



# Jefferson County Soil and Water Conservation District

## Internal Controls Over Selected Financial Operations Report of Examination

Period Covered:

January 1, 2012 — September 30, 2013

2014M-171



Thomas P. DiNapoli

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# State of New York Office of the State Comptroller

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## **Division of Local Government and School Accountability**

April 2015

Dear District Officials:

A top priority of the Office of the State Comptroller is to help district 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 districts 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 Board governance. Audits also can identify strategies to reduce costs and to strengthen controls intended to safeguard district assets.

Following is a report of our audit of the Jefferson County Soil and Water Conservation District, entitled *Internal Controls Over 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 district 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

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### EXECUTIVE SUMMARY

The Jefferson County Soil and Water Conservation District (District) is one of 58 such districts in New York State. These districts provide services and fund projects related to the conservation of soil and water resources, the improvement of water quality, the control and prevention of soil erosion and the prevention of floodwater and sediment damage.

The District is governed by a seven-member Board of Directors (Board). The Board is responsible for the general management and oversight of the District's financial and operational affairs. The Board appointed one of its members as the District Treasurer. The Executive Director (Director) is responsible for the District's daily operations and reports to the Board.<sup>1</sup>

The District's main revenues are State and federal aid and grants, an appropriation from Jefferson County and proceeds from sales and services provided to customers. District expenditures totaled about \$992,000 for the 2013 fiscal year, which included both District operations and grant program expenditures. From January 2005 through September 2013, the District received approximately \$2.4 million in funding from State and federal sources through 12 grants.

#### **Scope and Objective**

The objective of our audit was to evaluate internal controls over selected financial operations for the period January 1, 2012 through September 30, 2013. We extended the scope of our audit back to January 1, 2005 to review grant activity and billings for forestry services on lands of a business or businesses that the former Director appears to have been affiliated with. Our audit addressed the following related questions:

- Did the Board effectively monitor fiscal operations?
- Did the Board properly enter into an agreement and oversee the billing for forestry services provided by the District?
- Are internal controls over cash disbursements appropriately designed and operating effectively to adequately safeguard District assets?

#### **Audit Results**

The Board needs to improve its monitoring of the District's fiscal operations. The Board was not provided with the necessary financial reports and information to properly oversee operating and grant

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<sup>1</sup> The former Director resigned effective February 4, 2013.

activities, or to develop realistic or structurally balanced budgets. As a result, the District experienced financial difficulties and borrowed approximately \$669,000 from grant funds to help pay operating costs. Although the District has repaid most of these funds, approximately \$37,000 remains payable as of September 30, 2013 from the District's operating fund to its grant funds. The District obtained \$85,000 in additional funding from Jefferson County and sold District equipment for \$27,365 in order to help repay the loans from the grant funds. At the exit conference held on March 23, 2015, District officials stated they have since repaid an additional \$12,000 to the grants and will pay the balance of \$25,000 when the remaining grants with loan balances are closed. We were told that when the Board became aware of borrowing from certain grant funds to fund operations, a Board member contacted the New York State Department of Agriculture and Markets which informed the District that such borrowing from certain State grants is considered "a misuse of funds and a breach of the contracts."

Also, the Administrative Assistant (Assistant) did not maintain official copies of adopted budgets. The Assistant provided us with two versions of the 2011 budget and a Board member provided a third version. All three versions were different and no one was able to confirm which budget, if any, was the official budget adopted by the Board. The Assistant also provided us with a budget for 2012, but officials were unable to confirm whether it was the adopted version. In addition, the amount in the 2012 budget column in the 2013 budget did not agree with the 2012 budget provided to us. Without approved adopted budgets on hand, the Board is unable to compare the actual performance of revenues and expenditures against adopted budgets. In addition, the District's budget includes a combination of operating activity and grant activity. From our review of the 2012 budget, it appears that the operating activity is being financed by grant funds.

We also found the Board permitted the District to enter into an agreement to provide forestry services on lands outside the District to a business or businesses in which the former Director appears to have been affiliated, resulting in a potential conflict of interest. In addition, the Board did not establish written terms and rates for payment for these forestry services provided by the District, did not maintain records showing all work performed and did not ensure that all services were billed and payments were received. From January 2005 through September 2013, the District received \$36,035 for services and materials it provided. Because the District does not maintain documentation for all of the work it has provided, the District may not have billed and received all compensation to which it was entitled.

We also found internal controls over cash disbursements were not appropriately designed or operating effectively. The Board did not adequately segregate disbursement duties, audit and approve all claims for payment and ensure that checks were signed by the Treasurer or an assistant Treasurer. Because of these weaknesses, we reviewed 62 disbursements totaling approximately \$253,000 to assess whether claims were properly supported and were for a legitimate District purpose. Although we found no exceptions, these control weaknesses increase the risk that inappropriate cash disbursements could occur and remain undetected and uncorrected.

