



Is your Water and Sewer System in Financial Trouble?

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Learn. Invest. Grow. Prosper.

Local Government Financial Reporting in NC

- NC General Statutes requires adherence to generally accepted accounting principles (GAAP) for annual external financial reporting
 - GAAP represents national standardized reporting
 - Necessary for participation in debt market and grant environment
 - All local governments and public authorities, regardless of size, must adhere to requirement



Financial Reporting (cont.)

- Other quick facts
 - Reports are due to the Local Government Commission no later than October 31st
 - Audits must be conducted by an independent certified public accountant, chosen by the entity's governing board
 - Financial statements present *both* an economic picture of the organization, as well as a financial picture



What is an audit?

- Local governments and public authorities are required by G.S. 159-34 to have an annual *independent* audit
 - Contracted by the governing board
 - Bid process recommended but not required
- Auditors opine on whether or not the financial reporting follows GAAP, NOT on the financial condition of the entity



What is an audit? (cont.)

- Auditing standards have greatly “tightened up” on the relationship between auditor and client
 - Many governments receive findings that they have a weakness because staff cannot prepare their own financial statements
 - Auditors can propose entries and financial reporting options, but decisions may only be made by the entity’s management



Economic vs. Financial Perspectives

- Assets – Liabilities = Equity
- Economic equity represents *all* assets and *all* liabilities
 - Business perspective; likewise for proprietary funds and government-wide picture
 - Such equity referred to as net position
- Financial equity represents *financial* assets and *current* liabilities
 - Unique perspective of the governmental funds
 - Such equity referred to as fund balance



Net Position

- Equity used for proprietary funds (e.g., water, wastewater, electric)
- Equity position of the government-wide financial statements
- ***Net position does not reflect liquidity***
- Represents an *economic equity*
 - Net investment in capital assets
 - Restricted net position
 - Unrestricted net position



Enterprise Funds – How Are They Used?

- What is an Enterprise Fund?
- Why does government use them?
- Why are there so many different statements in my audit?
- What do these statements really tell me?



Enterprise Funds – How Are They Used?

- Enterprise Fund – may be used to report any activity for which a fee is charged to external users for goods and services.
- Required for activity financed by debt secured by pledge of revenue from fees and charges for the activity i.e. revenue bonds
- Used when you want to treat the service as an “enterprise” or business



Enterprise Funds – How Are They Used?

- In NC, most common enterprise fund is Water and Sewer
 - Others include Electric Funds, Solid Waste, Airports, Public Hospitals, School Food Service, Public Transportation, and a few recreation facilities
- Intended to be self-supporting
 - Not subsidized by tax revenues
- Enterprise Fund accounting helps measure full cost of providing the service
- Very similar to accounting for private business without income tax implications



Enterprise Funds – How Are They Used?

- Required Financial Statements
 - Full Accrual Basis of Reporting
 - Statement of Net Assets
 - Statement of Revenues, Expenses, and Changes in Net Assets
 - Statement of Cash Flows
 - Budgetary Basis of Reporting
 - Schedule of Revenues and Expenditures
 - Capital Project Schedule of Revenues and Expenditures



Enterprise Funds – How Are They Used?

- What is the difference between full accrual and budgetary reporting?
 - Full accrual accounting records revenue when it is earned and expenses when they are incurred – when cash is received or disbursed is irrelevant
 - Statement of Net Assets
 - Statement of Revenues and Expenses



How to Get the Most Out of Your Enterprise Fund

- Budgetary Reporting
 - Modified Accrual records resources when measurable and available and expenditures when paid and those that will be paid from current resources
- Advantages and disadvantages to both



How to Get the Most Out of Your Enterprise Fund

- Cash Flow Statement
 - What does it tell me?
 - Cash flow from operations
 - Cash flows from noncapital financing activities
 - Cash flows from capital financing activities



Enterprise Funds – How Are They Used?

- Budgetary Schedules
 - Primarily a management tool
 - Also report compliance with budget
 - Use of fund balance to balance budget



Enterprise Funds – How Are They Used?

- Enterprise Capital Project Funds
 - Budgetary schedule
 - Why does this fund “disappear” when you do the full accrual statements?
 - Why do we use separate schedules and budgets for capital projects?



Enterprise Funds – How Are They Used?

- Interim reporting for Enterprise Funds
 - Budgetary report
 - Accounts receivable and payable
 - Other current assets and current liabilities
 - Cash



Communications with Elected Officials

- Statutes charge staff to LGC with oversight responsibility and approval of most debt issued by local governments
- Analyze audit data to measure fiscal health of each entity
 - What data is key?



