

NIAGARA FALLS WATER BOARD

**Communication of Matters Related to Internal Control
Over Financial Reporting and Other Matters
December 31, 2020**

August 9, 2021

To the Board of Directors of
Niagara Falls Water Board:

In planning and performing our audit of the financial statements of the Niagara Falls Water Board (the Water Board) as of and for the year ended December 31, 2020 in accordance with auditing standards generally accepted in the United States of America, we considered the Water Board's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Water Board's internal control. Accordingly, we do not express an opinion on the effectiveness of the Water Board's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore material weaknesses or significant deficiencies may exist that were not identified.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented or detected and corrected on a timely basis. We did not identify any deficiencies in internal control that we consider to be material weaknesses.

A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

During our audit, we became aware of the following deficiencies in internal control other than significant deficiencies or material weaknesses, and other matters that are opportunities for strengthening internal controls and operating efficiency.

This communication is intended solely for the information and use of management, the Board of Directors, and others within the Water Board, and is not intended to be and should not be used by anyone other than these specified parties.

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NIAGARA FALLS WATER BOARD

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The following matters are considered deficiencies in internal control:

1. TIMELY REVIEW OF JOURNAL ENTRIES

Observation

We recognize that 2020 posed interesting challenges for most organizations due to the impact of the global pandemic in the United States. However, throughout fiscal 2020, we noted that journal entries were not approved and posted on a timely basis. The entries themselves were prepared and submitted for approval timely; however, in many cases we found the actual approval and posting of the entries occurred months after submission. Because the nature of the Water Board's operations, full closure was not an option during the pandemic and business was occurring as usual. Failure to post financial activity on a timely basis at any time poses a risk to the organization and puts the Board in a position to be making decisions on incomplete data.

Recommendation

Subsequent to year-end, personnel changes were made, and journal entries are being posted on a timely basis. However, given the current vacancy in the Director of Finance position, the segregation of duties that is normally in place is not operating as intended. It is important to ensure that the process for preparing journal entries is separate from the approval and posting of journal entries and that all entries are posted timely.

2. PAYROLL

Observation

During our audit, we noted that the Water Board currently uses a timeclock system for its employees. However, this time clock system is not integrated directly with the payroll system and therefore is only used as a check, if necessary, to determine whether an employee was working. Instead of using the timeclock to track time, Department Supervisors provide spreadsheets to payroll noting the hours worked for each employee during that pay period. These spreadsheets are used to manually record the payroll in the general ledger. Payroll is the single largest expense for the Water Board.

Recommendation

We recommend that the Water Board consider integrating the timeclock system into the payroll process to reduce not only the amount of effort needed by the payroll staff, but also the risk of inaccurate reporting of employee time. With a manual process (such as the Water Board's current process which requires payroll personnel to manually enter all information provided into the system), there is room for error. Integrating these two systems would reduce the likelihood of an error occurring.

3. APPROVAL OF BUDGET TRANSFERS

Observation

During our planning procedures, it was noted that the Board wasn't approving budget transfers for the first half of 2020, as the Director of Finance wasn't aware that the Board should be approving these.

Recommendation

As it is the responsibility of the Board to approve the budget, it is also their responsibility to approve any modifications to the budget. Therefore, we recommend that the Board implement a formal process in which any budget amendments or transfers be reviewed and approved by the Board. This policy could include various thresholds under which certain levels of management can initiate and approve transfers before Board action is required.

4. MANUAL SPREADSHEETS

Observation

We noted that several significant financial areas are tracked manually using excel spreadsheets prior to being recorded in the general ledger. For example, accounts payable for the Plant fund, capital project activity and capital assets are all currently tracked outside of the software. Such a system creates a potential for error due to the manual nature of the process.

Recommendation

We recommend that the Water Board consider utilizing capital asset software to help manage and maintain the capital asset activity, including all work-in-process. Additionally, we recommend that any capital project activity be tracked and recorded in the general ledger as it occurs.

5. CENSUS DATA TESTING

Observation

As part of our audit procedures, we selected 25 individuals (including active employees and retirees) who were included in the census information sent to the Water Board's actuary to determine the Water Board's other postemployment benefits liability. As a result of this testing, we noted several actives and retirees who were active prior to the transfer of operations from the City to the Water Board that did not have documentation in their files regarding their benefit elections and other personal information.

Recommendation

As the payer of these benefits, it's important that the Water Board have complete and accurate files. Therefore, we recommend that for those individuals where the Water Board doesn't have complete information, a form should be sent requesting the basic information (name, address, etc.), as well as missing information (elections, etc.) and have them sign and returned to the Water Board.