### **Comments of District Officials**

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

# Introduction

## Background

The Jefferson County Soil and Water Conservation District (District) is one of 58 such districts in New York State. These districts provide services and fund projects related to the conservation of soil and water resources, the improvement of water quality control, the prevention of soil erosion and the prevention of floodwater and sediment damage.

The District is governed by a seven-member Board of Directors (Board). The District's operating functions are administered and performed by an Executive Director<sup>2</sup> (Director), a District Administrative Assistant (Assistant) and three other field employees. The Board appointed one of its members as the District Treasurer.

The District's main revenues are State and federal aid and grants, an appropriation from Jefferson County, and proceeds from sales and services provided to customers. District expenditures totaled about \$992,000 for the 2013 fiscal year, which included both District operations and grant program expenditures. From January 2005 through September 2013, the District received approximately \$2.4 million in funding from State and federal sources through 12 grants.

## Objective

The objective of our audit was to evaluate the internal controls over selected financial operations. Our audit addressed the following related questions:

- Did the Board effectively monitor fiscal operations?
- Did the Board properly enter into an agreement and oversee the billing for forestry services provided by the District?
- Are internal controls over cash disbursements appropriately designed and operating effectively to adequately safeguard District assets?

## Scope and Methodology

We examined the District's financial operations for the period January 1, 2012 through September 30, 2013. We extended the scope of our audit back to January 1, 2005 to review grant activity and the provision of forestry services on lands of a business or businesses that the former Director appears to have been affiliated with.

We conducted our audit in accordance with generally accepted government auditing standards (GAGAS). More information on

<sup>2</sup> The former Director resigned effective February 4, 2013. The Board nominated a new Director on February 11, 2013, who was provisionally appointed on June 10, 2013.

such standards and the methodology used in performing this audit is included in Appendix B of this report.

**Comments of  
District Officials and  
Corrective Action**

The results of our audit and recommendations have been discussed with District officials and their comments, which appear in Appendix A, have been considered in preparing this report. District 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 Board to make this plan available for public review in the District's office.



## Board Oversight

The Board has the overall responsibility for the District's fiscal management and should take an active role in overseeing District operations. The Board should review necessary financial information in order to effectively monitor operations and develop realistic budgets. Such information includes the review of periodic budget-to-actual reports and grant activity. The Board should also ensure that budgets are structurally balanced and that grant proceeds are being used in accordance with grant requirements.

The District's operating activity, which consists of general and administrative functions, forest management services and the maintenance of recreational trails, is primarily funded by Jefferson County (County) appropriations. Other land-use programs are funded through federal and State grants. Grant agreements usually address how grant funds are to be used and normally require recipients to track the use of funds and maintain adequate supporting documentation detailing grant moneys received and expended.

The Board needs to improve its monitoring of the District's fiscal operations. The Board was not provided with the necessary financial reports and information to properly oversee operating and grant activities, and did not develop and adopt realistic and structurally balanced budgets. In addition, grant moneys were used to fund District operations, which in certain instances were not permitted.

### Fiscal Management

The Board is responsible for making sound financial decisions that are in the best interest of the District and the taxpayers that fund operations. In order to make informed decisions, it is important that the Board receive adequate information showing the results and performance of District operations. This information should include periodic reports showing budget-to-actual results for the District's operating and grant activities.

A Board member told us the Board relies on the Director to develop and provide budgets.<sup>3</sup> In addition, the Director is responsible for providing the Board with financial reports and the information necessary for decision making. Board members told us they relied on the former Director to manage the District's day-to-day operations. The Board did not adequately oversee the former Director's work or the District's fiscal operations.

<sup>3</sup> According to a letter from the former Director's attorney, the former Director assisted with the presentation of draft budgets to the Board.



The Assistant provided the Board with reports showing monthly revenues and expenditures and ending cash balances for the operating fund and grants. However, no budget-to-actual reports were provided. Such reports are necessary to monitor actual performance against the adopted budgets.<sup>4</sup> In addition, we found the District's budgets were not structurally balanced and the Board did not review actual results from prior years when developing current year budgets (see Budgeting section). The Board also did not receive comprehensive reports detailing grant funds awarded and expended to date to help determine the funds remaining for expenditure and to identify how grant moneys funds were expended. As a result, the Board was unable to effectively oversee and monitor the District's financial condition and grant activity.

