



Town of Southold

Financial Operations

Report of Examination

Period Covered:

January 1 — December 31, 2013

2014M-299



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

January 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 Southold, entitled 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*



State of New York Office of the State Comptroller

EXECUTIVE SUMMARY

The Town of Southold (Town) is located in Suffolk County (County), covers approximately 55 square miles and has a population of approximately 23,200. The Town is governed by an elected six-member Town Board (Board) which comprises the Town Supervisor (Supervisor) and five Board members. The Board is responsible for the general management and control of Town finances. The Supervisor is the Town's chief fiscal officer and is responsible for the Town's daily operations.

The Town's 2013 budgeted appropriations were \$47.9 million, funded primarily with real property taxes and State aid.

Scope and Objective

The objective of our audit was to review selected financial operations for the period January 1 through December 31, 2013. Our audit addressed the following related questions:

- Has the Board implemented effective controls over cash management to adequately safeguard Town assets?
- Did Town officials ensure that purchases were made in accordance with the Town's procurement policy?
- Did Town officials ensure that employees were paid correctly and leave accrual records were accurate?

Audit Results

The Board needs to improve controls over cash management to adequately safeguard cash collected in three Town departments. The Town does not have effective policies and procedures to ensure that cash is properly safeguarded in the Receiver of Taxes (Receiver), Town Clerk (Clerk) and Waste Management departments. Additionally, job duties in these departments were not adequately segregated and proper bank reconciliations were not performed.

Our review of the Receiver's office disclosed that accountability for recording collections was compromised because the Receiver's office used a generic username to access the cash receipt software application. Additionally, a running checkbook balance was not maintained in the accounting records, and check disbursements, adjustments and bank transfers were not accounted for in the checkbook.

Further, monthly bank reconciliations were incomplete because deposits in transit,¹ adjustments, bank transfers and other electronic debits from the bank account were not included.

We performed a reconciliation as of December 31, 2013 and found three deposits totaling \$35,903 that were not accounted for in the cash receipts records and two bank accounts that had beginning balances totaling \$23,591 as of December 1, 2013 that should have had no balance.² As a result of these deficiencies, there is an increased risk that Town money could be lost or misappropriated without detection and errors or irregularities could occur and remain undetected.

Our review of the Clerk's office's procedures disclosed deficiencies in the Clerk's records and bank reconciliations, the timeliness of deposits, daily cash reports and accountability within the Clerk's financial system. We were unable to verify if more than \$1 million received by the Clerk's office during our audit period was deposited intact and found that the Clerk's bank balance exceeded the cash receipt records by more than \$7,000 as of December 31, 2013.

We also reviewed 288 Clerk deposits and found that 18 credit card receipts totaling approximately \$6,600 were recorded from three to five days after they were actually received. In addition, nine deposits totaling \$5,850 were recorded from three to five days after they were received. As a result of these deficiencies, there is a risk that money was received but not deposited in the Clerk's bank accounts.

Although the Clerk's office's computer system was capable of allowing staff collecting fees to enter the form of payment received (i.e., cash, check or credit card) into the application software, staff consistently failed to do so. Therefore, the cash, check and credit card totals on the daily reports did not agree with the actual forms of payment listed on the deposit slips and credit card receipts. The Clerk's financial system was further compromised because the Clerk and her employees were all granted administrative access rights to log into the financial system, which allow an individual user to add new users, create and change user access rights, configure certain system settings and override management controls.

Our review of Waste Management procedures disclosed deficiencies in securing transfer station money, timeliness of deposits and accounts receivable adjustments. Transfer station employees drop off daily receipts into a mail slot at the Waste Management Department's administrative office, where they are left unsecured until the next morning. Because the money was not properly secured, there is an increased risk that transfer station money could be lost or stolen.

We found that 14 Waste Management cash receipts totaling about \$22,800 were deposited between one and three days after the cash was collected. Further, while accounts receivable adjustments appeared reasonable, there was no indication of prior supervisory approval for the 47 adjustments we reviewed. As a result, there is an increased risk that errors could occur and go undetected.

The Board also did not ensure that Town officials followed statutory bidding requirements and the Town's procurement policy. We identified \$115,529 in purchases that were not properly bid as

¹ A deposit in transit is cash (currency, coins, checks, electronic transfers) the office received and deposited in the Receiver's bank account which the bank has not yet processed and posted.

² Typically, when the tax collection period ends, the Receiver's bank account has a zero balance (after all tax money has been distributed to the Town and the County).

required by law and approximately \$24,000 in purchases that were made without obtaining quotes as required by Town policy. Further, officials did not develop and follow formal procedures for obtaining professional services. We reviewed payments to seven professional service providers totaling about \$317,000³ and found that Town officials did not solicit competition when obtaining these services. Officials also paid approximately \$23,000 to one professional service provider without the benefit of a written contract. Because of these deficiencies, the Board does not have adequate assurance that goods and services are acquired at the best cost.

Town officials also need to improve internal controls over payroll and accrued leave time records to ensure they are properly designed and operating effectively. While the Board adopted policies and procedures over timekeeping, it did not ensure that these policies and procedures were followed. For example, Town officials did not enforce the Town's timekeeping policies and procedures. As a result, the Town spent more than \$157,000 on an electronic time-management system that was not used effectively. Town employees did not use a consistent method to document time worked or sign their time records to certify the hours worked. As a result, employees were paid without adequate documentation for the hours worked and there was little uniformity in the timekeeping procedures, which could lead to errors or timekeeping abuse.

