

CITY OF ALBANY

# Office of Audit and Control

## **Performance Audit of the Albany Water Board - Accounts Payable**

**Audit Report  
June 2013**

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## PREFACE

The Office of Audit and Control exists to provide oversight, transparency and public accountability as a means to improve City services. This performance audit is a part of that function.

When the Office of Audit and Control takes on an audit client and, absent evidence of misconduct, that client addresses the audit's findings; it is our commitment to support and encourage their use of the audit process to improve their operations.

This audit was conducted with the full cooperation of the Department of Water and Water Supply and the Commissioner has committed to addressing its findings.

The proper use of the audit findings in these circumstances is to provide for oversight of the resulting changes and as the basis for informed public policy discussions.

Given that the Department of Water and Water Supply has given their full cooperation, it would be unfair and damaging to the audit process for this audit's findings to be used for political gain. As such, the Office of Audit and Control will view the political use of this audit's findings as detrimental to our mission.

We thank the Department of Water and Water Supply for their cooperation and commitment.

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## Executive Summary

The Department of Water and Water Supply (Water Department) has an excessive number of unpaid bills from 2010, 2011 and 2012. This is in spite of the fact that the Water Board has enough money to pay the outstanding bills. This situation arose when personnel failed to follow the adequate and appropriate internal controls adopted by the Water Board in 2010. As a result of this failure, when the Water Department's financial personnel attempted to provide Office of Audit and Control (OAC) with a complete list of its unpaid invoices, the list was missing a majority of the unpaid bills. As of the end of February, the Water Department vendors that responded to the audit questionnaire stated that they were owed \$17,116 from 2010 invoices, \$241,990 from 2011 invoices, and \$810,926 from 2012 invoices.

The impacts of this situation are numerous and obvious. First and foremost, many of the vendors who are owed money are local small businesses who depend on timely payments to keep their doors open and meet payroll. Beyond that, in order to obtain competitive prices, the City must be seen as a good organization with which to do business. Just as important is the need to properly plan the use of public resources. If a public utility is unaware of many of its expenses, it becomes difficult to accurately set rates and budget expenses. Most important to the City's water customers is that this situation makes it very difficult for the Water Department to determine the validity of the invoices it must pay.

Since the extent of this situation was brought to the management's attention in March, the processing of 2013 invoices has improved and \$369,000 of the 2011 and 2012 bills had been paid as of May 10<sup>th</sup>, 2013. Also, the Chief Fiscal Officer (CFO) has since resigned from her position. In response to the audit, the Water Department has committed to implementing the recommendations and diligently addressing the outstanding bills.

This situation would have been less likely to occur if the City had central intake of invoices. As the City's bill-paying process currently functions, invoices are mailed directly to departments. Outstanding invoices are not entered into the financial computer system or placed in a centralized file until after they have been signed by the department, the Purchasing Office, and then the Office of Audit and Control (OAC). As a result, invoices can sit unpaid at a department for many months with very few people knowing about it. If and when a new financial computer system is installed, the City should take that opportunity to initiate the central tracking of outstanding invoices from the date of receipt.

## Background

This audit was initiated as the result of issues identified in OAC's ongoing accounts payable audit process as well as a number of vendor complaints. In 2012, of all the city departments, the Water Department paid by far the largest number of invoices that were more than 10 months old. When OAC staff also considered vendor complaints about unpaid bills that were more than a year old, we concluded that there was a high likelihood that we would find a significant number of old, unpaid bills at the Water Department. As a result, the OAC audit plan was altered to accommodate this audit.

This performance audit was conducted in accordance with generally accepted government auditing standards (GAGAS) issued by the U.S. Government Accountability Office (GAO.) 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.

### Water Board Financial Structure

The Water Board is a New York State Authority that is a component unit of the City of Albany's finances. The Water Board receives the proceeds of the City's water customers' bills. It then uses that money to reimburse the City of Albany for the personnel, goods and services that it uses to provide water and sewer services to the customers. All Water Board bills and payroll are paid through the City's financial system and everyone who works on the Water Board's duties is a City employee assigned to the City's Department of Water and Water Supply.

