



Town of Jefferson

Selected Financial Operations

Report of Examination

Period Covered:

January 1, 2013 — July 15, 2014

2014M-332



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

March 2015

Dear Town Officials:

A top priority of the Office of the State Comptroller is to help local government officials manage government resources efficiently and effectively and, by so doing, provide accountability for tax dollars spent to support government operations. The Comptroller oversees the fiscal affairs of local governments statewide, as well as compliance with relevant statutes and observance of good business practices. This fiscal oversight is accomplished, in part, through our audits, which identify opportunities for improving operations and Town Board governance. Audits also can identify strategies to reduce costs and to strengthen controls intended to safeguard local government assets.

Following is a report of our audit of the Town of Jefferson, entitled Selected Financial Operations. This audit was conducted pursuant to Article V, Section 1 of the State Constitution and the State Comptroller's authority as set forth in Article 3 of the New York State General Municipal Law.

This audit's results and recommendations are resources for local government officials to use in effectively managing operations and in meeting the expectations of their constituents. If you have questions about this report, please feel free to contact the local regional office for your county, as listed at the end of this report.

Respectfully submitted,

*Office of the State Comptroller
Division of Local Government
and School Accountability*

Introduction

Background

The Town of Jefferson (Town) is located in Schoharie County and has 1,410 residents. The Town Board (Board) comprises four elected Board members and the elected Town Supervisor (Supervisor). The Board is responsible for managing and controlling the Town's finances and operations and protecting the Town's assets. The Supervisor,¹ as the chief fiscal officer, is responsible for maintaining the accounting records and providing monthly reports to the Board.

The elected Town Clerk (Clerk) has also been appointed to serve as the Tax Collector and is responsible for, among other duties, maintaining Town records and collecting water rents. The Clerk acted as the bookkeeper from January 2013 until February 2014. The new Supervisor's term began in January 2014. In February 2014, the Supervisor hired a local bookkeeping company to maintain the accounting records.

The Town provides various services, including general government support, a justice court, road repair and maintenance, snow removal, municipal lighting and water services. The Town's budgeted appropriations for the 2015 fiscal year are \$324,942 for the general fund, \$662,408 for the highway fund and \$28,000 for the water fund. These appropriations are funded mainly through real property taxes, sales tax, State aid and user fees.

Objective

The objective of our audit was to examine selected financial operations of the Town. Our audit addressed the following related questions:

- Did the Supervisor and Board ensure that disbursements were for proper Town purposes and water rents were properly accounted for and deposited?
- Did the Board and Supervisor adequately address deficiencies in the financial records of the Supervisor's office?

Scope and Methodology

We examined selected financial operations of the Town for the period January 1, 2013 through July 15, 2014.

We conducted our audit in accordance with generally accepted government auditing standards (GAGAS). More information on such standards and the methodology used in performing this audit is included in Appendix B of this report.

¹ The current Supervisor was elected in January 2014.

**Comments of
Local Officials and
Corrective Action**

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

The Board has the responsibility to initiate corrective action. A written corrective action plan (CAP) that addresses the findings and recommendations in this report should be prepared and forwarded to our office within 90 days, pursuant to Section 35 of the General Municipal Law. For more information on preparing and filing your CAP, please refer to our brochure, *Responding to an OSC Audit Report*, which you received with the draft audit report. We encourage the Board to make this plan available for public review in the Clerk's office.

Board Oversight

The Board is responsible for establishing internal controls to provide reasonable assurance that Town resources are adequately safeguarded and accounted for and that financial transactions are properly authorized. Town officials are responsible for implementing the Board's control directives by designing and documenting operating policies and procedures and properly delineating employee responsibilities. Included in such a control system is the proper segregation of duties to ensure that no one person controls all phases of a transaction and to provide for the work of one employee to be verified by another employee in the course of their duties.

The Supervisor and the Board did not ensure that all disbursements were for Town purposes and that all water rents were properly received and deposited because they did not establish adequate internal controls for the Town's cash disbursement process and for the collection of water rents. The Supervisor and Board did not establish adequate controls, such as requesting and reviewing canceled check images, to avoid the additional fees that the Town's bank would charge for the canceled check images. The Board was not aware of other controls that could help ensure the safety of Town funds, such as properly segregating duties and reviewing the list of water rents to be re-levied. Furthermore, the Board did not ensure that duties were properly segregated for bookkeeping or for water rent collections, or provide adequate oversight of those duties. As a result, Town funds are at a greater risk of misuse.

