

LONG ISLAND WATER CONFERENCE

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THE VALUE OF INTERNAL AUDITS

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Purpose of the Internal Audit Function

- Review of financial and operational policies and procedures
- Test and evaluate internal controls
- Review the efficiency, effectiveness and compliance of the water district's operations
- Perform a risk assessment to minimize risk to the water district
- Monitor internal controls during the year

Key Factors that Distinguish and Differentiate Internal and External Auditing

◎ *Focus*

- External Audit
 - Primarily attests to the financial statements and internal controls relative to financial reporting
- Internal Audit
 - Provides financial and operational assurance relative to district objectives.

Key Factors that Distinguish and Differentiate Internal and External Auditing

Financial

1. General Controls
2. Cash Receipts/Revenues
3. Cash Disbursements & Procurement
4. Financial Reporting
5. Capital Projects
6. Fixed Assets
7. Payroll

Non-Financial

1. Liability Management
2. Human Resource Issues
3. Attendance
4. Budget Development
5. Information Technology

Key Factors that Distinguish and Differentiate Internal and External Auditing

⊙ *Standards*

● External Audit

- Must follow appropriate accounting and auditing standards including

- GASB and FASB
- Generally Accepted Audit Standards
- Government Audit Standards (Yellowbook)

○ Internal Audit

- In accordance with the Commissioners Regulations must follow either GAS (Yellowbook) or IIA (Redbook) standards.

Key Factors that Distinguish and Differentiate Internal and External Auditing

⊙ *Timeframe*

- External Audit
 - An annual process that primarily focused on the districts year end of December 31.
- Internal Audit
 - Year-round process that focuses on the continued improvement of controls relative to the districts financial and operational risks.

Key Factors that Distinguish and Differentiate Internal and External Auditing

⊙ *Risk*

● External

- Identifies and assesses risk exposures related to financial reporting and potential fraud.
- Makes appropriate recommendations as a result of the risk assessment mainly relative to significant control deficiencies generally related to the financial reporting process.

● Internal

- Identifies and assesses business risks taking into account likelihood and impact on district objectives.
- Makes appropriate recommendations as a result of the risk assessment relative to financial and non financial activities.

Key Factors that Distinguish and Differentiate Internal and External Auditing

◎ *Follow-up*

● External

- Required to report on the results of the corrective actions taken on prior year findings and recommendations.
- Required to continue reporting uncorrected significant control deficiencies.

● Internal

- Monitors the implementation of corrective actions taken by management and reports to the Audit Committee.

Misconceptions of the Internal Audit Function

- Duplication of effort with the external auditor
- OSC will be performing audits so that should suffice
- The internal audits are mechanical and review the same type of transactions every year

How Can a Water District Better Utilize the Internal Auditor?

- Test and report on a wide variety of areas besides evaluation of controls
- Evaluate controls beyond the traditional transaction cycles
- Is there an area where the water district has concerns or issues with compliance?

How Can a Water District Better Utilize the Internal Auditor? (Continued)

- Is there an operational area that may be inefficient?
- Is there a less costly way at achieving the same result by exploring alternatives?

Best Practices

- Audit committee should discuss the audit plan with the internal auditor
- All procedures should be outlined in an engagement letter prior to commencing field work
- Internal audits should always be based on risk, be specific to a water district, and be constantly changing to assist in monitoring areas that need attention

Best Practices (Continued)

- Communicate and reiterate with the Board how the internal auditor can assist in improving the effectiveness and efficiency of a water district's operations and activities by helping them save money or taking advantage of additional revenues
- An in depth audit of internal controls once every five years is not sufficient
- Internal audits should assist, not criticize, water districts with improving operations, policies, procedures, and internal controls throughout the year

Top Ten Internal Control Deficiencies Cited In the New York State Comptroller's Reports – Local Government

10. Travel Expenditures

- ⊙ The Board did not adopt a formal, written travel policy.
- ⊙ Not all travelers attached proof of conference attendance to their travel expenditure reports and meal expenditure receipts, which also included individuals who were not authorized to travel by the Board.
- ⊙ The Board adopted a resolution establishing per diem travel rates which exceeded the rates set by the Federal General Services Administration (GSA).

9. Treasurer's Function

- ⊙ The Treasurer did not maintain accurate financial records and reports.
- ⊙ The Treasurer's duties were not segregated as they made all deposits, performed all recordkeeping functions, and prepared bank reconciliations without independent oversight.
- ⊙ The Treasurer did not provide monthly financial reports to the Board during the year and the Board did not review bank reconciliations.