Since at least 2005, the District routinely experienced cash flow difficulties and could not pay its operating expenditures from current revenues. As a result, District officials transferred or borrowed money from various State and federal grants to help finance operations, essentially using grant moneys to pay for routine operating expenditures that did not appear to be directly related to the grants. For example, the District used grant money to make the routine payroll and related retirement payments, which appeared unrelated to the grants. Although the Assistant maintained spreadsheets to track the grant borrowings and subsequent repayments, the borrowings were not included in the monthly reports presented to the Board.<sup>5</sup>

Several Board members told us that when they became aware of borrowing from grant funds in December 2012, the District notified the New York State Department of Agriculture and Markets<sup>6</sup> (Ag and Markets). In January 2013, Ag and Markets completed a review of three grants that were active at the time and found that the District

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<sup>4</sup> In March 2013, the Board started receiving budget-to-actual reports for the general and administrative functions. However, the budget-to-actual reports for forest management and maintenance of recreation trails were not generated. In addition, no comprehensive reports detailing grant activities were being provided to the Board at this time.

<sup>5</sup> We were told by a District employee that the former Director instructed the employee to transfer or borrow money from various State and federal grants to help finance the District's operating expenditures. A Board member also told us that the Board was not notified of, nor asked to approve, these uses of grant funds. A letter from the former Director's attorney indicates that the Board was aware that grant monies were being used for operating expenditures and that final decisions regarding these uses of grant funds were made by the Board. The former Director's attorney also indicated that he believes grant funds could be used for operating expenditures.

<sup>6</sup> The District had received approximately \$2.4 million in funding from State and federal sources from 12 grants that were active from 2005 to September 2013. Of the 12 grants, six were funded by Ag and Markets totaling \$1.7 million during this period.

had borrowed approximately \$104,000 from these grants. According to a letter from Ag and Markets, “[t]he reallocation of state monies for purposes other than those specified in the [grant] contracts is a misuse of funds and a breach of the contracts.” Therefore, Ag and Markets temporarily suspended funding to these grants until the District implemented a series of recommendations, including:

- Restore grant moneys to the balances in each contract account as identified in the review.
- Establish separate interest-bearing accounts for each grant.
- Establish a policy that prohibits the borrowing from State grants, regardless of source, to meet other District obligations.
- Have an audit performed by a qualified accounting firm.

In February 2013, the District initiated corrective action based on the recommendations provided by Ag and Markets. For example, the District established separate bank accounts for the Ag and Market grants, had an audit completed by an accounting firm and adopted policies as recommended. Because of the District’s financial difficulties, the Board requested and received \$85,000 in additional funds from the County and sold surplus equipment for \$27,365<sup>7</sup> to help restore grant moneys to the necessary balances. As a result of the District’s efforts of implementing corrective actions, Ag and Markets has resumed its funding of the District’s State grants.

We reviewed the District’s accounting records showing the borrowing and repayment transactions within all active grants during our audit period. We found the District borrowed approximately \$669,000 from December 2005 through January 2013. The District has since repaid \$570,000,<sup>8</sup> leaving \$99,000 not repaid as of September 2013.<sup>9</sup> However, the District’s operating fund paid approximately \$62,000 in payroll costs which were chargeable to the grants. After factoring in these costs, approximately \$37,000 remains payable to the grants.<sup>10</sup> At the exit conference held on March 23, 2015, District officials stated they have since repaid an additional \$12,000 to the grants and

<sup>7</sup> This amount was used to pay another federal grant not related to Ag & Markets.

<sup>8</sup> The District was able to repay \$112,365 of this \$570,000 because it received \$85,000 in additional funding from the County and \$27,365 from the sale of District equipment.

<sup>9</sup> From January 1, 2012 through September 30, 2013 the District borrowed approximately \$188,000 and repaid \$343,000, of which \$216,000 was repaid for borrowings prior to January 1, 2012.

<sup>10</sup> Payroll costs related to the administration of a grant are initially charged to the District’s operating fund. Grant funds are then transferred to the operating fund to reimburse these costs.

will pay the balance of \$25,000 when the remaining grants with loan balances are closed.

## **Budgeting**

It is essential that the Board adopts structurally balanced budgets that provide for recurring expenditures to be financed by recurring revenues and ensures that budgeted financing sources equal budgeted expenditures. The Board should review actual results from prior years when developing a budget because historical information may be a useful source when forecasting future activity. The Assistant should also maintain an official copy of the adopted budget.

The Assistant did not maintain an official copy of the Board's adopted budgets. The Board minutes typically indicate that the Board officially adopted a particular year's budget. However, the minutes do not document the amount of the budgeted appropriations for that budget year. We requested the District's adopted budgets for 2011, 2012 and 2013. We were provided with the following:

- The Assistant provided two versions of the 2011 budget and a Board member provided a third version. All three versions were different and no one was able to confirm which budget, if any, was the official Board-adopted budget.
- The Assistant provided a budget for 2012, but officials were unable to confirm whether it was the adopted version. In addition, the amount in the 2012 budget column in the 2013 budget did not agree with the 2012 budget provided to us.<sup>11</sup>

Because the annual budget represents the District's financial plan for the fiscal year, it is important for District officials to have a copy of the adopted budget, to know what the budgeted amounts are and to monitor actual results against the budget throughout the year to ensure that expenditures and revenues are within budgeted amounts.

