



City and Town of Poughkeepsie Joint Water Project

Board Oversight

Report of Examination

Period Covered:

January 1, 2013 — May 31, 2014

2014M-236



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

December 2014

Dear Joint Water Project 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 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 City and Town of Poughkeepsie Joint Water Project, entitled Board Oversight. 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

New York State General Municipal Law authorizes local governments to enter into intermunicipal cooperation agreements (IMA) with other local governments. The City of Poughkeepsie (City) and Town of Poughkeepsie (Town) entered into an IMA in October 1991 to form the Poughkeepsie Joint Water Project (JWP). The JWP provides water to City and Town residents and produces water up to a maximum capacity of 19.3 million gallons per day.

The JWP is governed by the Joint Water Board (Board) which comprises six members, three selected by the City and three selected by the Town. The Board is responsible for the overall financial management of the JWP, including establishing internal controls to ensure that financial transactions are executed in accordance with statutory and managerial authorization and the IMA. The JWP's 2013 expenditures were \$3,287,115, funded by the City and Town.

Scope and Objective

The objective of our audit was to examine JWP operations for the period January 1, 2013 through May 31, 2014. We extended our scope to July 22, 2014 to review the annual reconciliation of expenditures. Our audit addressed the following related question:

- Did the Board provide sufficient oversight over the JWP's financial operations in accordance with the IMA between the City and Town?

Audit Results

The Board does not ensure that the JWP is operated in accordance with the IMA. While the City and Town are required to make quarterly estimated payments to cover JWP operating costs, the Board has not required the City to make its required payments. As a result, the JWP does not have sufficient funds to pay its expenditures in a timely manner. We found that 70 percent of the 271 invoices reviewed were paid late causing the JWP to incur late fees totaling \$13,121. These invoices were paid between one and 130 days late, with an average of 25 days late.

The IMA requires that an annual reconciliation of expenditures be done before March 1 of each year to ensure that all costs are properly allocated. However, the 2013 reconciliation was not completed until July 2014. When the reconciliation is not completed in a timely manner, neither the City nor the Town know their actual liabilities and may have difficulties if they are required to contribute more money than anticipated. The JWP may also experience financial difficulties because of a lack of funds to operate the JWP.

The City handles the financial activities of the JWP, but does not deposit JWP funds into a separate bank account, as required by the IMA. Instead, the City uses the City's concentration account, thus commingling JWP funds with City funds. As a result, the Board is not being provided with a clear picture of JWP finances. Furthermore, there is no rationale to support the 4 percent administrative fee¹ that the City charges the Town for maintaining JWP financial activities. Finally, the Board has not provided for contingency funds in the budget as required by the IMA. As a result, there is risk that the JPW might not have sufficient resources if an emergency or unforeseen expenditures occur.

Comments of Joint Water Project Officials

The results of our audit and recommendations have been discussed with JWP officials and their comments, which appear in Appendix A, have been considered in preparing this report. JWP officials generally disagreed with our recommendations. Appendix B includes our comment on an issue raised in the JWP's response letter.

¹ Four percent of the JWP's annual budget

Introduction

Background

General Municipal Law (GML) authorizes local governments to enter into intermunicipal cooperation agreements (IMA) with other local governments. The City of Poughkeepsie (City) and the Town of Poughkeepsie (Town) entered into an IMA in October 1991 to form the Poughkeepsie Joint Water Project (JWP). The agreement was updated in August 1995. The City owned and operated a water treatment facility located adjacent to the Hudson River at the time of the IMA. The JWP draws water from the Hudson River, treats it and distributes it through different delivery systems to City and Town residents and other third parties outside City and Town borders. The JWP produces water up to a maximum capacity of 19.3 million gallons per day.

The JWP is governed by the Joint Water Board (Board) which comprises six members, three selected by the City and three selected by the Town. The Board is responsible for the overall financial management of the JWP, including establishing internal controls to ensure that assets are properly safeguarded and that financial transactions are executed in accordance with statutory and managerial authorization and the IMA. The Board has delegated some of its administrative duties to the Water Plant Administrator (WPA), who is responsible for preparing the annual budget, making recommendations to the Board regarding payment of expenditures and other general administration duties. The City is responsible for administering the JWP operating fund, including processing and generating purchasing documents, payroll, disbursements and all other accounting reports. The JWP's expenditures for 2013 were \$3,287,115, of which, based on consumption, \$1,656,965 (51 percent) was the City's responsibility and \$1,630,150 (49 percent) was the Town's responsibility.