Finally, the Board did not establish adequate policies and procedures for maintaining leave accrual records or monitoring leave accruals earned and used. Our review of leave accrual records for 25 Town employees and the leave time credited and carried forward during 2013 disclosed no significant discrepancies. However, when accurate leave records are not maintained and periodically reconciled with the time records, Town officials cannot ensure that employees are compensated for the amounts to which they are entitled.

Comments of Local Officials

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

³ See Appendix B for more information on our sample selection.

Introduction

Background

The Town of Southold (Town) is located in Suffolk County (County), covers approximately 55 square miles and has a population of approximately 23,200. The Town is governed by an elected six-member Town Board (Board) which comprises the Town Supervisor (Supervisor) and five Board members. The Board is responsible for the general management and control of Town finances. The Supervisor serves as the Town's chief fiscal officer and is responsible for the Town's daily operations. The Town Comptroller (Comptroller) is responsible for maintaining the accounting records and reviewing the Town's procurement function.

The Town provides various services to its residents including waste management, highway improvements and maintenance, parks and recreation, public safety and general government support. Budgeted appropriations for 2013 totaled \$47.9 million, funded primarily with real property taxes and State aid.

Objective

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

- Has the Board implemented effective controls over cash management to adequately safeguard Town assets?
- Did Town officials ensure that purchases were made in accordance with the Town's procurement policy?
- Did Town officials ensure that employees were paid correctly and leave accrual records were accurate?

Scope and Methodology

We examined the Town's financial records for the period January 1 through December 31, 2013.

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.

Comments of Local Officials and Corrective Action

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

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

Cash Management

The Board is responsible for establishing adequate internal controls to properly safeguard the Town's cash assets. It is important that the Board and Town officials institute adequate policies and procedures to ensure that all money the Town receives is properly safeguarded, receipted and recorded. Policies and procedures should address Town-wide receipt practices to ensure consistency and coordinate departmental operations.

An important component of internal controls is properly segregating duties to ensure that no individual controls all phases of a transaction or implementing compensating controls when segregating duties is not feasible. For example, Town officials could have someone other than those responsible for collecting and reconciling cash review cash receipt records and perform monthly bank reconciliations to verify that the records are timely, accurate and complete. All receipts should be deposited intact in a timely manner.⁴

The Town has 10 departments⁵ whose operations involve collecting cash receipts. With one exception, each department collects,⁶ records, deposits and reports its own receipts. However, the Town has no formal policies and procedures in place to govern collecting and handling cash receipts. We reviewed the operations of the Receiver of Taxes (Receiver), the Town Clerk (Clerk) and the Waste Management Department, which are the departments with the highest volume of cash receipts.

The Board needs to improve controls over cash management to adequately safeguard cash collected in three Town departments. The Town does not have effective policies and procedures to ensure that departmental cash is properly protected by the Receiver, the Clerk and the Waste Management departments. Additionally, job duties in these departments were not adequately segregated and proper bank reconciliations were not performed.

Our review of the Receiver's office disclosed deficiencies in real property tax records and accountability over tax collections. We also identified deficiencies in the Clerk's office's records, reports and accountability. Finally, our review of Waste Management's

⁴ Intact means in the same amount and form (cash or check) as received.

⁵ The Receiver of Taxes, Town Clerk, Justice Court, Building Department, Waste Management, Recreation Department, Human Services, Police Department, Trustees' of the Freeholders and Zoning Board of Appeals

⁶ The Building Department collects cash receipts but transfers the amounts collected to the Town Clerk's office for recording and depositing.

procedures disclosed deficiencies in timeliness of deposits, securing transfer station money and accounts receivable adjustments. As a result of these deficiencies, there is an increased risk that Town money could be lost or misappropriated or errors and irregularities could occur and remain undetected.

Receiver of Taxes

The Receiver is responsible for collecting and depositing payments, maintaining accurate real property tax receipt records, reporting the amounts collected and promptly remitting tax payments. The Receiver is further required to ensure that all tax money collected is deposited intact and remitted to the Supervisor within specified timeframes.⁷

All money in the tax collection bank account should be distributed to the Town and County when the tax collection period ends. Additionally, an up-to-date checkbook balance should be maintained and periodically reconciled with the bank balance to ensure cash accountability. Finally, to help ensure individual accountability over tax collection, each employee should use their own individual username to access the Receiver's office software application when recording cash collected, to ensure that tax collection activity can be associated with a specific employee.

For the 2013 tax year, the Receiver's office collected more than \$115 million in revenues.⁸ Our review of procedures in place in the Receiver's office disclosed a failure to segregate duties or implement compensating controls and deficiencies in accounting records and bank reconciliations. As a result, there is an increased risk that the Town may not be collecting all the tax revenue to which it is entitled.

Segregation of Duties – The Receiver was responsible for performing many incompatible duties, such as preparing and making all bank deposits and performing bank reconciliations, and was the sole signatory on the Receiver's office bank accounts. Concentrating such duties (i.e., cash custody reconciliations and disbursing funds) with one individual with little or no oversight weakens internal controls and significantly increases the risk that errors or irregularities could occur and remain undetected and uncorrected.

Accountability for recording collections was also compromised because the Receiver's office used a generic user name to access the cash receipt software application. Although employees had their own usernames and passwords, during high collection periods,⁹ employees

⁷ By law, all money collected should be deposited within 24 hours from when it is received and remitted to the Supervisor by the 15th of the month following the month it is received.

⁸ Real property taxes for the 2013 tax year were collected from December 1, 2012 through May 31, 2013.

⁹ December and May

used either their individual username or the generic username to record collections. As a result, accountability over the real property taxes collected was diminished and tax collection activity could not be associated with an individual employee.