In addition, the Board did not review historic revenues and expenditures to help ensure that the budgets were realistic and structurally balanced. The Board received proposed budgets that included the current year's adopted budget, the next year's proposed budget and anticipated revenues and expenditures for the current year. However, the Board did not review or analyze the prior year's actual results to help ensure budget estimates were reasonable.

The District's budgets include a combination of operating activity and grant activity. According to our review of the 2012 budget and discussions with District officials, it appears that the operating

<sup>11</sup> According to a letter from the former Director's attorney, the former Director assisted with the presentation of draft budgets to the Board.

activity is being partially financed by grant funds in the budget. As shown in Figure 1, the District's estimated operating expenditures exceeded the estimated financing sources (revenues and appropriated fund balance) by \$247,500. This difference was primarily financed by grant funds because estimated grant financing sources exceeded the estimated grant expenditures by \$235,000 in the budget. In addition, the budget also did not balance in total. Total estimated expenditures exceeded total estimated financing sources by \$12,500.<sup>12</sup>

<b>Figure 1- 2012 Budgeted Amounts</b>			
	<b>Financing Sources<sup>a</sup></b>	<b>Appropriations</b>	<b>Surplus/(Deficit)</b>
Grant Moneys	\$1,485,000	\$1,250,000	\$235,000
Operating Activity	\$587,000	\$834,500	(\$247,500)
<b>Total Budget</b>	<b>\$2,072,000</b>	<b>\$2,084,500</b>	<b>(\$12,500)</b>
<sup>a</sup> Includes estimated revenues and appropriated fund balance			

If grant funds are restricted for a particular purpose, they typically cannot be used to finance general operating activities. It is important for the Board to adopt a structurally balanced budget that does not depend on grant moneys to fund the District's general operating activities. In 2013, the Board adopted a budget that did not include grant funds as a financing source for operating activities. However, the operating budget still was not structurally balanced as appropriations were \$26,791 higher than financing sources.

The Board is unable to adequately manage District operations if it does not adopt and monitor realistic and structurally balanced budgets. Also, the lack of a structurally balanced budget will have negative impacts on the District's financial condition because it does not provide adequate and appropriate financing sources to cover operating costs.

## Recommendations

1. The District should consult with its attorney, as appropriate, to determine whether repayment of amounts borrowed from grant funds to pay operating expenditures is required pursuant to the grant agreements.
2. The Director should provide the Board with complete and accurate financial reports, including budget-to-actual results of revenues and expenditures for operating and grant activities.
3. The Director should maintain and provide to the Board detailed grant fund reports that identify the funds received, funds expended and balances remaining for each grant.

<sup>12</sup> The estimated financing sources and estimated expenditures were not totaled correctly in the 2012 budget. For example, the individual financing source line items in the budget were \$25,000 less than the total financing sources shown in the budget. As a result of the addition errors, the 2012 budget was \$12,500 out of balance.

4. The Board should review actual results from prior years to ensure budget estimates are reasonable and it should adopt budgets that are structurally balanced.
5. The Assistant should maintain an official copy of the adopted budget.

## Forestry Services

The Board is generally responsible for designing controls to help ensure services the District provides are proper and billed at agreed-upon rates and supported by detailed descriptions of work performed. This helps to ensure that the District receives the compensation to which it is entitled.

The Board permitted the District to enter into an agreement to provide forestry services on lands outside the District to a business or businesses with which the former Director appears to have been affiliated, resulting in a potential conflict of interest. In addition, the Board did not properly oversee the billing of forestry services provided on these same lands. The Board did not establish agreed-upon rates of payment for the services provided, did not ensure adequate records and support were maintained to show all work performed and did not have procedures to ensure that all services provided were billed and that payments for services were received. As a result, the District may not have billed and received all compensation to which it was entitled.

### Potential Conflict of Interest

General Municipal Law (GML) limits the ability of municipal officers and employees to enter into contracts in which both their personal financial interests and their public powers and duties conflict.<sup>13</sup> Unless a statutory exception applies, GML prohibits municipal officers and employees from having an interest in contracts with the municipality for which they serve when they also have the power or duty – either individually or as a board member – to negotiate, prepare, authorize or approve the contract; to authorize or approve payment under the contract; to audit bills or claims under the contract; or to appoint an officer or employee with any of those powers or duties. For this purpose, a contract includes any claim, account, demand against or agreement with a municipality.