## Scope, Objectives and Methodology

### Scope

The City of Albany's Department of Water and Water Supply accounts payable for January 1, 2011 through February 2013 was reviewed.

### Objectives

The objective of this audit was to determine whether the Department's accounts payable internal control policies are adequate and are being followed.

### Methodology

1. To determine if internal controls of the accounts payable management are adequate and being followed, OAC staff did the following:
  - a. Reviewed the Department's policy and procedures.
  - b. Interviewed the City Treasurer and the Chief Fiscal Officer of the Water Department.
  - c. Reviewed accounts payable aging and tested for compliance with the Department's policy and procedures.
  - d. Verified accounts payable balances by contacting vendors and confirming any outstanding balances the Water Department provided to OAC.
  - e. Looked at open Purchase Orders and compared them to contracts awarded in 2011 to identify issues.
  - f. Summarized outstanding balances from prior years.

# Audit Results

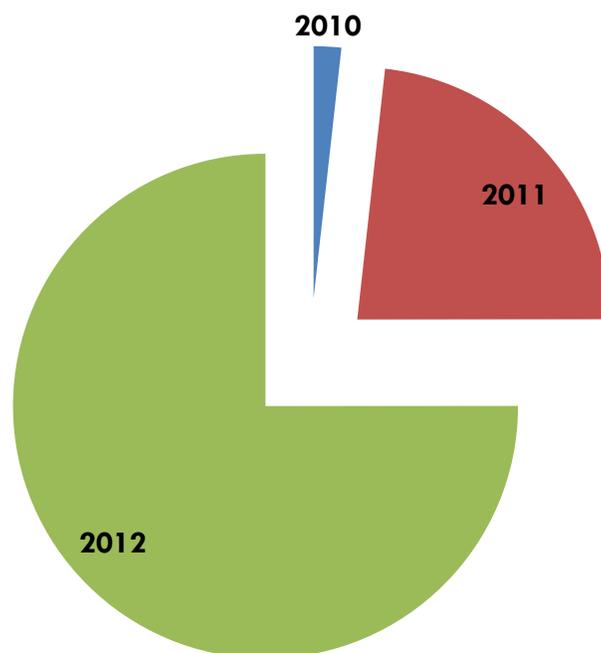
## Accounts payable management

The Department of Water and Water Supply adopted internal control policies in compliance with the NYS Internal Control Act, the Public Authorities Accountability Act of 2005 and the Public Authorities Reform Act of 2009. The most recent revision of the Albany Water Board, Albany Municipal Water Finance Authority Internal Control Policy – Purchasing is dated April 21, 2010.

The department does not appear to be in compliance with the April 2010 Internal Control Policy. The former CFO did not review vendor monthly statements and did not audit a minimum of 30 random vendor accounts monthly, nor did she delegate the responsibility to a staff member. Vendors reported outstanding balances from 2010, 2011, 2012 and 2013.

OAC mailed letters requesting confirmation of the Water Department’s accounts payable balances to 200 vendors. 160 vendors responded. 94 vendors agreed with the Water Department’s balance. 66 vendors did not agree with the Water Department’s balance. Vendors provided statements of outstanding invoices as of 2/28/2013 that totaled \$1,569,853 which was 136% more than the \$653,224 that the Water Department reported to OAC. \$17,116 of the vendor’s reported balances was outstanding from 2010 invoices, \$241,990 was outstanding from 2011 invoices, \$810,926 was outstanding from 2012 invoices and \$499,821 was outstanding from January and February 2013 invoices. The possibility exists that there is a larger outstanding balance as 40 vendors did not respond. Also, OAC may not have sent confirmation requests to all of the vendors for the Water Department.