6. UNCOLLECTIBLE BILLINGS

Observation

The Water Board currently has a significant balance of uncollectible water and sewer billings that is being carried, and this amount increases annually. Based on our audit procedures and inquiries of management, 100% of the amounts transferred to the City of Niagara Falls from one-year prior to December 31, 2020 are reserved as uncollectible. Of that, a small percentage of the amounts transferred are ultimately collected through the City of Niagara Falls tax re-levy process. In addition, 100% of the amounts more than 120 days old from the non-transferred receivables are reserved as uncollectible. The financial impact of these allowances is that over \$6.3 million has been deemed uncollectible as of December 31, 2020. The Water Board, in various bond issuances has covenanted that it will enforce the payment of any and all charges owed to the Water Board for use of the System. The Act (Public Authorities Law Section 1230-j(6)) provides that any rates, fees, and charges that remain unpaid shall constitute a lien on the premises that received the service and that such lien may be enforced in the same manner as a lien for taxes. The Board is currently not receiving any supporting documentation or verifying if amounts collected through the tax process are getting remitted to the Water Board from the City.

Recommendation

We recommend that the organization review all outstanding accounts receivable and determine whether those amounts are in fact uncollectible and those amounts should be written off the books. Additionally, for those customers that are deemed uncollectible, an assessment should be made to ensure that no additional services are being provided to those customers. The organization should consider working with the City of Niagara Falls or the County of Niagara to use American Recovery Plan funds available to assist with getting customers in Qualified Census Tracts current on their utility bills. This is a specific allowable distribution of these funds. Additionally, it's critical that the Water Board develop a process to reconcile the list of transferred billings to the actual collections, and to further verify that collections from the City are being returned to Water Board.

7. TRIAL BALANCE REPORTING

Observation

In connection with our audit, we noted that the Authority's trial balance does not support the information reported in the external financial statements. Specifically, the long-term debt is reported and tracked in the Plant fund trial balance along with the assets. So, there is no standalone financial tracking of the Authority separate and distinct from the Water Board.

Recommendation

The debt, under the enabling legislation, belongs to the Authority and should be reported consistently internally and externally. Therefore, we recommend that management review the current accounting for these transactions and make the necessary adjustments to ensure that all internal reporting is consistent with the audited financial statements.

8. INTERFUND ACTIVITY

Observation

We noted that interfund balances between the Water Board, Plant, Water, and Sewer trial balances have been accumulating for several years. As of December 31, 2020, the accumulated amounts owed between funds was approximately \$8.1 million; however, a significant portion of that balance does not represent an amount that will be repaid between the funds.

Recommendation

We recommend that management review the interfund activity and only record amounts due to or from that have an expectation of repayment. If amounts are not to be repaid, then any funds moved from one fund to another should be reflected as a transfer in or out on an annual basis.

9. SEGREGATION OF DUTIES

Observation

During our audit, we noted instances where segregation of duties should be reviewed and the identification of key controls over activities should be documented. The Water Board has undergone a significant amount of turnover in recent years which has led to a concentration of certain duties.

Recommendation

We recommend that the Water Board study the current internal control environment and develop a plan to reassign non-compatible duties, provide additional monitoring of functions and create cross-training of certain functions as appropriate. Additionally, in connection with this analysis, the Water Board should ensure that key controls are identified and documented for all accounting transaction cycles within the organization.

The following are considered other matters for the consideration of management:

10. REVIEW OF POLICIES SURROUNDING ABANDONED PROPERTIES

Observation

During our planning procedures, it was noted that there is currently a policy in place pertaining to the treatment of abandoned properties. Under the current policy, the Water Board continues to provide water to, and send bills to, houses which are abandoned.

Recommendation

We recommend that the Water Board review the policies and procedures currently in place surrounding abandoned properties to ensure that the procedures are operating effectively and are minimizing the risk of water loss whenever possible and within current regulations.

11. COMPLIANCE WITH LAWS AND REGULATIONS

Observation

The Water Board and Authority's books and records were not ready for audit in time to enable management to file their 2020 annual report and audit with the Authorities Budget Office (ABO) in accordance with the Public Authorities Reform Act. While they met the March 31, 2020 deadline for filing the December 31, 2019 audit, this was only a result of the extensions provided due to the global pandemic that was occurring. Under the Public Authorities Reform Act, all budgets are due to the ABO by November 1st of the year prior to the budget being effective. The Water Board's 2021 budget was submitted to the ABO on December 31, 2020. In addition, the Water Authority's 2020 budget was submitted over 3 months after the due date. The Authority's 2021 budget has not yet been filed with the ABO and was due on November 1, 2020. The Authority has failed to file their annual report and audit reports for 2019, which are due by 3/31 of the subsequent year.

Additionally, the ABO requires that each Board member "participate in a State approved training regarding their legal, fiduciary, financial and ethical responsibilities as board members of an authority within one year of appointment to the Board". During our testing, we were not able to ascertain if the Authority Board members have completed this.