Objective

The objective of our audit was to examine JWP operations. Our audit addressed the following related question:

- Did the Board provide sufficient oversight over the JWP's financial operations in accordance with the IMA between the City and Town?

Scope and Methodology

We examined the Board's oversight of the JWP for the period January 1, 2013 through May 31, 2014. We extended our scope to July 22, 2014 to review the annual reconciliation of expenditures.

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 C of this report.

**Comments of Joint Water
Project Officials and
Corrective Action**

The results of our audit and recommendations have been discussed with JWP officials and their comments, which appear in Appendix A, have been considered in preparing this report. JWP officials generally disagreed with our recommendations. Appendix B includes our comment on an issue raised in the JWP's response letter.

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 GML. 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 JWP office.

Board Oversight

The Board is responsible for managing and overseeing the JWP's fiscal affairs and safeguarding its resources. The City handles JWP financial activities for which it receives an administrative fee. The Board delegates some of its administrative duties to the WPA; however, the Board is responsible for ensuring that the JWP is operated in accordance with the IMA. The IMA requires that the City and Town make quarterly estimated payments to the JWP to cover operating costs and that an annual expenditure reconciliation be completed by March 1 each year. It also requires that JWP funds must be maintained in a separate bank account and that the annual budget must include a provision for contingencies.

The Board does not ensure that the JWP is operated in accordance with the IMA. The Board does not require the City to make its quarterly estimated payments for operating costs and the annual reconciliation of expenditures for 2013 was not completed until July 22, 2014. In addition, JWP funds were not deposited into a separate bank account and there is no rationale to support the 4 percent administrative fee² that the City charges the Town for maintaining JWP financial activities. Finally, there is no provision for contingency funds in the JWP budget. As a result, the JWP does not have sufficient funds to pay its expenditures in a timely manner, causing, for example, 70 percent of the 271 invoices we reviewed to be paid late, with late fees totaling \$13,121. Further, neither the City nor the Town know the actual JWP liabilities and there is a risk that the JPW might not have sufficient resources in the event of an emergency.

Late Bill Payments

The IMA requires the City and Town to make quarterly estimated payments to the JWP on or before the first days of January, April, July and October, based on the annual budget of the JWP, to cover the costs of operations. JWP expenditures are allocated 51 percent to the City and 49 percent the Town based on actual water consumption. The WPA prepared the Town's bills. The City billed the Town for quarterly estimated payments for water consumption as required and the Town made the payments. However, the Board did not require the City to make its quarterly estimated payments. Therefore, JWP had only money from the Town to cover the operating costs of the water treatment facility.

The JWP paid \$2,814,720 to 153 vendors during our audit period. We examined payments to the 10 highest paid vendors, a total of 271 invoices. These included vendors for power suppliers, water

² Four percent of the JWP's annual budget

treatment chemicals, sludge disposal and health insurance. The City did not pay 189 tested invoices (70 percent) timely. Bills were paid between one and 130 days late; on average, invoices were paid 25 days late. As a result, the JWP incurred and paid late fees totaling \$13,121 on the 189 invoices. In addition, while we were conducting fieldwork, the JWP received a termination notice from its electrical supplier because of late payment. The WPA told us that he receives this type of notice on a regular basis. Furthermore, the WPA informed us that some vendors now refuse to do business with the JWP because of its reputation for paying bills late.

Due to the City's late remittance of payments to vendors, the JWP has incurred unnecessary expenditures. Because the City does not make quarterly estimated payments to the JWP's fund, as required, the JWP does not have sufficient cash to pay its ongoing expenditures in a timely manner. The Board Chair told us that if the Board did require quarterly estimated payments from the City, he believed the City might not be able to pay them because of the City's current poor financial condition. Subsequent to our fieldwork, a City official informed us that they gave the Town a credit of \$10,541 for late fees incurred. Although this credit helps to compensate the Town for the late fees incurred by the JWP, the credit represents only a portion of the late fees that have been caused by the City's management of the commingled bank account.

The Board's failure to require the City to adhere to the IMA could create significant problems for the JWP if one of its vendors terminates services or refuses to supply the necessary resources to continue JWP operations, such as electricity or water treatment chemicals.