Cash Disbursements

If it is not feasible to segregate duties, Town officials must institute compensating controls such as designating a Board member to serve in a supervisory role over the cash disbursement function. Supervisory or Board oversight, such as an independent review of bank statements and reconciliations, acts as a compensating control to the inadequate segregation of disbursement duties.

After the Board approves vouchers for payment, the Clerk creates an abstract of the approved vouchers to be processed by the bookkeeper. The Supervisor is responsible for making payment of all items on the Board-approved abstract. After processing the checks, the Supervisor compares the approved abstract with the checks and manually signs the non-payroll checks for payment. Payroll checks are electronically signed with the Supervisor's signature. The Supervisor must also ensure that the Town's blank check stock is secured.

The Supervisor and Board cannot ensure that all disbursements were made for proper Town purposes because no one verifies that

the checks that cleared the bank were for proper Town purposes. The Town does not receive canceled check images. In addition, no one reviews the bank statements or bank reconciliations. Moreover, several Town officials² have access to outdated blank check stock.

Furthermore, the bookkeeper has access to Town bank accounts and can disburse funds using the Supervisor's electronic signature. The bookkeeper also records transactions and performs bank reconciliations. Other than the annual audit performed by the Board, the bookkeeper operates with little oversight and, as a result, errors, irregularities, theft or abuse could occur and not be detected or corrected in a timely manner.

The Board did not realize the importance of reviewing canceled check images, bank statements and bank reconciliations. Additionally, the official Town bank charges a fee for including check images with the bank statements. The Board did not want to incur the additional costs for receiving the check images.

As a result of these deficiencies, we examined a sample of 232 disbursements totaling approximately \$236,300³ to determine if they were for proper Town purposes. We verified that check numbers and amounts agreed with the approved invoices. We found minor exceptions which we discussed with Town officials. While approved vendor invoices appeared to be for proper Town purposes, without reviewing canceled check images, we could not verify the actual payees. Therefore, there is no assurance that the vendors listed on the abstracts were the actual vendors paid. We also reviewed 61 transfers from Town bank accounts totaling approximately \$800,700. We found all transfers were for proper Town purposes and adequately supported.

Without reviewing canceled check images, personal or unauthorized purchases can be made from Town accounts without Town officials' knowledge. Further, because no one independent of the bookkeeper reviews bank statements or reconciliations, the Town continues to face the risk that unauthorized checks could be issued or cash withdrawals or electronic fund transfers (EFTs) could occur without being detected.

Water Rents

An effective system of internal controls over the collection of water rents includes proper segregation of duties so that one individual does not perform the three key duties of billing, collecting and recording water rents. If it is not practical to segregate duties because of limited

² The Supervisor, Clerk and Deputy Clerk all have access to the blank check stock.

³ See Appendix B for sampling information

staff resources, the Board must establish compensating controls to mitigate the risks associated with the inadequate segregation of duties. These controls can include having someone independent of the process review the billing, receiving and accounting records associated with the collection of water rents. Also, the Board could require the Supervisor's office or the Clerk to maintain a water rents receivable control account.⁴ This control account would provide an independent record that could be periodically reconciled with the detailed customer accounts maintained by the Clerk to help ensure the accuracy of the records and to detect errors or irregularities.

The Supervisor and Board did not ensure that water rents were properly billed, collected, recorded and deposited. The Clerk and Deputy Clerk bill, collect and record all money for water rents with no oversight. Both can create bills and apply payments for water rents. They do not maintain a control account to track amounts collected against those billed. The Clerk and Deputy Clerk remit daily collections to the Supervisor for deposit. However, the Supervisor does not verify that the amount he receives agrees with the amount collected by the Clerk and Deputy Clerk. Although the Board approves adjustments prior to the Clerk or Deputy Clerk applying the adjustments to water accounts, it does not review the individual customer accounts adjustments to ensure that only Board-approved adjustments are made. Lastly, the Board does not review and approve the list of re-levied water accounts at year end.

These deficiencies occurred because the Supervisor and Board did not establish adequate controls over water rent collections. They did not ensure that the duties for water rent operations were adequately segregated or that sufficient compensating controls were in place. Additionally, Board members were unaware that they had to review and approve the re-levy list for remaining unpaid accounts at year end.

As a result of these deficiencies, we examined 92 billings totaling approximately \$8,400 to determine if they were properly billed, recorded and deposited. We found only minor deficiencies, which we discussed with officials. We verified that 20 unpaid water customer accounts were true and accurate. We also reviewed 94 deposits totaling approximately \$11,800. We found seven transactions totaling \$847 that were not recorded in the cash receipts journal. However, we did verify that the \$847 was deposited into the bank account. Without adequate segregation of duties or compensating controls, cash receipts from water rents are at risk for theft or abuse.