The ABO also requires that board members complete an Acknowledgement of Fiduciary Responsibility upon appointment. During our testing, we noted that the Authority was unable to provide these forms for 2 Authority board members.

Recommendation

The Board and management have a fiduciary responsibility to comply with the laws and regulations of the State of New York. Based on our findings that several of the required compliance actions are not being performed, we recommend that the Water Board and the Authority review the guidance put forth by the ABO and ensure that all required elements are being performed. The Water Board and the Authority must ensure that all necessary procedures are in place to meet these regulations.

12. INTERNAL BILLINGS

Observation

During our audit, it was noted that the Water Board bills themselves for water and sewer charges for owned facilities. Subsequently, checks are cut and sent over to the City to be processed as part of collections and are then remitted back to the Water Board. Annually, as part of the audit process, this activity is reversed out of revenue and expense on the books of the Water Board to ensure these amounts are not overstated. The total activity approximates \$1,000,000 annually.

Recommendation

We recommend that the Water Board discontinue the practice of cutting checks to themselves for use of their owned facilities. Instead, interbank transfers and interfund transactions should be utilized to account for this activity.

13. INFORMATION RISK MANAGEMENT

Observation

Based on our discussions with Water Board personnel during planning, we have noted that the technology controls within the organization include some undocumented policies and practices or are based solely on external mandates and laws. Furthermore, formal IT risk assessments are not being performed and security awareness training is not documented as occurring on a regular basis. It was communicated that the Water Board does not maintain a Computer Security Incident Response Plan and therefore may not be able to sufficiently respond in the event of an incident.

Recommendation

While laws and regulations are intended to outline the minimum expectations and protocols, each organization should have specific policies that are tailored to their operations and activities. The lack of a formal documented policies and procedures exposes the Water Board to possible interruptions and potential loss or corruption of data. In light of the national cyber-attacks against critical infrastructure, it is imperative that the Water Board fully assess and address the weaknesses that may exist.

14. WATER LOSS CONTROL

Observation

Based on our review of reports provided by the Board, the average annual volume of unaccounted for water has been approximately 68-70% since 2011. The impact of this loss is an estimated \$400,000 - \$500,000 on an annual basis. Additionally, on top of this unaccounted-for water, there are amounts billed to residents under the DRIP program, but which is ultimately credited back on their bills. There are currently over 200 residents that are included in this program. Therefore, the actual cost to the Board related to unaccounted for or unbillable water is much greater than half million dollars annually. Nationally, the average amount of water loss is less than 20%, and, in some reports, as low as 16% (according to a study by the US EPA). Based on reports provided by management, the water losses in systems in and around Niagara County range from 22-74%. Water loss can occur in many ways, either unknown resulting from leaks and theft, to those known instances like fire suppression and flushing of mains.

Recommendation

To ensure long-term viability of the organization, a plan to systematically locate and remediate water loss must be put into place. Water losses at 3 times the national average, or at the upper end of the Niagara County region, for at least the past 10 years is not sustainable. Identifying and securing funding for assistance in stemming these losses should be a priority for the Water Board going forward. Additionally, developing a specific operational or capital budget line for leak detection, prevention and correction is critical to the success of reducing these losses.

15. BANK RECONCILIATIONS

Observation

During our audit of cash and the accompanying bank reconciliations, we noted old outstanding checks that were being carried over an annual basis.

Recommendation

We recommend that management review those outstanding checks and either remit the amounts to New York State under the unclaimed property laws, void and reissue the checks, or determine if the obligation was otherwise satisfied and can be returned to the Water Board's cash.

16. SUPPORTING DOCUMENTATION AND FUTURE GASB PRONOUNCEMENT

Observation

In 2017, the Governmental Accounting Standards Board (GASB) issued Statement Number 87 – Leases, to better meet the information needs of financial statement users by improving accounting and financial reporting for leases by governments. This Statement requires the recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and recognized as inflows of resources or outflows of resources based on the payment provisions of the contract. Under this Statement, a lessee is required to recognize a lease liability and an intangible right-to-use lease asset, and a lessor is required to recognize a lease receivable and a deferred inflow of resources. This Statement was originally effective for the Water Board during the year ended December 31, 2020; however, Statement Number 95 will allow the Water Board to postpone the implementation of Statement Number 87 for 18 months.

As part of the audit, we obtained contracts, documents, and agreements to support various components of the audit. While we ultimately were able to obtain what we needed, at times it took considerable effort internally to locate the information.

Recommendation

In preparation for the implementation of this Statement, we recommend that the Water Board accumulate a listing of all significant contracts and/or lease agreements and review all such agreements to determine how they will need to be reported once this Statement is implemented. To best do this, we encourage management to begin a process of centralization of all key contracts, grants, documents, and agreements that have financial implications to be maintained in the Finance office. This will facilitate retrieval in the future and ensure that all accounting is proper.