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June 13, 2014

Thomas P. Hand, Chairman
Members of the Board of Commissioners
Massapequa Water District
84 Grand Avenue
Massapequa, NY 11758-4990

Report Number: 2014M-100

Dear Mr. Hand and Members of the Board of Commissioners:

The Office of the State Comptroller works to identify areas where local government officials can improve their operations and provide guidance and services that will assist them in making those improvements. Our goals are to develop and promote short-term and long-term strategies to enable and encourage local government officials to reduce costs, improve service delivery, and account for and protect their entity's assets.

In accordance with these goals, we conducted an audit of the Massapequa Water District (District) for the period January 1 through December 31, 2013, which addressed the following question:

- Has the Board appropriately provided individual life insurance policies to the District's employees?

The results of our audit have been discussed with District officials, and their comments, which appear in Appendix A, have been considered when preparing this report. District officials generally agreed with our recommendation and indicated they planned to take corrective action. Appendix B includes our comment on an issue raised in the District's response letter

Background and Methodology

The District is located in the Town of Oyster Bay in Nassau County and serves the entire incorporated village of Massapequa Park and part of the hamlet of Massapequa. The District's total revenue for the 2013 fiscal year was more than \$6.2 million, which was generated primarily

from water usage charges and real property taxes. The District's 2013 expenditures totaled approximately \$5 million.

The District is governed by an elected three-member Board of Commissioners (Board), comprising a Chairman, Secretary and Treasurer. The District's Business Manager is responsible for the general management of the District's operations under the Board's direction. The Board, as a whole, is responsible for managing the District's investments and employee and Board fringe benefits.

We interviewed appropriate District officials to obtain an understanding of the organization and the accounting system, and reviewed pertinent documents. Further, we reviewed the District's internal controls and procedures over the computerized financial databases to help ensure that the information produced by such systems was reliable. After reviewing the information gathered during our initial assessment, we evaluated the District's internal controls for the risk of potential fraud, theft and/or professional misconduct. We then decided on the reported objective and scope by selecting for audit the area most at risk.

To accomplish the objective of this audit and obtain valid audit evidence, we interviewed District officials and reviewed State Comptroller's Office opinions and publications, District financial records and District records regarding life insurance policies. We conducted this performance audit in accordance with generally accepted government auditing standards. 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.

Audit Results

General Municipal Law (GML) and Insurance Law provide the authority for a board of commissioners of a water district, by resolution, to provide its officers and employees with group life insurance as a fringe benefit. There is no similar authority for a water district to provide individual life insurance policies for its officers or employees by board resolution outside of a collective bargaining agreement (CBA).

The District's individual employment agreements with four administrators state that the District will purchase and pay the premiums for an individual universal life insurance policy for each person.¹ Each policy has a total face value of \$100,000.² The policies' values increase over time

¹ This universal life insurance product is a type of whole life insurance policy. These insurance policies are interest-sensitive, which means that the policies' investment earnings are allocated differently based on current fluctuations in interest rates. Also, the policies have a cash value buildup that includes the amounts of premiums paid and interest earned. With individual policies, there is a separate policy written for each individual holding a policy. Group insurance policies have a single policy written that can include a number of participants and generally have less expensive premiums per participant.

² Three administrators, who were hired between January 1, 1998 and January 1, 2008, each have two universal life insurance policies, both with a face value of \$50,000. The remaining administrator, hired after January 1, 2008, has a single universal life insurance policy with a face value of \$100,000.

as the District pays the premiums and the policies accrue dividends. Each policy has a lower cash surrender value, which also increases over the life of the policy.

If an administrator retires after completing 20 years of service, or upon reaching age 55 with a minimum of five years of service, the District transfers ownership of the policy to the individual. At that point, the individual can then either continue making premium payments or redeem the policy for its cash surrender value. However, if the administrator is terminated for cause, the District would withdraw this benefit and terminate that individual's life insurance policy. District officials told us that the District chose to purchase individual policies so that it could transfer ownership of the policies to the individuals upon their retirement, whereas this would not be an option with a group policy.