Municipal officers and employees have an interest in a contract when they receive a direct or indirect monetary or material benefit as a result of a contract. Municipal officers and employees are also deemed to have an interest in the contracts of a firm partnership or association of which they are a member or employee, and a corporation of which they are an officer, director or employee, or directly or indirectly own or control any stock. As a rule, interests in actual or proposed contracts on the part of a municipal officer or employee, or his or her spouse, must be publicly disclosed in writing to the municipal officer or employee's immediate supervisor and to the governing board.

According to Board minutes, in 2005, the former Director asked the Board to approve the performance of timber marking/forest management

<sup>13</sup> We believe that the former Director was a "municipal officer or employee" because the District falls within the statutory definition of the term "municipality."

services on lands of a business that the former Director appears to have been affiliated with. In response, the Board authorized the District to enter into a forest management agreement with this private corporation (Corporation). Board minutes contain no further description of the services to be provided by the District and no description of the terms under which those services would be provided to the Corporation.<sup>14</sup>

Between 2005 and 2013 the District issued 10 invoices and received \$36,035 for services provided to this Corporation and/or a limited liability company (LLC) wholly owned by the Corporation for, among other things, forestry services and forestry management services. These invoices and payments imply the existence of contracts between the District and the Corporation and/or the LLC.

In our view, the former Director is deemed to have had an interest in one or more of these contracts because of his relationship with the Corporation and the LLC during the period of time when the District was providing services to the Corporation and/or LLC. We were told by District officials that the former Director was the Chief Executive Officer of the Corporation, and we were provided with documents indicating that the former Director was the president and a director of the Corporation,<sup>15</sup> as well as president of the LLC.<sup>16</sup> We also believe that the former Director had the power to negotiate these contracts because Board members told us that the former Director was responsible for negotiating contracts,

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<sup>14</sup> District staff and the current Executive Director told us the services included maintaining boundary lines, updating a forest management plan, plowing roads and administering the marketing, harvesting and sale of timber.

<sup>15</sup> The letter from the former Director's attorney also states that "[d]epending on the date of services, [the former Director] may have been an officer or director of [the Corporation]."

<sup>16</sup> The precise nature of the former Director's relationship to the LLC is not entirely clear. The letter from the former Director's attorney states that the former Director was never a "member, owner, manager or employee" of the LLC, but also stated that "depending on the date of service, [the former director] may have been a director of [the LLC]." New York State Limited Liability Company Law, however, makes no mention of a limited liability company having one or more "directors," providing instead for these types of organizations to be governed, managed and operated by "members," "managers," "employees" and "agents." Under these circumstances, because the attorney's use of the word "director" implies a position with the LLC having governance and/or managerial functions, we believe the former Director should be properly regarded as either a "member" or "employee" of the LLC notwithstanding the attorney's statement to the contrary. Moreover, even if the former Director cannot be viewed properly as an LLC member or employee, we still believe that he would have been deemed to have had an interest in the LLC's contracts. In our view, because the LLC is wholly owned by the Corporation, the two organizations share an overlap or identity of interest sufficient to cause the Corporation to be regarded as a party to the LLC's contracts with the District for purposes of Article 18 of GML. Therefore, inasmuch as the former Director was an officer or director of the Corporation, we believe that he would have been deemed to have had an interest in the LLC's contracts with the District.



and the Assistant told us that the former Director instructed her on the dollar amounts to bill the Corporation for the services performed by the District.<sup>17</sup> Therefore, unless a statutory exception is applicable in these instances, the former Director would have had a prohibited interest in one or more of the District's contracts with the Corporation and/or LLC.

The only statutory exception that might apply in this instance is set forth in GML. That exception applies to interests in contracts that would be prohibited by virtue of a municipal officer or employee being an officer or employee of a private firm, corporation or association, but only if the individual's private remuneration is not directly affected by the municipal contract and the individual's private duties do not directly involve the procurement, preparation or performance of the municipal contract.

We were told by the former Director's attorney that the former Director has never been compensated by the Corporation or the LLC. The former Director's attorney also told us that the former Director was not responsible "for securing services or for making payments" on behalf of either organization. However, we found no indication that anyone other than the former Director acted on behalf of the Corporation and/or the LLC in arranging for the District's services.