⁴ A control account is a general account showing totals of transactions with detailed figures appearing in subsidiary ledgers.

Recommendations

The Board should:

1. Establish an internal control structure to include compensating controls to mitigate the risks associated with the collection of water rents and disbursement of Town funds, including:
 - Providing an independent review of canceled check images to approved abstracts,
 - Reviewing and approving the annual list of re-levied water rents,
 - Creating a control account for water rents and
 - Performing an independent review of bank statements and reconciliations.

The Supervisor should:

2. Implement compensating controls for cash disbursements and water rent collections, including:
 - Destroying outdated check stock,
 - Maintaining a control account for water rents and
 - Reconciling the water rent receipts collected by the Clerk and comparing the amounts to the deposited amounts.

Records and Reports

The Board has a responsibility to oversee the Town's fiscal activities and safeguard its resources. The Supervisor, as chief fiscal officer, is responsible for performing basic accounting functions, including maintaining accounting records, providing useful monthly financial reports to the Board and filing the annual financial report with the Office of the State Comptroller. The accounting records and reports must be complete, accurate and current to be relevant and useful for managing Town operations and, where applicable, for the use of analysis by outside stakeholders.

The new Supervisor adequately addressed deficiencies in the financial records of his office shortly after his term began in January 2014. The new Supervisor reviewed several of our prior audits and found that our recommendations were not being implemented. He has made progress implementing our prior repeated recommendations.

The Clerk maintained the Supervisor's records for the majority of our audit period. The Clerk's and bookkeeper's duties are not compatible. Someone other than the Clerk should perform the bookkeeping duties. We also identified deficiencies in her records for that period that included the following:

- The Clerk mistakenly remitted approximately \$26,400 in duplicate payroll withholdings to the Internal Revenue Service (IRS) during the audit scope period. The additional amounts remitted came from Town money, not from amounts withheld from employees. The IRS refunded those payments and we verified they were deposited into Town accounts.
- We reviewed general fund expenditures for 2013 and found Town records showed that the Town spent approximately \$9,200 more than what was reported on the annual update document (AUD). Further, the Town records showed \$1,000 more in expenditures than what actually cleared Town bank accounts. The Clerk did not know why the records showed these differences and could not verify what created the differences.
- The Clerk inaccurately recorded transfers between Town bank accounts in the same fund as expenditures in the accounting records. She recorded transfers of \$213,000 in the general fund and \$401,000 in the highway fund. As a result, the expenditures reported to the Board for those funds were overstated by those amounts.

- The December 2013 year-end balance sheet did not present an accurate record of the Town's financial condition because it included negative cash accounts and incorrect payroll withholding amounts. The Clerk could not explain why these account lines were not accurate.

Beginning in February 2014, the Supervisor hired a bookkeeping company to maintain the Town's financial records. We compared 33 cash receipt transactions totaling approximately \$97,200 from source documents to the accounting records and verified they were recorded and deposited. We compared 89 disbursements totaling approximately \$53,300 and verified they were reported and supported. Other than minor deficiencies, which we communicated to Town officials, the Supervisor's financial records were adequate and accurate after the bookkeeping company was hired. Further, the bookkeeping company has included additional reports when reporting to the Board, including balance sheets, profit and loss statements and transaction detail reports by account for all funds.

The Board now receives current and accurate information to more effectively make decisions and manage Town operations. Additionally, with accurate accounting records, the Town can submit accurate financial information to outside stakeholders, such as through submission of the AUD, and provide a more transparent view of Town operations its residents and taxpayers. The additional reports provided by the bookkeeping company will enhance the Board's ability to monitor and manage the Town's financial position.

We commend Town officials on making substantial improvements in the Town's financial records and reports.

APPENDIX A
RESPONSE FROM LOCAL OFFICIALS

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

Sean Jordan
Supervisor
Leah Blumberg
Clerk/Collector
Donald VanValkenburg
Highway Superintendent

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February 20th. 2015

H. Todd Eames, Chief Examiner
Office of the State Comptroller
Binghamton Regional Office
44 Hawley Street - Suite 1702
Binghamton, New York 13901-4417

Chief Examiner Eames:

Several specific remedies were discussed between me (Town Supervisor), the Town Clerk and the audit team from your office regarding the findings in the Audit Report. I am pleased to announce that all of those remedies have already been established at the time of this writing.