Because of a weak control environment, we reviewed all cash records and deposits made by the Receiver's office during May 2013, totaling \$43.5 million, and during December 2013, totaling \$31.6 million,¹⁰ to determine if deposits were made intact and deposited in a timely manner. Although we did not find any discrepancies, allowing the Receiver to be responsible for incompatible duties without compensating controls increases the risk that property tax receipts might not be deposited and irregularities could occur and remain undetected and uncorrected.

Records and Bank Reconciliations – Although the Receiver maintained computerized cash receipts records and recorded check disbursements in the checkbook register, he did not maintain a running checkbook balance in the accounting records or perform proper bank reconciliations.

The deputy tax receiver reconciled deposits with the cash receipts recorded in the computer software application. However, because the Receiver did not maintain a running book balance and account for check disbursements, adjustments and bank transfers, the deputy's reconciliation was inadequate. Further, the Receiver's monthly bank reconciliations were incomplete because deposits in transit,¹¹ adjustments, bank transfers and other electronic debits from the bank account were not included.

We performed a reconciliation as of December 31, 2013 and found the following discrepancies:

- Three deposits totaling \$35,903 were not accounted for in the cash receipts records. These deposits were for real property tax payments that were returned due to insufficient funds.
- Two bank accounts had beginning balances totaling \$23,591 as of December 1, 2013 that should have had no balance.¹² The Receiver stated that these balances represented real property tax refund checks that were outstanding and that letters were

¹⁰ We reviewed the two months that the Receiver's office collects the majority of tax payments.

¹¹ A deposit in transit is cash (currency, coins, checks, electronic transfers) the office received and deposited in the Receiver's bank account which the bank has not yet processed and posted.

¹² Typically, when the tax collection period ends, the Receiver's bank account has a zero balance (after all tax money has been distributed to the Town and the County).

sent to property owners requesting an attestation that the checks have not been cashed.

Although the Receiver was able to provide an explanation and support for these discrepancies, without adequate cash records and timely and complete bank reconciliations, there is an increased risk that error or irregularities could occur, go undetected and remain uncorrected.

Town Clerk

The Clerk is responsible for collecting payments for dog, sporting and marriage licenses and the fees associated with her role as the Town's registrar of vital statistics. Additionally, the Clerk records the fees collected by the Building Department¹³ and the fees collected at the Town's beaches for parking permits. Properly recording the amount and form of payment received (i.e., cash or check) enables Town officials to trace these transactions from the point of collection through the accounting records to bank deposits and monthly reports to help ensure accountability. Further, to help ensure individual accountability over fees collected in the Clerk's office, employees should not be granted administrative access rights to the Clerk's office's financial system and each employee should use a unique username and password to access the system. This helps ensure that transaction activity can be associated with an individual employee.

The Clerk's office deposited cash receipts totaling more than \$1 million during 2013 without adequate processes and procedures in place over financial operations. Our review disclosed deficiencies in the Clerk's records, bank reconciliations, timeliness of deposits, reports and accountability within the Clerk's financial system and a failure to segregate duties or implement compensating controls.

Records and Bank Reconciliations – Although the Clerk's deputy maintained cash receipts records (containing the receipts listed on daily reports from the software application), she did not maintain a running cash balance in the accounting records, did not record check disbursements in the checkbook register and did not properly reconcile the bank account. When performing bank reconciliations, the deputy simply listed the deposits and checks that cleared the bank. Although she reviewed monthly bank statements to determine whether all deposits were included and all checks that cleared the bank were for proper Clerk expenditures, she did not account for outstanding checks or deposits in transit in the reconciliations.

As a result of our review, the deputy clerk reconstructed all 2013 monthly bank reconciliations, established a running cash balance

¹³ The Building Department receipts are recorded and deposited by the Clerk's office. The Building Department collects the receipts and transfers the collections to the Clerk's office.

and recorded check disbursements in the manual cash register for the entire year. We reconciled the bank statements and compared the cash balances with the Clerk's updated manual cash records and found that the bank balance exceeded the cash register balance by more than \$7,000 at year-end. The deputy was unable to provide an explanation for this difference.

Because of inaccurate and incomplete records, we reviewed all 288 deposits made during our audit period to determine if they were deposited intact and in a timely manner. The deposits we reviewed included cash collected for permits, licenses and certificates; Building Department receipts; and parking permits receipts collected at the Town beaches by beach attendants, totaling more than \$1 million.

While these collections were deposited in a timely manner, they were not always recorded in the records in a timely manner. Specifically, we found that 18 credit card receipts totaling approximately \$6,600 were recorded from three to five days after they were actually received. All of these receipts were for fees collected at the Building Department. In addition, we found that nine deposits made by beach attendants totaling \$5,850 were recorded from three to five days after they were received. The Clerk's records were not sufficient to determine if funds deposited by the Clerk's office were intact.

Although the computer system used in the Clerk's office was capable of allowing staff collecting fees to enter the form of payment received (i.e., cash, check or credit card) into the application software, staff consistently did not do so. Therefore, the cash, check and credit card totals on the daily reports for the audit period did not agree with the actual form of payment listed on the deposit slips and credit card receipts. For example, on February 26, 2013, the daily report indicated that the Clerk received \$381.98 in cash, \$850 in checks and \$0 in credit card receipts. However, the deposit slip showed receipts of \$75 in cash, \$1,117.98 in checks and \$39 in credit cards. As a result, there is an increased risk that money collected in the Clerk's office could be lost or misappropriated.