**OUTSTANDING ACCOUNTS PAYABLE  
BALANCES AS OF 2/28/13**



Vendors called OAC and expressed frustration at the lack of payment on 2010, 2011 and 2012 invoices that were outstanding at the time of this audit. One vendor admitted changing invoice dates on 2011 invoices to 2012 dates. The vendor said that the change was made on advisement of staff at Water because they told the vendor that they were unable to process 2011 invoice payments. At a 5/9/13 meeting to communicate audit results the former Water Department CFO said that neither she nor her staff would ask a vendor to change an invoice nor did she remember approving and signing the voucher with the changed dates falsely stating that the materials were furnished to the municipality on the dates stated. The former CFO did in fact sign the voucher with the changed dates. A different vendor informed OAC that they had been told in February that “the check is in the mail” for 2011 unpaid invoices, but to date they have not received the check. The check number provided by the former CFO was not typical of the City check numbers and the Treasurer’s Department has no record of such a check being created.

OAC tracked payments since the audit began. The table below shows the balances reported by vendors as of 2/28/13 and the outstanding balances decreased by 2013 payments through 5/10/13. The Water Department is currently scheduling payments for outstanding invoices.

Outstanding Accounts Payable					
	2010	2011	2012	2013	TOTAL
Outstanding as of 2/28/2013	17,116	241,990	810,926	499,821	1,569,853
Outstanding after 2013 payments through 5/10/2013	15,488	177,729	505,968	144,181	843,366

**Finding 1 –The Water Department owed outstanding balances on vendor invoices from 2010, 2011 and 2012 as of 2/28/2013.**

Vendors responded to letters sent out by OAC that \$1,569,852 was outstanding as of 2/28/13 while Water Department supplied an amount outstanding of \$653,224.28.

Paying very old invoices significantly reduces the department’s ability to certify that the services or materials were rendered to the City on the dates stated and that the charges are correct.

Age of the outstanding balances:

- 2010 invoices totaling \$17,115 were not paid and were not recorded as expenses on the Water Department’s books as of 2/28/2013. Of the 2010 outstanding balance \$1,628 has been paid and \$15,488 is outstanding.
- 2011 invoices totaling \$241,990 were not paid and were not recorded as expenses on the Water Department’s books as of 2/28/2013. Of the outstanding balance \$64,261 has been paid and \$177,729 is outstanding.
- 2012 invoices totaling \$810,926 were not paid and were not recorded as expenses on the Water Department’s books as of 2/28/2013. Of the outstanding balance \$304,958 has been paid and \$505,968 is outstanding.
  - OAC reviewed progress on outstanding balances reported by OK Office Supply and WW Grainger. While WW Grainger’s outstanding balance has been brought up to date, OK Office informed OAC on 6/11/2012 of an outstanding balance of \$6,779 for 2011 invoices. OAC was contacted on 9/11/2012 and given a September 2012 statement of

outstanding invoices. Ok Office Supply then responded to the March 2013 OAC audit letter requesting confirmation of the outstanding balance reported by the Water Department on 4/29/2013 with an outstanding balance of \$3,579.

The following issues are examples of late payments. Staff did not follow departmental policy and procedures causing a breakdown in the accounts payable management resulting in outstanding balances and late payments.

1. Purchases were made on overspent or closed purchase orders and were processed for payment late or not at all.
  - a. 2012 purchases referenced 2012 Hershberg and Napa purchase orders that had been fully expended and 2013 purchase requisitions were submitted and processed to increase the 2012 purchase orders after the invoices were received by the Water Department.
2. A change order that increased the cost of the Bethlehem Avenue Area Stormwater Management System was not pre-approved by the Board of Contract and Supply, and the related purchase order was not increased to accommodate the additional cost of the change order before the work was completed by the contractor (Carver Construction). The change order was processed after the work was done, was approved by the Board of Contract and Supply, and the vendor was paid four months after the invoice was submitted to the Water Department. Additional work by M Sullivan on the Marion Avenue Stormwater Management System increased the contractor's original bid amount by \$9,904.61. In a 4/18/13 telephone conversation, the Water Department's former CFO said there was a change order for the Marion Ave project and she was looking into it. Subsequently, the Deputy Commissioner researched the issue and located the June 2012 change order. All change orders must be approved by the Board of Contract and Supply and the Water Department did not submit the change order for the Marion Avenue project. The Deputy Commissioner is working on obtaining the proper approvals so the outstanding balance can be paid.