Under these circumstances, if the former Director was involved in arranging for the District to provide services to the Corporation and/or the LLC, then we believe that the statutory exception would not have applied because the former Director would have been directly involved in the procurement of the contracts for the Corporation and/or LLC. In that case, the former Director would have had a prohibited interest in the District's contracts with the Corporation and/or LLC. If the statutory exception applied, the former Director's interest in the contracts would not have been prohibited, but he would have been required to disclose the interests in writing to the Board.<sup>18</sup>

Furthermore, while New York State Soil and Water Conservation Districts Law permits the District to perform certain functions on lands of the District's directors, officers and employees, according to Ag and Markets, this provision applies to services performed on land within the District and to services performed on land outside

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<sup>17</sup> The letter from the former Director's attorney states that the Board was responsible for establishing how much the District would charge for its services. We note, however, that we found no reference in the Board's minutes to the charge for the District's services made prior to the rendition of those services.

<sup>18</sup> It appears that no such written disclosure was made, but it also appears that the Board was aware of the former Director's relationship to the Corporation and/or the LLC.

the District, pursuant to a duly authorized agreement with another soil and water conservation district or other governmental entity. This provision does not apply in this instance because the services provided to the Corporation and/or the LLC were performed on land outside the District,<sup>19</sup> but not pursuant to an agreement with another soil and water conservation district or other governmental entity. Without such an agreement, it is our understanding that the District lacked authority to provide services to the Corporation and/or LLC because the land was located outside the District.

## **Billing**

The Board is responsible for developing and approving the terms and rates of payments for services provided to customers. The Board should also ensure that all work performed is documented and billed and that payment is received for the work.

District officials could not provide us with a signed, written agreement with the former Director's affiliated Corporation. Instead, the Assistant provided us with an unsigned, undated document entitled Memorandum of Understanding (MOU) that purports to set forth the responsibilities of the parties, including the fees for the District's services. Board members told us that they never reviewed the document and they were not aware of the terms included in it. Board members indicated that when they authorized the arrangement with the Corporation, they knew that the District would be receiving revenue for forestry services. However, they did not know many details about the arrangement.

The Assistant told us that the former Director instructed her on the dollar amounts the District should bill the Corporation.<sup>20</sup> However, she was not provided with support for the amounts billed or detailed descriptions of the services provided and no detailed records were maintained by the District to track the services provided. The Board minutes indicate that on several occasions the former Director informed the Board of the services being provided to the Corporation, and the dollar amount of revenues the District would receive for some of these services. However, Board members told us they did not closely monitor the arrangement by reviewing the services being provided or the amounts billed and received by the District. Because Board members did not ensure that there was a written agreement with the Corporation, did not ensure that the District maintained documentation of all work performed and did not review or approve amounts charged for services, the Board cannot ensure that all services provided to the Corporation were properly billed.

<sup>19</sup> The District's territory is in Jefferson County, but the services were provided in Lewis County.

<sup>20</sup> According to a letter from the former Director's attorney, the former Director did not have a role in determining how much the District would charge for such service and the Board was responsible for such matters.

Based on our review of the District's billing and accounting records from January 2005 through September 2013, the District issued 10 invoices and received \$36,035 for services provided to the Corporation and/or a LLC wholly owned by the Corporation. Two of the invoices, totaling \$20,749, are consistent with the billing rate for services included in the unsigned MOU (8 percent of the Corporation's timber sales). However, because the Board never approved the MOU, it is uncertain whether the amounts paid were the amounts the Board intended at the time that it authorized the agreement with the Corporation. Furthermore, most of the remaining invoices included vague descriptions of the work performed and the billing method was inconsistent between invoices. For example, one invoice referenced "forestry service: 144 hours 9/1/08-9/30/09" billed at a rate of \$25 per hour, while another invoice referenced "forestry management" and charged a lump sum amount of \$2,900. Yet another invoice showed a \$2,875 charge for "forestry services: stand #10 and marking stands #2 and 3." There was no written contract that sets forth the terms of the arrangement and no detailed records were on file showing what services were actually provided. Therefore, District officials have no assurance that billings were correct and that the District received fair and adequate consideration for the services it rendered.

In 2013, District officials compiled a final billing to the Corporation using all the information they were able to gather, such as employee estimates of time worked and related mileage and supply costs. This final bill was paid by the Corporation in April 2013 and the District no longer provides forestry services to the Corporation.

## Recommendations

The Board should:

6. Ensure that all District officers and employees are familiar with the conflict of interest provisions of GML.
7. Ensure any services the District provides on lands of the District's directors, officers and employees are either performed on land within the District or are performed pursuant to a duly authorized agreement with another soil and water conservation district or other governmental entity.
8. Ensure all services the District provides are billed at agreed-upon rates, are supported by detailed descriptions of the work performed and that revenues for all services provided are received.