Clerk's Financial System – Accountability within the Clerk's financial system was weakened because the Clerk did not adequately segregate incompatible duties within the office. The Clerk did not ensure that all office employees had unique usernames and passwords to gain access to the financial system. For example, one deputy clerk used two usernames and all clerks used a generic username to process marriage licenses. This reduced accountability within the financial system because, if any of those individuals entered inappropriate information, the identity of that individual could not be determined.

The Clerk's financial system was further compromised because the Clerk, two deputies, two clerks and two information technology employees were all granted administrative access rights to log in to the financial system. An individual who has system administrative rights can add new users, create and change user access rights, configure certain system settings and override management controls.

Due to the lack of accountability, we reviewed the receipt numbering sequence listed on a report generated from the application software on four days during our audit period¹⁴ to determine if all receipts were included and accounted for. Our review included 219 receipts totaling \$17,244. We found three receipts that were unaccounted for.

The deputy was able to provide us with support for two receipts totaling \$90¹⁵ after performing a search in the application software. However, these supporting documents were not maintained in the daily records for review. Officials were unable to determine the dollar amount or provide supporting documentation for the remaining receipt. When receipts are not properly accounted for, there is a risk that money was received but not deposited, in the Clerk's bank accounts.

Waste Management

The Waste Management Department (Department) charges customers for household garbage, yard waste, metal, tires and construction and demolition debris brought to the transfer station for disposal. The Department also sells garbage bags for customers use.

Town officials should have adequate controls over money collected at the Town's transfer station. Additionally, authorizing transactions, recordkeeping, and receiving and handling cash should not be performed by same individual. When the individual who handles cash can authorize and make account adjustments and is also involved in billing and maintaining the accounts receivable records, there is an opportunity to misappropriate funds and conceal the theft by manipulating records.

During our audit period, the Department collected revenues totaling approximately \$2.3 million. However, the Town's transfer station did not have adequate controls in place over collecting money. Our review of Department's procedures disclosed deficiencies in depositing and securing transfer station money, and a failure to segregate duties or implement compensating controls over billing and accounts receivable duties.

¹⁴ We selected one day from each quarter of 2013 that fell in the middle of the quarter.

¹⁵ These receipts were for marriage licenses (\$40) and permits (\$50).

Transfer Station Receipts – Between one and three scale operators are assigned to the transfer station each day,¹⁶ and they charge customers for waste and debris brought to the station for disposal. All scale operators use the same cash drawer. Additionally, when one scale operator is assigned to work, this employee must ensure that the transfer station is not left unattended. When the assigned scale operator takes a break, another Department employee provides coverage at the transfer station scale house. However, scale operators do not count the cash drawer prior to or after the Department employee is on duty.

Further, the assigned scale operator drops off the daily collections in an unsecured mail slot at the Department’s administrative office at the end of each workday. While locked at this time, several employees have access to this office. As a result, money is left unsecured until the next morning (for Sunday through Thursday collections) and through the weekend for money collected on Friday and Saturday.

We examined the transfer station cash receipts for a two-week period in June 2013. We reviewed 14 cash deposits totaling about \$22,800 and 14 credit card receipts of about \$9,750 to determine whether the cash deposits were made intact and in a timely manner and if the credit card receipts were accurately recorded and deposited in the bank.

All the cash deposits were deposited intact and all the credit card receipts were accurately recorded and deposited in the bank. However, cash deposits were made between one and three days after the cash was collected. Because money was not properly secured (e.g., kept in a safe) and deposited in a timely manner, there is an increased risk that transfer station money could be lost or stolen.

Accounts Receivable – The transfer station allows commercial business customers to charge for debris disposal and be billed at a later date. The Department clerk’s billing and accounts receivable duties were incompatible with no compensating controls in place.

The clerk prepares invoices, collects payments, posts payments in the accounts receivable ledgers and prepares and makes bank deposits. Moreover, she was able to make account adjustments, such as voiding invoices or changing the billing or payment amounts, without approval from a supervisor.

Due to this lack of segregation of duties, we reviewed the Department’s receivable activities for the last two weeks of June 2013, which

¹⁶ The transfer station is open daily from 7 a.m. to 5 p.m. (except holidays). More operators are needed and assigned on weekends and during the transfer station’s busiest months (May through September).

included 14 deposits composed of multiple payments totaling \$204,080. These deposits were made intact and in a timely manner. We also reviewed 47 adjustments made during the same time period, totaling \$2,490. While all adjustments appeared to be reasonable, we found no indication of any prior supervisory approval.

When the Department clerk's duties are not segregated and compensating controls are not in place, it increases the risk that errors can occur and go undetected. Further, it provides an opportunity to misappropriate funds and conceal shortages by manipulating records.

Recommendations

The Board should:

1. Ensure that an adequate system of policies and procedures is established over collecting and recording cash receipts by Town departments and officials.

Town officials should:

2. Properly segregate duties in the Receiver's and the Clerk's offices so that one individual is not responsible for preparing and making deposits, signing checks and reconciling bank accounts or provide appropriate compensating controls.
3. Require that unique usernames and passwords are used for software applications and administrative rights are restricted to only those individuals who need them.
4. Prepare monthly bank reconciliations in a timely manner.
5. Maintain adequate cash records so that the cash balance can be compared to the reconciled bank balance each month.
6. Improve internal controls over Waste Management accounts receivable. At a minimum, cash handling and maintaining receivable records should be segregated. Where segregating incompatible duties is not feasible, officials should establish compensating controls, such as implementing supervisory review procedures.

Purchasing

An effective procurement process helps the Town obtain the right quality and quantity of services, materials, supplies and equipment at the best price and in compliance with the Town's procurement policy and other applicable legal requirements. By seeking competition, such as obtaining verbal or written quotes from a number of potential vendors, Town officials can ensure that procurement is not influenced by favoritism, extravagance or fraud.