They are as follows:

- A water control account has been established as described in the audit report.
- The Town Board will now review and approve the list of re-levied water accounts at year end.
- All outdated check stock, blank or otherwise, has been voided in the manner recommended by the Comptroller's office.
- The Town now receives from the bank (at no additional cost to the Town) copies of all cancelled checks for all Town accounts.
- Copies of all bank statements and reconciliations, as well as copies of all cancelled checks, are now available for additional review by the Town Board.

I understand the importance of, and am in agreement with, all of the newly established controls. Prior to this audit, I recognized gaps in controls and operational deficiencies, and made every effort to move the Town forward in a secure and responsible manner. This Audit Report has validated and reinforced my efforts, and has provided additional recommendations to further enhance the daily operations of the Town. Additionally, I appreciate the distinction between my

understanding and the Town Board's general lack of understanding of the establishment of these controls.

The Audit Report indicates several deficiencies in bookkeeping duties prior to my taking office and having the bookkeeping duties delegated to a proper bookkeeping authority. Additionally, this Audit Report has reiterated prior audit report findings indicating that the duties of Town Clerk and Bookkeeper are not compatible. Said deficiencies do not need to be repeated, as they are listed in this and several past audit reports, however, their occurrence should not be taken lightly. The Town, with the implementation of recommendations repeatedly made throughout the years by the New York State Comptroller's Office, as well as the appointment of a new Town Clerk on November 1, 2014, has now moved past these prior deficiencies and less than ideal circumstances, and as long as I am Town Supervisor, the Town will not regress from this forward progress.

Respectfully,

Sean Jordan, Supervisor
Town of Jefferson

APPENDIX B

AUDIT METHODOLOGY AND STANDARDS

To accomplish our audit objective, we interviewed Town officials, tested cash disbursements and water rents and reviewed records and reports for the period January 1, 2013 through July 15, 2014.

- We reviewed Board minutes and Town policies and procedures to obtain an understanding of the internal controls over cash disbursements, water rents and records and reports.
- We selected all 37 transactions excluding payroll, totaling \$4,946, payable to the Clerk, Deputy Clerk and Supervisor for review because those disbursements would be most at risk.
- We judgmentally selected payments to 10 personal-use vendors, totaling \$4,546, because those disbursements would be at high risk.
- We judgmentally selected the months of December 2013 and June 2014 to compare the accuracy of the recording and reporting of the records of the Clerk in 2013 and of the bookkeeping service in 2014 for the general fund. We reviewed all 39 transactions, totaling \$22,011, for the month of December 2013 and all 36 transactions, totaling \$17,230, for the month of June 2014.
- We judgmentally selected 44 checks totaling \$59,904 from the general fund for additional testing, including selecting duplicate check numbers and check numbers missing from the check sequence and verified that they were correctly recorded and reported.
- We selected all 20 highway fund transactions, totaling \$14,366, for December 2013 and all 17 transactions, totaling \$16,167, for June 2014. These were judgmentally selected for further review to compare the accuracy of the records of the Clerk in 2013 and of the bookkeeping company in 2014.
- We judgmentally selected 20 highway fund checks from the highway fund, totaling \$93,744, for additional testing, including duplicate check numbers and check numbers that were missing from the check sequence. We verified that the checks were correctly recorded and reported.
- We judgmentally selected all nine transactions for the water fund, totaling \$3,399, for the months of December 2013 and June 2014 for further review to compare the accuracy of the recording and reporting of the records of the Clerk in 2013 and of the bookkeeping service in 2014.
- We reviewed all 61 EFTs, totaling \$800,687, to determine if they were for proper Town purposes.
- We recalculated all 92 water billings to determine if the billings were accurate.
- We randomly selected 17 water customers and their associated 94 water receipts to determine if the receipts were deposited and recorded accurately.

- We recalculated all 43 IRS payments, totaling \$97,438, for 2013 to determine if the payments were accurate.
- We compared calendar year 2013 disbursement totals for the general fund and the highway fund to the AUD and bank statements to determine if they were recorded and reported accurately.
- We judgmentally selected the balance sheet for December 2013 to determine if it balanced properly.
- We judgmentally selected the months of March 2014 and June 2014 and tested all 89 disbursements totaling \$53,317 for the general fund, highway fund and water fund to determine if they were recorded and reported accurately.
- We judgmentally selected the months of March 2014 and June 2014 and tested all 33 revenues totaling \$97,168 for the general fund, highway fund and water fund to determine if they were recorded and reported accurately.

We conducted this performance audit in accordance with GAGAS. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

APPENDIX C

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