Annual Reconciliation

The IMA requires that the Board, before March 1 of each year, calculate the actual operational, maintenance and capital costs for the completed calendar year and compare payments received from each party for the calendar year. Appropriate credits or debits should be included in the March bills. The purpose of this annual reconciliation is to ensure that all JWP costs are properly allocated between the City and Town. The credit or debit should be applied to the second quarterly (April) payment. The 2013 actual expenditures were \$3,287,115 of which \$1,656,965 (51 percent) was the City's responsibility and \$1,630,150 (49 percent) was the Town's responsibility.³

The reconciliation for 2013 was not completed until July 22, 2014, instead of March 1, 2014 as required. When the reconciliation is not performed in a timely manner, neither the City nor the Town know

³ The percent allocations for the City and Town for 2013 include rounding differences.

the actual liabilities and may have difficulties if the reconciliation requires them to contribute more money to the JWP operations than anticipated. The JWP may also experience financial difficulties because of the lack of funds necessary to operate the JWP.

Commingling of Funds

The IMA requires that the JWP's financial activities be administered by the City and that JWP's funds be maintained in an account that is separate from other City funds. By maintaining separate accounting records, the Board should be able to know the JWP's financial position at all times.

The City handles the JWP's financial activities and collects the revenues intended for the JWP. Although the City maintains a separate bank account for JWP funds, the City does not deposit funds collected for the JWP into the JWP account. The JWP account should include quarterly estimated payments from the City and Town. However, the City does not deposit its own quarterly estimated payments into the JWP account. In addition, although the City does deposit the Town's quarterly estimated payments, the City deposits them into the City's concentration account instead of the JWP account. The concentration account contains all of the City's funds, thus commingling JWP funds with City funds. The City subsequently transfers just the amount of funds needed from the City's concentration account to the JWP account to cover payment of expenditures when checks are issued to vendors from that account. Therefore, any remaining JWP funds remain in the City's account.

Although the IMA specifically states that JWP funds must be segregated, the Board has not required the City to abide by the IMA. As a result, there is a lack of transparency in the financial position of the JWP and the Board is not being provided with a clear picture of the JWP's assets. Furthermore, it appears the City is using the JWP funds for City purposes,⁴ causing JWP bills to not be paid in a timely manner.

Administrative Costs

The City is providing administrative services for the JWP such as paying bills and processing payroll and employee benefits. The IMA provides that the City administers the JWP's financial activities and that the JWP will reimburse the City for the costs incurred. The Town is being charged 4 percent of the JWP's annual budget for its share of these services; in 2013, the Town paid \$131,485 for administrative costs associated with the JWP. Accurate cost allocations can help in preparing annual budgets and provide the Board with an accurate picture of operating costs.

⁴ Because the Town's quarterly payments are kept in the commingled account, the City has been using that money to pay the City's bills while it waits to pay the JWP bills, causing the late fees to be incurred by the JWP.

Although the percentage the Town has been charged has not changed recently, there is no rationale behind the amount. Neither the City nor Board could provide an analysis or any documentation to support this amount. As a result, neither the Board nor City officials know if the City absorbs or subsidizes any of the costs of these services, though the City is responsible for 51 percent of the overall cost of JWP operations.

Without an analysis of the time and costs incurred by the City to administer the JWP's financial activities, neither party can be confident it is being properly charged. In addition, without an accurate accounting of costs, the JWP cannot develop accurate annual budgets.

Contingency Fund

The IMA stipulates that the JWP budget include a provision for contingencies. A contingency line item may be included in the budget by a governing board to provide funding for unexpected events. It is important that the JWP be prepared for any such events.

The Board has not set aside funds for a contingency fund. JWP expenditures are reconciled to the penny at the end of the year, leaving no fund balance. In the case of an emergency or any unforeseen expenditures, the JWP would need to amend its budget and either transfer from a budget line or request additional funding from the City and Town. The Board Chair told us that, in the case of an emergency, the City and the Town would need to provide the money to cover the emergency.

As a result, the JWP is at risk of not having sufficient resources in the case of an emergency or not being able to pay unforeseen incidental expenditures that it may incur.

Recommendations

The Board should:

1. Ensure that the City makes the required quarterly estimated payments.
2. Ensure that bills are paid before or on due dates.
3. Ensure that the annual reconciliation is performed by March 1 of each year.
4. Ensure that the City deposits all quarterly payments from the City and the Town into a JWP account.
5. Analyze the time and costs incurred by the City to administer the JWP's financial activities to determine the accuracy of the 4 percent administrative service charge to the Town.