General Municipal Law (GML) requires that purchases in excess of \$20,000 and public work contracts in excess of \$35,000 be publicly advertised for competitive bidding. Exceptions to the bidding requirements include purchases costing less than these bidding thresholds or those made from contracts awarded by the State or the county in which the local government resides. GML further requires that the Town's adopted procurement policy provides guidance for all purchases not subject to competitive bidding, including professional services, thus assuring taxpayers that public funds are prudently and economically used.

Obtaining written proposals through a request for proposal (RFP) process is an effective way to procure professional services at the best value and document how service provider selections were made. In addition, when acquiring professional services, the Board and service provider should enter into a written agreement indicating the contract period, services to be provided and basis for compensation.

The Board did not ensure that Town officials followed statutory bidding requirements and the Town's procurement policy. We identified \$115,529 in purchases that were not properly bid as required by law and approximately \$24,000 in purchases that were made without obtaining quotes as required by Town policy. Further, officials did not develop and follow formal procedures for obtaining professional services and did not have written contracts in place with all professional service providers. As a result, the Board does not have adequate assurance that goods and services are acquired at the best cost.

Competitive Bidding

Town officials did not comply with GML requirements or the Town's procurement policy for purchases that required competitive bidding. We reviewed seven purchases¹⁷ totaling \$328,715 that exceeded the

¹⁷ The Town made multiple payments for some purchases tested (e.g., automotive repair). We grouped the vendor history data to include vendors that were paid more than \$20,000 for goods and services over the course of our audit period. The Town made disbursements exceeding \$20,000 to 70 vendors. For more information on our sample selection, see Appendix B.

bidding threshold. Purchases from three vendors totaling \$115,529 were made without public bids or were not obtained through State or County contracts. For example, the Town obtained automotive repair services for police vehicles totaling \$88,710 from two vendors¹⁸ without competitive bids.

The police chief told the Comptroller that he considered the services provided to be from a sole source vendor and therefore exempt from the competitive bidding. Additionally, purchases for emergency vehicle items, such as lighting and radios, totaling \$26,819 were not competitively bid. By not following GML and the Town's own procurement policy, Town officials cannot assure taxpayers that purchases are made in the most economical manner.

Written Quotes

The Town's procurement policy requires that department heads and Town officials obtain three written quotes for purchases costing between \$1,000 and \$9,999 and public work contracts costing between \$999 and \$34,999. Documented verbal quotes, while not required, are preferred for purchases costing less than \$1,000.

Department heads and Town officials did not always comply with the Town's procurement policy. We reviewed 12 purchases¹⁹ costing between \$3,000 and \$9,999 to determine if the three required written quotes were obtained. The documentation for four purchases totaling about \$24,000 did not include any evidence that written quotes were obtained. For example, the Town purchased lights from a local vendor for \$9,680. We identified the same lights available from another vendor for approximately \$2,600 less than what the Town paid. The failure to obtain quotes in accordance with the Town's policy can result in the Town's incurring higher than necessary costs for the goods and services purchased.

Professional Services

The Town's procurement policy does not require soliciting written proposals or quotes or other competitive methods when contracting for professional services. In 2013 the Town paid \$798,108 to 38 professional service providers comprising legal services, external audit services and other various professional services, such as engineering, architectural and consultation services.

We reviewed payments made during our audit period to seven of these providers totaling about \$317,000²⁰ (e.g., legal, external audit, engineering and consulting services) to determine if the services were obtained through a competitive process. Town officials did not solicit

¹⁸ These included services totaling \$58,037 from one vendor and \$30,673 from another.

¹⁹ See Appendix B for more information on our sample selection.

²⁰ Ibid.

competition when obtaining these professional services. For example, Town officials paid more than \$95,000 for external auditing services during the audit period without seeking competition.

We also reviewed the payments made to these professional service providers to determine if the services were supported by contracts and to determine if the payments complied with the contracts' terms. The Town had contracts with six professional service providers and payments made to these professional service providers agreed with the related contracts. However, Town officials paid an attorney approximately \$23,000 without the benefit and protection of a contractual agreement.

When the Board does not require using competition to obtain professional services, Town officials and taxpayers cannot be assured that the Town is receiving qualified and necessary professional services as economically as possible. Additionally, written contracts provide protection to ensure that the Town receives the appropriate services for the agreed-upon fees.

Recommendations

The Board should:

7. Ensure that Town officials comply with GML and the Town's policy requirements when obtaining goods and services.
8. Consider revising its procurement policy to require Town officials to obtain professional services through a competitive process.
9. Enter into written agreement with all professional service providers, indicating the contract period, the services to be provided, the timetable for completion and the basis for compensation.

Payroll

Payroll comprises a significant portion of the Town's budget. To properly control and account for these costs, the Board must adopt policies and procedures that include provisions to ensure that time worked and leave time earned is properly approved, documented, monitored and controlled so employees are paid only those amounts to which they are entitled. Town officials should periodically monitor these procedures to determine if they are being correctly and consistently applied. During 2013, salaries and wages, including overtime, totaled more than \$10.1 million. The significant costs involved highlight the importance of good controls over timekeeping and leave accrual records.

Town officials did not ensure that employees were paid correctly or that leave accrual records were accurate, because controls over payroll and leave time were not properly designed or operating effectively. While the Board adopted policies and procedures over timekeeping, it did not ensure that these policies and procedures were followed. As a result, Town officials spent more than \$157,000 on a timekeeping system that was not used effectively. Town employees did not use a consistent method to document time worked or sign time records certifying that they actually worked the stated hours. The lack of uniformity in timekeeping procedures could lead to errors or abuse. Furthermore, the Board has not established adequate policies and procedures for maintaining leave accrual records or monitoring leave accruals earned and used. These weaknesses increase the risk of error and for abuse of leave time benefits.

