identified facilities are billed. Program staff identify Title V facilities through historical Department data, self-reporting by facilities, regional office observations, and Program outreach activities. Department officials have also developed the Program's "Air Facilities System," a nine-module database system, which includes emission inventory and fee billing data for all known Title V facilities.

Recommendation 3

Develop a process to appropriately account for all Title V permit fees, interest and penalties.

Status - Implemented

Agency Action - We found that the Department's current accounting and internal control systems do an effective job of identifying, billing, collecting, categorizing, and recording Title V fees, fines, penalties, and interest revenue.

Recommendation 4

Every month reconcile the Title V bills to the amounts collected and the amounts outstanding.

Status - Partially Implemented

Agency Action - Program officials receive a monthly report of collections and unpaid invoices from their billing and collections contractor. These reports are used as a basis for dunning letters that are sent to facilities whose bills are at least 75 days overdue. However,

Program officials do not reconcile the billings, collections, and unpaid invoices to prepare a formal accounts receivable and assure themselves that all unpaid invoices have been brought to their attention.

Recommendation 5

Develop formal policies and procedures for billing, collecting and accounting for Title V revenue, and monitor these activities to ensure that they are performed as intended.

Status - Partially Implemented

Agency Action - Department officials have developed formal procedures for governing the billing, collecting, and recording of Title V revenues; and they assert that these activities are monitored continually. But since officials do not formally document their monitoring procedures, we have no assurance that they actually do so.

Recommendation 6

Streamline the Title V billing process, and in conjunction with this effort, consider processing Title V bills entirely in-house.

Status - Implemented

Agency Action - Program officials informed us that they considered this recommendation and opted to continue using their contracted billing agent. However, they did indicate that Program staff now mail Program-related bills in-house, in an effort to streamline the billing process.

Recommendation 7

Formally contract for locked box banking services on the basis of competitive bids, and evaluate paying for the services with fees rather than a compensating balance.

Status - Implemented

Agency Action - The Department issued an Invitation for Bids in April 1999 to implement this recommendation. Two bids were received and a contract award letter was issued in July 1999. The new contract provides for a service-based fee arrangement.

Recommendation 8

Charge all direct and indirect Program costs to the Program Account.

Status - Not Implemented

Agency Action - Department officials indicate that they have been unable to charge all direct and indirect Program costs to the Program account because it has insufficient funds, which they blame on the approved permit fee ceiling (see next Recommendation).

Recommendation 9

Seek a change in the State law regarding the maximum permit fee so that the law is consistent with Federal regulations regarding the minimum permit fee, and ensure that the permit fees cover all reasonable direct and indirect Program costs.

Status - Implemented

Agency Action - Department officials requested a fee increase to $48 per ton. In response, the Legislature approved a fee increase to $45 per ton to commence in the 1999-00 budget year. Based on the forecasted data for fiscal years 1998-99 and 1999-00, Program officials should be able to cover most, if not all, Program-related costs with this increase.

Recommendation 10

Seek clarification in the State law regarding how to treat working capital in the Program Account, and apply the full amount of any Account surplus beyond working capital needs when calculating the Permit fee. Also consider refunding any surplus beyond working capital needs to the other State appropriations that were charged for Program costs.

Status - Implemented

Agency Action - Program officials have considered the Program account balance (surplus or deficit) when calculating the annual permit fee. To date, because year-end balances have been dedicated to impending Program costs, they could not be refunded to non-Program revenue sources. Thus, we believe Program officials are complying with the governing statutes regarding the permit fee calculation, and further clarification is not necessary.

Recommendation 11

Consider proposing legislation to change the Program reporting period to coincide with the Program billing cycle.

Status - Implemented

Agency Action - Department officials informed us that they have considered this recommendation and determined that the calendar year is the preferred reporting period for facilities. Their

decision considered the regulated industry's business cycle, as well as the need for pre-invoice emissions statement reviews.

Recommendation 12

Ensure that a completed annual report is issued by September 30 of each year. If a draft, but not the final, report is available by that date, and the draft report is submitted to the Governor's Office, ensure that the draft report is also submitted to the Legislature and the State Comptroller.

Status - Not implemented

Agency Action - Program officials have yet to issue a final annual report before the September 30 due date. However, they stated that they are working to comply with the mandated date. They also said they believe that it would not be an appropriate response to the legislative mandate to issue a draft report.

Recommendation 13

Ensure that the financial statements included in the annual report are prepared in accordance with government accounting standards, and include balance sheets, revenue/expenditure statements, and budget versus actual comparisons.

Status - Implemented

Agency Action - Financial statements are now prepared in conformity with the cash basis of accounting.

Major contributors to this report were Gerald Tysiak, Frank Patone, Dianne Hart, Ricardo Pimental, and Lei Zhang.

We would appreciate your written response to this report within 30 days, indicating any additional actions planned or taken to address any unresolved matters discussed in this report. We also thank the management and staff of the Department of Environmental Conservation for the courtesies and cooperation extended to our auditors during this review.

Very truly yours,

Frank J. Houston
Audit Director

cc: Charles Conaway