6. Ensure that the annual budget includes a provision for contingencies, as required by the IMA.

APPENDIX A

RESPONSE FROM JOINT WATER PROJECT OFFICIALS

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

Poughkeepsies' Joint Water Project Board

3431 North Road

Poughkeepsie, New York 12601



October 22, 2014

Office of the State Comptroller
Newburgh Regional Office
33 Airport Center Drive, Suite 103
New Windsor, NY 12553

Attention: Ms. Tenneh Blamah

Subject: Response to Report of Examination (2014M-236) approved by Joint Water Board on October 21, 2014

Dear Ms. Blamah:

The objective of the audit was to examine Joint Water Project (JWP) operations for the period January 1, 2013 through May 31, 2014. OSC then extended its scope to July 22, 2014 to review the annual reconciliation of expenditures and address the following related question: Did the Board provide sufficient oversight over the JWP's financial operations in accordance with the Inter-Municipal Agreement (IMA) between the City and Town? The Executive Summary of the Report states "The Board does not ensure that the JWP is operated in accordance with the IMA", and the Report then cites a few examples.

The City and Town of Poughkeepsie entered into an IMA on August 3, 1995 to form the JWP. The purpose of the JWP was and is to produce high quality water at low cost for the residents and businesses in the two municipalities. Water quality is maintained and costs stay low through the economies of scale and efficiencies made possible through this strategic municipal collaboration. The IMA also contemplates that the JWP may have excess capacity available for sale to neighboring communities.

The IMA provides that the Joint Water Board (Board) oversee the JWP on behalf of the City and Town. The Board is comprised of three members representing the City and three members representing the Town. The Board, like boards generally, may only carry out its powers and responsibilities by adopting resolutions to act upon the vote of a majority of its members. The Board may properly act, therefore, when it is empowered to do so by a provision of the IMA **and** the action is authorized by a majority vote of the Board.

In instances when a proposed resolution of the Board to act does not receive four votes, the Board has no power to act. In such instances it would be improper for the Board to take an action, even when the action is part of its responsibilities pursuant to the IMA. The City and Town agreed upon this governance structure in their IMA to ensure continued collaboration. Part of such collaboration includes interpreting and applying the IMA, an almost 20 year old

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agreement, in light of current realities. The Board therefore disagrees with the premise of the Report that the Board must adhere to every minute provision of the IMA no matter how immaterial or irrelevant the provision is now to the present priorities of the JWP and the municipalities that own it.

See
Note 1
Page 14

The Board notes that the Report cites no instance of violation of any rule of municipal finance. Rather the Report notes a handful of instances where the Board has not strictly adhered to a few provisions of the IMA. The Board believes that it has the implied power, as the representatives of the parties to the IMA, to make immaterial modifications to the IMA as part of its ongoing administration of the JWP.

Sincerely,

Mark Newton, Chairman
Poughkeepsies' Joint Water Project Board

APPENDIX B

OSC COMMENT ON THE JOINT WATER PROJECT OFFICIALS' RESPONSE

Note 1

The IMA between the City and Town is a legal contract that both parties must adhere to. Although, the Board may consider paying over \$13,000 in late fees to be immaterial, they were caused by the failure of the Board to require the City to make its quarterly estimated payments to the JWP as required by the IMA. This caused the JWP to not have enough money to pay its invoices on time. The late fees are an unnecessary expenditure that is passed on to the users in the form of water fees that result in the waste of user fee moneys. The JWP should be operated as efficiently as possible and in accordance with the IMA.

APPENDIX C

AUDIT METHODOLOGY AND STANDARDS

Our overall goal was to examine Board oversight of the JWP's financial operations. To accomplish our audit objective and obtain valid audit evidence, we performed the following procedures:

- We reviewed the IMA between the City and the Town.
- We interviewed JWP officials and Board members regarding JWP operations and oversight.
- We reviewed 271 invoices from the 10 highest paid vendors during the audit period to determine if payments were timely.
- We reviewed the 2013 expenditure water reconciliation for accuracy and appropriateness.
- We traced cash receipts from source documentation to the bank statements to determine if they were deposited in a separate account.
- We reviewed 2013 total expenditures for accuracy.
- We inquired as to the allocation of administrative costs and contingency provisions.
- We reviewed annual budgets for contingency provisions.

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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