Timekeeping

In January 2008, the Board adopted policies and procedures for implementing an electronic time-management system (system) at a cost of about \$100,000. Since implementation, Town officials spent an additional \$56,000 for upgrades to the system. According to the Board-adopted timekeeping policy, Town officials implemented this system to automate the payroll process, eliminate unnecessary paperwork and provide for greater accuracy and consistency across departments.

The timekeeping system assigns each employee an individual user identification and unique password. Employees are required to punch into this system through ID terminals or on their workstations upon arrival and departure from work. At the end of each pay period, the department heads must approve and sign off on each employee's timecard for an employee to be paid. When the system was initially implemented in 2008, the policy required employees of four

departments²¹ to use the system. However, in November 2010 the policy was amended to include all Town departments' employees unless the Board exempted them.

In addition to the Board-adopted policies and procedures for timekeeping, the Town has an employee handbook that includes additional timekeeping provisions. The handbook requires employees to sign the time records to certify the accuracy of time worked in addition to the department head certification. Signatures on time records attest to the records' accuracy and serve as supporting documentation for payroll processing.

However, all Town employees did not use the Board-implemented system. Instead, several departments²² continued to use various manual time sheet forms to record employees' time worked, even though these departments did not receive a Board exemption from using the system. Additionally, because departments used varying time sheets, employees did not record their work time in a consistent manner.

For example, employees working at the Town Hall used the system, which showed their workdays' start and finish, their time worked certification and approval by the department head. However, Highway Department employees do not complete their own time sheets. Instead, a clerk in the department enters information from a daily attendance sheet maintained by the Deputy Highway Superintendent onto individual time sheets. Highway Department employees did not review or sign these individual time sheets.

Further, departments not using the system did not submit time sheets for full-time employees to the payroll clerk.²³ The only information provided to the payroll clerk for these employees were payout requests for overtime worked.²⁴ The payroll clerk added full-time employees' salary information into the system at the beginning of the year and never verified that employees actually worked or charged the proper leave accruals when not working.

We reviewed time sheets and payroll journals for 25 employees paid during one pay period²⁵ in February 2013. Although the hours

²¹ Town Hall, Town Hall Annex, Human Resource Center and Recreation Center. Transfer Station, Highway and Public Safety were not required to initially use the time-management system.

²² Highway Department, Public Safety and Waste Management.

²³ The payroll clerk reviewed non-salaried employee time sheets.

²⁴ Based on the Town's collective bargaining agreement, employees have the option to accrue overtime worked as compensatory time off or to be paid for it.

²⁵ Refer to Appendix B for further information on our sample selection.

worked reported on the time sheets agreed with the payroll journals, Town officials have no assurance that the time employees worked was accurately recorded because time sheets were not always signed by employees and department heads. We found seven time sheets that were not signed by the employees and six that were not signed by the department heads.

The Board's failure to require all departments to use the system has resulted in employees being paid without adequate documentation for the hours worked.

Leave Accruals

The Board should ensure that all employee leave time is verified, approved and monitored. This can be accomplished by establishing and implementing policies and procedures to provide clear guidance to Town officials on how leave time is earned, used and accounted for. Additionally, it is essential that the Town maintain accurate leave accrual records to ensure that each employee's leave balance is accurate. Proper accounting for employee leave accruals requires that leave records are periodically reconciled with time sheets and department records. Finally, paid leave should be granted in accordance with formally established Town policies and applicable collective bargaining agreements (CBAs).

The Board did not establish adequate written policies and procedures for maintaining leave accrual records or monitoring accrued leave time earned and used. Consequently, Town officials did not use a consistent method to record and account for employees' accrued leave time and department heads established informal procedures to record leave time earned and used within their departments.

Town employees are granted vacation, sick and personal paid leave time according to the positions held and the length of Town employment, in accordance with CBAs. The Town's employee handbook requires department heads to submit signed and approved leave request forms to the accounting department with time sheets. Town policy requires department heads to submit a benefit time sheet (monthly document) to the accounting department for review, which lists each employee and the accrued leave time used with the approved leave request forms by the 10th day of each month.

The Town's payroll is processed biweekly, with no payroll lag.²⁶ Therefore, the payroll clerk must process payrolls before she can

²⁶ A lag in payroll means that an employee performs services during a period and is subsequently paid for such services on a pay date that occurs at the end of the period. Lags in payroll are implemented to allow time for the individual processing payroll to receive employees' time sheets and process payroll based on the actual recorded hours worked and leave time used during the pay period.

determine if an employee had adequate accrued leave time to cover absences. In addition, approved leave request forms were not always submitted with the monthly document. Thus, accounting department personnel could not properly determine if leave accrual balances were accurate.

Further, because time sheets were not always prepared by individual employees or signed by department heads, leave accrual balances could not be verified for accuracy. Lastly, the Highway Department and the Police Department submitted the required monthly document annually. The lack of reliable and timely time and attendance records limits the Town officials' ability to maintain accurate payroll and leave accrual records and ensure that employee leave balances are accurate.

We reviewed the leave accrual records maintained for 25 Town²⁷ employees to determine whether leave time was properly deducted from their leave accrual balances during 2013. We also determined whether leave time credited and carried forward during 2013 agreed with the CBA.