The District currently holds seven individual life insurance policies with face values totaling \$400,000 for its four administrators. As of December 31, 2013, these policies had a cash surrender value of \$23,559.³ Because GML only authorizes group term life insurance for employees of a water district, the District is not authorized to offer whole life insurance policies for its employees and administrators. Also, because these policies have a cash surrender feature, this may constitute an unauthorized investment of District funds.

Recommendation

1. The Board should review the insurance policies it currently holds and consult with its counsel and insurance broker to take steps to ensure all insurance policies are in compliance with legal requirements.

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 of Commissioners to make this plan available for public review in the Secretary's office.

Sincerely,

Gabriel F. Deyo

³ Each policy has a different anniversary date. We determined the total cash surrender value by aggregating the cash surrender value reported for each policy at its respective 2013 anniversary date.

APPENDIX A

RESPONSE FROM DISTRICT OFFICIALS

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

The District's response letter refers to an attachment that supports the response letter. Because the District's response letter provides sufficient detail of its actions, we did not include the attachment in Appendix A.



Massapequa Water District

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Commissioners
Thomas P. Hand
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Stanley J. Carey, Superintendent
Constance A. Belegirinos, Business Manager

May 29, 2014

Mr. Gabriel F. Deyo, Deputy Comptroller
Division of Local Government and School Accountability
Office of the State Comptroller
110 State Street
Albany, New York 12236

Dear Mr. Deyo:

The Board of Commissioners of the Massapequa Water District ("District") acknowledges receipt of the preliminary draft findings of your full financial audit of the District. As stated in your initial December 12, 2013 letter, the audit focused "on policies and procedures related to the internal controls of the District" and covered the period from "January 1, 2013 to December 31, 2013".

Prior to the commencement of the audit the District provided encrypted information from our financial accounting system through your Electronic Filing Data Exchange system, including all cash disbursements and payroll activities for our most recent completed fiscal year. At the entrance conference, the District provided its "minutes, annual financial reports, budgets, records, policies" and numerous other documents in full compliance with the request of the Office of the State Comptroller ("OSC").

During the actual audit this past spring, our Business Manager Connie Belegirinos and Superintendent Stan Carey worked closely with your audit staff, we commend them for their diligence and professionalism. At the exit conference, it was my pleasure to meet with both [REDACTED] and [REDACTED] and the Board deeply appreciates their constructive comments regarding the District's operations.

Turning to the audit itself, the Commissioners were very pleased that OSC made no audit findings and/or recommendations regarding the District's accounting records or internal control policies. While the audit covered every facet of the District's financial operations, the preliminary findings raised only one question for review, "Has the Board appropriately provided individual life insurance policies to the District's employees?"

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of the inhabitants of the Massapequa Water District*

Consistent with this singular issue, OSC made one recommendation requesting that the MWD consult with our “counsel and insurance broker to take steps to ensure that all insurance policies are in compliance with legal requirements”.

Pursuant to OSC request, our general counsel provided the District with a formal opinion letter on May 23, 2014 (copy enclosed). In sum, the New York State Taylor Law mandates good faith “collective bargaining” between the District and its employees concerning all “terms and conditions of employment”. We are also advised by counsel that the New York State Public Employee Relations Board has defined life insurance as a negotiable term of employee compensation. Critically, as there is no “plain and clear prohibition” by either statute or (decisional) case law against individual whole/universal life insurance policies, they constitute a legitimate subject of collective bargaining. Finally, as the life insurance policies in question have been incorporated into the District’s CBA agreements for over fifteen (15) years, the District cannot repudiate this fringe benefit for its employees until its current CBA expires in 2016. At that time, the District will give every consideration toward negotiating term policies for its employees.

See Note 1 Page 7

Very truly yours,

/s/ Thomas P. Hand
Chairman

APPENDIX B

OSC COMMENT ON THE DISTRICT'S RESPONSE

Note 1

We acknowledge that the Public Employee Relations Board's conclusion regarding negotiability is not limited to group life insurance and do not criticize the District from a legal perspective on including group or individual life insurance as a benefit in the CBA. Accordingly, we adjusted the report to no longer reference the employees covered by this CBA.