### **Recommendation 1.1: Follow the established departmental policy “Albany Water Board Albany Municipal Water Finance Authority Internal Control Policy – Purchasing”.**

Process vendor invoices in a timely manner according to the Water Department's policy and procedures. From the Water Department's Policy and Procedures:

- “6. When an invoice is received, the Financial Analyst processes a voucher with supporting documentation. This is approved by the Chief Fiscal Officer and sent to the purchasing department for processing. Vouchers for professional services such as engineering are also approved by the Commissioner or Assistant Commissioner.*
- 7. Vouchers are processed in the purchasing department and forwarded to the Office of Audit and Control for audit and payment.”*

### **Recommendation 1.2: Review Vendor accounts to ensure that payments are processed in a timely fashion.**

From the Water Department's Policy and Procedures:

*“Once a month, the CFO or his/her designee will randomly select vendors for an internal audit. The minimum number of vouchers to be reviewed per month will be 30. Each voucher will be reviewed for the following:*

- 1. Original copies are in vendor file (i.e. office copy of voucher)*
- 2. Verification of signatures/approval.*

3. Proper and complete backup is attached to voucher to support payment.
4. Invoices are signed to verify actual receipt or performance of services by authorized personnel.
5. If the vendor is under an existing contract or agreement, the charges will be verified against terms of the document. (I.e. price, services provided, etc.)

*As part of the audit, all vouchers will be tied back to the general ledger for that vendor for the selected time frame. If there are missing invoices, a copy of the payment and its supported documentation will be requested from City Hall, and it will be noted as an exception in the report. The importance of looking at a vendor in totality is critical, since we will be able to track any variances or discrepancies, whether it lies in signatures, type of goods/services being provided and its frequency, reasonableness of such purchases, or duplication of payments. Since some vendors do provide statements on a monthly basis, any charges/payments should be tied back to that as well. Discrepancies in any of the above areas will be reported to the Commissioner and Assistant Commissioner.”*

**Recommendation 1.3: Monthly vendor statements should be reviewed by someone other than the person processing the vendor payments.**

Both invoices and vendor statements were given to the former CFO. The statements were not being reviewed, but no one knew that except the former CFO.

**Finding 2 – Late penalties of \$46,102 on property taxes were paid by the Water Department.**

The Water Department paid penalties totaling \$46,102.49 because property taxes for properties owned by the Water Board were paid three months after the due date.

**Recommendation 2.1: Pay property tax bills by the due date.**

Pay property tax bills by the due date in order to avoid paying late penalties and wasting public resources.

**Finding 3 – 2012 Purchase orders were overspent and 2013 purchase requisitions were submitted to increase 2012 purchase orders.**

Blanket purchase orders are overspent. 2012 expenses were incurred against purchase orders that were fully expended and 2013 purchase requisitions were processed in order to increase the 2012 purchase orders. Purchases made on a blanket purchase order should be tracked so the purchase order is not overspent and all purchases of goods or services are properly authorized.

**Recommendation 3.1: Track blanket purchase orders and related purchases.**

Track blanket purchase orders and related purchases to ensure that the purchase orders are not overspent and that unauthorized purchases of goods or services do not occur.

**Finding 4 – Invoice dates on unpaid invoices from 2011 were changed to 2012 dates and submitted for payment.**

A vendor was allegedly advised to change 2011 invoice dates to 2012; the bookkeeper was told by a Water Department employee that otherwise the invoices would not be paid. A Water Department employee approved the payment falsely stating that the materials were furnished to the municipality on the dates stated.