While we found no significant discrepancies, because the leave accrual records were not appropriately maintained, Town officials have no assurance that leave time used is accurately recorded. Additionally, when accurate leave records are not periodically reconciled with time records, officials cannot determine the proper amount of separation payments for employees either retiring or resigning from their positions and ensure that such employees are compensated for the amounts to which they are entitled. Further, there is a risk of errors and the potential for abusing leave benefits.

Recommendations

10. The Board and Town officials should enforce and monitor timekeeping policies and ensure that all Town employees are using the Town's timekeeping system to provide greater accuracy and consistency across departments.
11. The Board should establish adequate policies and procedures for tracking and monitoring employee leave accruals to ensure these policies are followed.

²⁷ See Appendix B for more information on our sample selection.

APPENDIX A
RESPONSE FROM LOCAL OFFICIALS

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

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OFFICE OF THE SUPERVISOR
TOWN OF SOUTHOLD

January 22, 2015

VIA EMAIL and FIRST CLASS MAIL

Mr. Ira McCracken, Chief Examiner
Office of the State Comptroller
NYS Office Building, Room 3A10
250 Veterans Memorial Highway
Hauppauge, NY 11788-5533

RE: Town of Southold Audit – Preliminary Draft Findings

Dear Mr. McCracken:

By way of response to your letter dated December 23, 2014, please find below the Town's responses to your Office's preliminary draft findings:

Recommendation 1:

The Board should ensure that an adequate system of policies and procedures is established over collecting and recording cash receipts by Town departments and officials.

Town Response:

Several improvements were made during the course of the audit to more adequately safeguard cash collections. Furthermore, the Town Board intends to conduct a thorough review of all policies and procedures in place for collecting and receiving cash receipts by all Town Departments and revise procedures where necessary to ensure proper control.

Recommendation 2:

Town officials should properly segregate duties in the Receiver and Clerk offices so that one individual is not responsible for preparing and making deposits, signing checks and reconciling the bank accounts or provide appropriate compensating controls.

Town Response:

The Town Board is reviewing current procedures with the Town Clerk and Tax Receiver and will direct, where necessary, that said procedures be revised to ensure proper segregation of duties.

Recommendation 3:

Town officials should require that unique user names and passwords are used for software applications and administrative rights are restricted to only those individuals who need them.

Town Response:

Unique user names and passwords are required by the Town's Records Confidentiality and Security Policy, Sections B(5) and C(1). The Town Board will consider revisions to the current policy to add additional methods to ensure secure access to software applications used by Town employees.

Recommendation 4:

Town officials should prepare monthly bank reconciliations in a timely manner.

Town Response:

The Town Board will request that the Town Clerk and Tax Receiver review procedures for reconciliations to ensure timeliness.

Recommendation 5:

Town officials should maintain adequate cash records so that the cash balance can be compared to the reconciled bank balance each month.

Town Response:

The Town Clerk and Tax Receiver have implemented revised procedures creating an internal general ledger which is routinely reconciled to bank statements. Additional measures will be considered.

Recommendation 6:

Town officials should improve internal controls over Waste Management accounts receivable. At a minimum, cash handling and maintaining receivable records should be segregated. Where segregating incompatible duties is not feasible, officials should establish compensating controls, such as implementing supervisory review procedures.

Town Response:

The Town Board will review and consider revisions to the Waste Management District's procedures to segregate cash handling and improve internal controls relating to cash handling

and accounts receivable and consider supervisory review procedures, including prior approval for any adjustments made to accounts receivable.

Recommendation 7:

The Board should ensure that Town officials comply with General Municipal Law and the Town's policy requirements when obtaining goods and services.

Town Response:

The Town Board has reviewed its Procurement Policy to ensure compliance with the General Municipal Law and will reissue directives to all Department Heads regarding compliance prior to purchasing.

Recommendation 8:

The Board should consider revising its Procurement Policy to require Town officials to obtain professional services through a competitive process.

Town Response:

The Town Board will consider an amendment to its Procurement Policy to address competitive bidding for professional services.

Recommendation 9:

The Board should enter into written agreements with all professional service providers, indicating the contract period, the services to be provided, the timetable for completion and the basis for compensation.

Town Response:

Where practicable, the Town Board will direct the Town Attorney to draft a professional services agreement that includes all essential terms of the engagement.

Recommendation 10:

The Board and Town Officials should enforce and monitor its timekeeping policies and ensure that all Town employees are using the Town's timekeeping system to provide greater accuracy and consistency across departments.

Town Response:

The Town Board will review existing timekeeping policies with each Department Head and make amendments where necessary to create consistency and improve accuracy.

Mr. Ira McCracken
Page 4 of 4
January 21, 2015

Recommendation 11:

The Board should establish adequate policies and procedures for tracking and monitoring employee leave accruals to ensure these policies are followed.

Town Response:

The Town Board will review existing policies and procedures for tracking leave accruals for all employees and direct compliance and draft amendments where practicable.

Thank you for your attention. If you have any questions, feel free to contact the undersigned.

Very truly yours,

Scott A. Russell
Supervisor & Chief Financial Officer

SAR/lk

APPENDIX B

AUDIT METHODOLOGY AND STANDARDS

Our overall goal was to assess the adequacy of internal controls put in place by officials to safeguard Town assets. To accomplish this, we performed an initial assessment of internal controls so that we could design our audit to focus on those areas most at risk. Our initial assessment included evaluations of financial condition, fiscal records and reports, cash management, purchasing, claims processing, payroll, information technology, capital projects, grants and the following departmental operations: Town Clerk's office, Receiver of Taxes' office, Highway, Parks and Recreation, Fleet Services and the Ferry District.