## Cash Disbursements

The Board is generally responsible for designing adequate internal controls over cash disbursements to safeguard District assets. The Board should establish controls to ensure that all disbursements are properly authorized, supported by appropriate documentation, made for valid business purposes and properly recorded. Furthermore, job duties should be properly segregated to ensure that no single person controls all phases of a transaction, when practicable. If not practicable, it is important for the Board to provide sufficient oversight of the District's financial operations. Also, the Board is required to audit and approve all claims for payment. Authorization for such payment should be documented in Board meeting minutes.<sup>21</sup> Lastly, the appointed Treasurer or the assistant Treasurer, if one has been appointed, must sign all checks disbursing District funds.

Internal controls over cash disbursements were not appropriately designed or operating effectively. The Board did not adequately segregate duties, audit and approve claims prior to payment and ensure that checks were signed by the Treasurer or assistant Treasurer. As a result, there is an increased risk that inappropriate payments could occur and remain undetected.

Duties over the cash disbursement process are not adequately segregated because the Assistant controls all phases of the disbursement process. The Assistant processes checks through the District computer, signs checks, maintains the District's accounting records, prepares monthly and annual financial reports and performs bank reconciliations. Although the Board appointed one of its members as Treasurer, he does not sign checks. All cash disbursement duties should not be performed by one individual without adequate compensating controls, such as management oversight. Either the Treasurer or an assistant Treasurer must sign all District checks. As a control measure, the Board may require the Assistant to co-sign such checks.

The current Director began providing some additional oversight beginning in February 2013 by reviewing bank reconciliations. However, the current Director does not ensure the reconciled bank balances agree with accounting records or that all cash disbursements are accounted for. As a result, this review does not provide a sufficient check of the Assistant's duties. In addition, the District does not have a process for anyone to regularly review canceled checks or check

<sup>21</sup> This would entail noting the range of the voucher numbers and the total dollar amount of the vouchers.

images. The review of canceled checks or check images by an individual who is not involved in the cash disbursement process is a good compensating control.

Furthermore, the Board does not audit and approve all claims prior to payment. The Board only audits and approves the claims relating to reimbursements of Board member expenditures. Beginning in May 2013,<sup>22</sup> the current Director began auditing and approving all claims. However, the Director also has the ability to initiate and record a transaction, and prepare, sign<sup>23</sup> and disburse checks. While it is a good practice for the Director to review claims as part of the cash disbursement process, it is part of the Board's oversight responsibilities to audit and approve claims for payment. After claims have been audited, the Board should direct the Assistant to provide the Treasurer with a written order to pay the claimants the allowed amounts and document such approval in the minutes.<sup>24</sup> Although the Board is provided monthly disbursement reports of checks issued, sufficient information is not provided, such as invoices, to help determine if disbursements are for proper District purposes. As a result, the Board is not providing adequate oversight of cash disbursements and there is an increased risk of erroneous or improper payments.

Because of the weaknesses identified, we reviewed 62 check disbursements totaling approximately \$253,000 to determine whether they were properly supported and were for a legitimate District purpose. We also verified selected salaries paid pursuant to Board authorizations. We reviewed bank statements to verify that the transfers out of District accounts were for legitimate purposes, that in-bank withdrawals were proper and that the bank-adjusted balance<sup>25</sup> agreed with the cash balance per the accounting records. Although we found no exceptions, the internal control weaknesses that we identified increase the risk that inappropriate cash disbursements could occur and remain undetected and uncorrected.

## Recommendations

The Board should:

9. Ensure that duties relating to disbursements are segregated so that no one person controls all phases of a disbursement transaction or, as a compensating control, provide adequate oversight of the cash disbursement process.

<sup>22</sup> Prior to this date, we were told that the former Director audited and approved claims mainly for contractual expenditures and the Assistant's expense reimbursements.

<sup>23</sup> In addition to the Treasurer and Assistant, the Director is also authorized to sign checks.

<sup>24</sup> Claims paid from petty cash may be audited by the Board after payment.

<sup>25</sup> Adjusted for outstanding checks and deposits-in-transit

10. Ensure that the Treasurer or an assistant Treasurer signs all checks disbursing District funds.
11. Audit all non-petty cash claims before they are paid, ensuring that each claim has sufficient supporting documentation and represents a valid District expenditure.
12. Ensure that its authorization to pay claims is documented in the minutes and in an order directing the Treasurer to pay the amounts allowed on audit.

## **APPENDIX A**

### **RESPONSE FROM DISTRICT OFFICIALS**

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





**JEFFERSON COUNTY  
SOIL AND WATER CONSERVATION DISTRICT**

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April 14, 2015

Rebecca Wilcox, Chief Examiner  
NYS OSC SYRACUSE REGIONAL OFFICE  
State Office Building, Room 409  
333 E. Washington Street  
Syracuse, New York 13202-1428

Re: OSC # 2014 M-171

Dear Ms. Wilcox:

Please accept this document as our (SWCD) response to the internal controls audit. The Board of Directors (Board) and staff of the SWCD have reviewed the draft report and generally concur with the draft findings of the audit. We will address each section of the board oversight separately.