An invoice date should not be revised. Staff should not request that vendors change invoice dates or alter an original invoice. If the product was shipped to the customer when originally recorded, a customer request to change the date is grossly inappropriate and should not be considered, as changing invoice dates can indicate fraud, or at least financial reporting failures. Generally Accepted Accounting Principles (GAAP) requires that expenditures be recorded in the accounting period the expenditure is incurred. Changing invoice dates would cause expenses to be recorded in a different accounting period than when the expenses were incurred.

**Recommendation 4.1: Process invoices in a timely manner.**

Process invoices in a timely manner.

## APPENDIX

### MANAGEMENT RESPONSE

First, the Department of Water and Water Supply would like to commend the Office of Audit and Control for a thorough and comprehensive report detailing the accounts payable issue in the Department. The Department concurs with the findings of the report and will adopt, or has adopted, all of its recommendations.

Management in the Department first became aware of the accounts payable issue on December 8, 2012, when a vendor contacted the Commissioner's office directly concerning his outstanding unpaid invoices. The Executive Staff immediately investigated and found that this appeared more widespread than a single unpaid vendor. Until then, no one in management was aware of the issue since all late notices from vendors went directly to the now former Chief Fiscal Officer (CFO).

When confronted, the Department's former CFO, whose job was to process the invoices and to ensure all internal control procedures were being followed, acknowledged that she had not been, in her own words, "on task" with regard to her duties and responsibilities. She promised to rectify the problem. Simultaneously, the Office of Audit and Control already had begun its own inquiry after receiving complaints from other unpaid vendors.

Once we learned of the extent of the issue, the Department instituted day-to-day oversight of the financial office and the former CFO to ensure that invoices were being processed in a timely fashion. Despite repeated attempts to encourage the processing of outstanding late invoices, management concluded the level of progress was unacceptable. As a result, some of the duties previously assigned to the former CFO were assumed by the Executive Office staff. Finally, as a result of a team effort by the Executive Office staff, the number of unpaid invoices began to drop significantly.

Since the Department was not confident the former CFO could re-assume her duties, the staff began to discuss a change in leadership of the financial unit as the only viable next step to ensure timely processing of invoices and adherence to the Department's internal control procedures. The CFO resigned from the Department effective May 10, 2013.

Subsequent to the former CFO's resignation, an internal financial review of all activities involving the former CFO was undertaken. While the issues discovered in the audit report were generally confirmed, an additional issue (not within the scope of the audit) was also identified. In this regard, our review identified 23 vendor checks, approximating \$90,000 in total, disbursed directly from restricted Board and Authority accounts which should have been approved, processed, and disbursed by the City.

Although these disbursements were paid to valid Department vendors and appear to be supported by valid vendor documentation, such disbursements were in conflict with established Department and City purchasing policies and control procedures. This issue, similar to the accounts payable issue, appears to be limited to actions of the Department's former CFO. Significantly, without minimizing the importance of these procedural issues, our review disclosed no evidence of misuse of cash, fraud, or similar irregularities in connection with the activities of the former CFO.

The internal review also resulted in several recommendations relating to the disbursement and approval procedures from these restricted accounts. These recommendations, along with those recommendations discovered in the audit, are in the process of being adopted

Finally, as of June 4, we are pleased to report that substantially all invoices identified in the audit have been processed by the Department, essentially eliminating the backlog. Staff is working diligently to stay current as 2013 invoices come into the Department. In addition, the Department is in the process of recruiting a new CFO.

**AUDITORS' RESPONSE**

We would like to thank the Water Department management for their cooperation during this audit and for taking the initiative to review the Board and Authority Accounts. We will meet with them and their accounting consultant to review the disbursements and controls for these accounts and to determine if any duplicate invoices have been paid.