During the initial assessment, we interviewed Town officials, performed tests of transactions and reviewed pertinent documents such as policies, Board minutes and financial records and reports. After reviewing the information gathered during our initial assessment, we determined where weaknesses existed and evaluated those weaknesses for the risk of potential fraud, theft and professional misconduct. We then decided upon the reported objective and scope by selecting for audit those areas most at risk. We selected cash management, purchasing and payroll for further audit testing.

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

Cash Management:

- We reviewed policies and procedures related to the management of cash.
- We interviewed Town officials and employees responsible for the management of cash and maintaining the cash records.
- We reviewed cash receipts records and reports, cash ledgers and bank reconciliations to determine if these records were accurate and maintained in a timely manner.
- We reviewed the controls in place over the computer software application used to record cash transactions.
- We performed a bank reconciliation for May 2013 for one of five bank accounts maintained by the Receiver. We selected the bank account that contained the highest volume of cash deposits. Due to the lack of a cash ledger, we developed a cash balance to reconcile with the bank balance using reports generated from the computer application software and the corresponding bank statements for that month.
- We reviewed two months of tax collections during our audit period to determine if deposits were made intact and in a timely manner. We reviewed the collections made during May and December 2013. We selected these two months because this is the time period in which the office receives the highest volume of receipts. We compared reports generated from the computer application software with deposit slips and the bank statements.

- We performed a bank reconciliation for December 31, 2013 for the bank account maintained by the Town Clerk. We obtained the cash ledger maintained by the Clerk's deputy and the December 2013 bank statements. We selected December to determine if there was any discrepancy at year-end.
- We reviewed all 288 deposits made by the Clerk's office to determine if deposits were made intact and in a timely manner.
- We reviewed the receipt numbering sequence for four days of cash collections at the Clerk's office during our audit period to ensure that the receipts for these days were issued in sequential order. To select the four days, we chose one day from the middle of each quarter.
- We reviewed the cash collected in the scale house at the Waste Management Department for a two-week period during June 2013 to determine if deposits were made intact and in a timely manner. We selected June due to the higher volume of cash collected during the summer months.
- We reviewed the accounts receivable collected at the Waste Management Department for the last two weeks in June 2013 to ensure that deposits were made intact and in a timely manner.

Purchasing:

- We reviewed the Town's procurement policy.
- We interviewed Town officials and employees to obtain an understanding of internal controls over the procurement process.
- We obtained a list of all vendors paid during the audit period and compared all claims packages for seven professional service providers to determine the vendor list's reliability.
- We reviewed purchases for seven vendors paid more than \$20,000 during our audit period. We selected our sample by sorting the Town's vendor history to include all vendors that were paid more than \$20,000 for goods and services excluding utilities, payroll, local municipalities and professional service providers. We determined that the Town made disbursements exceeding \$20,000 to 70 such vendors. We then used a random number generator to select 10 percent of these vendors. We reviewed purchases from these vendors to determine the following:
 - o If the purchases were subject to competitive bidding requirements per the Town's policy and GML, and were competitively bid. If not competitively bid, we verified whether the purchases were made pursuant to a valid State or County contract.
 - o If the Board approved and awarded a bid to the vendor. If the Town selected the vendor in connection with a competitive bid, we reviewed the bid documents to verify that the Town selected the lowest responsible bidder.

- o If the purchases were made in accordance with the bid specifications. If the vendor was not approved in the Board minutes, we made inquiries of Town officials regarding the vendor and the purchases made.
- o If the purchases were awarded to the lowest responsible bidder or otherwise and, if not, whether an explanation was provided of why the lowest bid was not selected.
- Whether or not reviewed 12 purchases costing between \$3,000 and \$9,999 during our audit period to determine adherence with the procurement policy and whether written RFPs were issued and written quotes were obtained from at least three vendors. We selected our sample by sorting the Town's vendor history to include all vendors that were paid between \$3,000 and \$9,999 for goods and services excluding utilities, payroll, local municipalities and professional service providers.²⁸ If written quotes were not obtained, we made inquiries to determine if a lower price for goods was available.
- We reviewed payments made to the seven highest paid professional services providers during our audit period. We selected our sample by sorting the vendor history to include all professional service vendors, excluding insurance providers. We reviewed all claims packages, contracts and Board resolutions to determine if payments to these providers were made in accordance with contractual agreements. We also made inquiries of Town officials about RFPs prepared for these services provided.

Payroll:

- We interviewed Town officials and employees and reviewed policies and procedures relating to payroll, timekeeping, leave accruals, CBAs and the employee handbook to identify controls over payroll and gain an understanding of the Board-adopted electronic time-management system.
- We interviewed Town officials and department officials to determine the process used to record time worked and leave accruals used.
- We reviewed CBAs and the employee handbook to determine how much of each type of accrual (vacation, sick, personal and compensatory time) each employee was entitled to earn during the audit period.
- We reviewed leave accrual records for 25 employees on payroll during February 2013. We selected our sample to specifically include five highway employees, five waste water management department employees and fifteen employees from the remaining Town departments. We ensured that our sample included both full-time and part-time employees and employees that were paid overtime. We chose February because that month had the highest overtime payouts. We tested these leave records to determine the following:
 - o If employees were paid accurately by comparing the payroll processed by the accounting department with individual time sheets.

²⁸ We then selected the first and last purchase for each thousand dollar increment starting at \$3,000 and ending at \$9,000 (there were no purchases in the \$8,000 threshold).

- o If time sheets were signed by individual employees and department heads.
- o If leave accruals earned and used were in accordance with CBAs and the employee handbook and if the amounts of leave carried over were in excess of that allowed by these agreements.
- o If approved leave slips were submitted to the accounting department.

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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