*Fiscal Management:* The Board concurs that there was not adequate financial oversight provided by the Board. Borrowing of grant funds ended as of January 13, 2013. As of June 10, 2013, the SWCD completed implementing a series of corrective measures in order to restore contractual arrangements with the Department of Agriculture and Markets. As part of this agreement with Ag and Markets, the SWCD was allowed to offset some of the "borrowed" money with SWCD time earned through grant completion. As of the end of 2014, Rounds 12 and 14 were closed out and adequate technical and administrative time had been earned to cover the remaining balance of the Round 16 borrow.

*Budgeting:* The 2013 budget was developed in February 2013. At the time of development the SWCD was aware that the budget was not structurally balanced. Additional cost cutting measures allowed the SWCD to finish 2013 with a structurally balanced budget. Budgets for 2014 and 2015 have been structurally balanced. As of 2014, the forest management and recreational trails contract with Jefferson County were combined. The 2014 and 2015 budgets include these contract funds within the overall budget for the SWCD. Additionally, as of March 2013, the Board was provided with a separate grant funding report.

*Forestry Services:* The Board concurs with the findings in regards to forestry services outside of the county. The final billing compiled in 2013 was a result of findings from a private audit that was performed.

*Cash Disbursements:* The Board concurs there was a lack in internal controls over cash disbursements. The Board also realizes that with a small staff there can be difficulties with total segregation of duties in the cash disbursement process. Field staff and the executive director are not in the office on a day to day basis during the construction season. USDA staff co-located in the office are unable to accept or record payment on behalf of the SWCD. The Board reviews and approves an itemized monthly disbursement report of checks issued, along with supporting documentation, such as invoices.

The Board and staff of the Jefferson County SWCD will work together to develop a corrective action plan for formal submittal to OSC within 90 days.

Sincerely,

Jason Bast  
Chairman

## **APPENDIX B**

### **AUDIT METHODOLOGY AND STANDARDS**

The objective of our audit was to evaluate internal controls over selected financial operations for the period January 1, 2012 through September 30, 2013. We extended the scope of our audit back to January 1, 2005 to review grant activity and the provision of forestry services lands of a business or businesses that the former Director appears to have been affiliated with.

To achieve our audit objective and obtain valid audit evidence, we performed the following audit procedures:

- We reviewed the Board minutes and relevant policies. We interviewed Board members and District employees, as related to our audit objective.
- We determined whether information is provided to Board members that would assist them in developing realistic budgets and effectively monitoring the District's fiscal operations.
- We reviewed the District's records to evaluate how the District accounts for its operating activity and grant funds. We then reviewed records relating to federal and State grants, which were active from January 2005 through September 2013, to determine the amount of grant funds received or borrowed by the Districts' operating fund, and whether they were subsequently repaid. We also inquired as to the reason why grant funds were borrowed.
- We calculated outstanding balances owed by the Districts' operating fund to the grant funds as of September 30, 2013.
- We reviewed the District's 2012 budget to determine the amount of operating activity being subsidized by grant funds.
- We inquired of District officials, Board members and the former Director regarding forestry services provided to a private corporation to assess if the former Director had a prohibited conflict of interest in the contract. We evaluated internal controls over the billing for these forestry services and inquired as to the terms and rates of payment for services provided and whether or not documentation was maintained evidencing all work performed. We also reviewed invoices to identify all billings for the services provided to the corporation. We traced billings to duplicate receipts and bank deposits to verify payments were received by the District.
- We evaluated internal controls over cash disbursements to determine if disbursements were made for proper purposes.
- For the period January 2012 through September 2013, we judgmentally selected 12 high-risk cash disbursements totaling \$171,930 by selecting payments made to District officials or unusual or questionable vendors, or for excessive dollar amounts or purchases of unusual items or services. We also randomly selected 50 cash disbursements totaling \$81,382. We examined

vouchers, invoices, canceled checks and disbursement records to ensure that the disbursements were adequately supported and were made for a legitimate District purpose.

- We judgmentally selected the bank statements for September 2013 and ensured that the adjusted bank balance from the statements agreed to the cash balance in the District's accounting records. We also ensured that all transfers out of these accounts were for appropriate purposes. We selected this month because we had no expectation that more or fewer errors would occur in this month than in any other month.
- We reviewed all bank statements from January 2012 through September 2013 to ensure in-bank withdrawals were for appropriate purposes. We reviewed September 2013 bank statements to verify that transfers out of District bank accounts were for legitimate purposes.
- We verified that the salaries paid to the Assistant and Directors (former and current) for 2012 and 2013 agreed with the Board-approved salary amounts.

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.

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