8. Board Oversight

- ⊙ The Fire Company's Board did not conduct or contract an annual audit of the Clerk/Treasurer's records and reports as required per the Fire Company's by-laws.
- ⊙ The Board did not establish adequate written policies and procedures governing areas such as cash receipts, disbursements, online banking, and information technology.
- ⊙ The Fire Department's by-laws did not define financial oversight responsibilities and did not provide specific guidelines on how management should exercise its decision-making power.

7. Information Technology

- ⊙ The Board did not adopt formal, written information technology policies and procedures for individual access rights, disaster recovery and password security management.
- ⊙ The Board did not establish policies and procedures regarding breach notifications and disaster recovery plans.
- ⊙ Former Village personnel still had active user accounts and access to the Village's network.
- ⊙ The Board did not develop a written disaster recovery plan.

6. Claims Auditing/Processing

- ⊙ The Board did not adopt a formal, written claims processing policy.
- ⊙ Claims were paid before the Board reviewed or approved them.
- ⊙ The Board did not ensure that all claims were supported with adequate documentation, for appropriate purposes, and approved prior to payment.
- ⊙ The Board did not review each claim to determine if the claims were properly itemized and included appropriate supporting documentation.

5. Cash Receipts

- ⊙ The Board did not establish and implement adequate internal controls over the cash collections process.
- ⊙ Fire Department officials did not adopt written financial policies or procedures and addressing cash receipts and fundraising procedures/accountability.

5. Cash Receipts (Cont.)

- ⊙ Fire Department officials did not deposit or account for all donations received or deposit money received from fundraisers.
- ⊙ Fire Company officials did not maintain sufficient documentation to indicate the amount of money received at each fundraising event and did not always maintain adequate records to identify the source of each bank deposit.

4. Purchasing/Procurement

- ⦿ Fire District and Village officials did not seek competitive bids and quotes when selecting professional service providers, or procuring other large purchases, per Board policies.
- ⦿ Resolutions that the Board passed to approve claims for payment did not include information necessary to determine the number and dollar amount of the claims authorized for payment.

4. Purchasing/Procurement (Cont.)

- ⊙ Fire District and Village officials did not obtain quotes for various purchases in accordance with the Fire District and Village procurement policies.
- ⊙ Not all checks were signed by both the President and Treasurer in accordance with the Fire District's procurement policy.

3. Credit Cards

- ⦿ Credit card charges for purchases totaling almost \$25,000 did not comply with the purchasing policy.
- ⦿ Fire District officials did not adequately monitor or establish written policies and procedures for gasoline credit card purchases.
- ⦿ Not all credit card purchases contained documentation verifying the receipt of goods or services.

3. Credit Cards (Cont.)

- ⊙ There was no record of the Board approving and formally adopting the Fire District's credit card policy.
- ⊙ Credit card charges were approved by the Board despite not having adequate supporting documentation, such as itemized receipts.
- ⊙ The Secretary-Treasurer did not reconcile monthly credit card statements to individual receipts.

2. Budgeting

- ⊙ The water and sewer funds' tentative budgets were not balanced and included deficits.
- ⊙ The Village's tentative budget included a tax levy that exceeded the Village's tax levy limit.
- ⊙ The Board overrode the 2017-18 property tax levy limit and increased the tax levy by 21 percent, even though unassigned fund balance would provide enough funding for operations for nearly two years without a tax levy.

2. Budgeting (Cont.)

- ⊙ The proposed budget did not comply with the tax levy limit as it included a tax levy above the limits established by law.
- ⊙ The Board adopted unrealistic budgets that contributed to the significant growth of total fund balance over a three-year period.

1. Financing Operations/Management

- ⊙ Financial reports were inaccurate or not prepared and submitted to the Board or to the Office of the State Comptroller.
- ⊙ Fire District officials did not establish the levels of fund balance to be maintained or the thresholds for reserves.
- ⊙ The Fire District had not filed an annual financial report with OSC for multiple years as required by law.

1. Financing Operations/Management (Cont.)

- ⊙ The Board borrowed money each year from the Fire District's reserve funds to fund operating expenses, which was not in compliance with municipal law.
- ⊙ The Executive Committee did not provide adequate oversight of fundraising activities.

1. Financing Operations/Management (Cont.)

- ⊙ Village officials did not develop a comprehensive, written multiyear financial or capital plan.
- ⊙ The Board relied on fund balance as a financing source rather than using recurring revenue to finance recurring expenditures.

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