Communications with Elected Officials

- Budgetary compliance
- Liquidity measures in enterprise funds
 - Ratio of liquid assets to current liabilities
- Cash flow from operations and after debt service
- Income on budgetary basis
- Internal control issues and other findings
- Other statutory compliance issues



Communications with Elected Officials

- Results of our analysis may result in unit letter to elected officials
- Written documentation of our concerns
- Ask for a response within 45 days
- Letter and response go to LGC if unit is seeking debt approval



Communications with Elected Officials

- How should you respond?
 - Promptly
 - Thoroughly; be sure to address each item discussed in the letter
 - With action whenever possible; describe results of action
 - Planned action as applicable



Communications with Elected Officials

- SLGFD staff may contact you for follow up
- Staff also may offer to visit unit
 - Often most effective if unit has internal control challenges
 - Not punitive
- If debt issuance is pending, may ask officials to come to Raleigh for meeting
- May suggest you attend LGC meeting when your item is up for consideration



Strategies For Maintaining Fiscal Health

- Operating in Current Environment
 - Communication more important than ever
 - Management
 - Board
 - Department heads
 - Staff
 - Press
 - Current and accurate record-keeping



Strategies For Maintaining Fiscal Health

- Operating in Current Environment (cont.)
 - Monitoring budget
 - Amend regularly
 - Watch revenues – amend as necessary
 - Tighten or continue firm enforcement of purchase orders – be mindful of open orders
 - Strict enforcement of pre-audit for purchases and for contracts
 - Bid contracts and services
 - Travel
 - Training



Strategies For Maintaining Fiscal Health

- Operating in Current Environment (cont.)
 - Interim financial reports
 - Budget to actual
 - Current assets and current liabilities
 - Cash flow projection



Strategies for Maintaining Fiscal Health

- Transfers from Water and Sewer Fund
- **159G-37. Application to CWSRF, Wastewater Reserve, DWSRF, and Drinking Water Reserve -**
(b) Certification. - The Division of Water Infrastructure shall require all local governments applying for loans or grants for water or wastewater purposes to certify that no funds received from water or wastewater utility operations have been transferred to the local government's general fund for the purpose of supplementing the resources of the general fund. The prohibition in this section shall not be interpreted to include payments made to the local government to reimburse the general fund for expenses paid from that fund that are reasonably allocable to the regular and ongoing operations of the utility, including, but not limited to, rent and shared facility costs, engineering and design work, plan review, and shared personnel costs.



Strategies for Maintaining Fiscal Health

S427 2011 Session

- One of outcomes was that units are supposed to show that rates are adequate to cover operating costs and debt service before State grants or loans are given for expansion of water systems



Internal Controls

- What do we mean by “internal controls”?

*as **defined** in accounting and auditing, is a process for assuring achievement of an organization's objectives in operational effectiveness and efficiency, reliable financial reporting, and compliance with laws, regulations and policies*



Internal Controls

A business practice, policy or procedure that is established within an organization to create value or minimize risk

A series of business processes, practices and policies that, when followed, ensure that no one person controls a transaction from beginning to end



Internal Controls

- Good internal control goes beyond segregation of duties
 - Important but not the only concern
 - Collusion will circumvent even the strongest system of internal control
 - Tone at the top



Internal Controls

- But I trust my employees!
- Trust but verify
- Professional skepticism
- Good internal controls are designed to catch human errors in addition to fraud
- Auditors must test internal controls, but that is not foolproof



Internal Controls

- Why should you be concerned?
- LGBCFA states that “ Each local government or public authority shall establish and maintain an accounting system designed to show in detail its assets, liabilities, equities, revenues, and expenditures. The system shall also be designed to show appropriations and estimated revenues as established in the budget ordinance and each project ordinance as originally adopted and subsequently amended.” (§ 159-26)



Internal Controls

- As elected officials, you are ultimately responsible for the accounting system in your unit of government



Internal Controls

- What can you do?
 - Tone at the top
 - Staffing and training
 - Be a part of the solution
 - Roles that board members can play in maintaining effective internal controls
 - Use annual audit as a learning experience, not as a burden



Internal Controls

- Memos
 - #568 - *Internal Controls*
 - #569 - *Internal Controls in Small Governments*



Internal Controls

- Signs that you have internal control weaknesses:
 - Material errors in financial records that go undetected until the audit
 - Records that are not ready to be audited in a timely manner
 - Unit is paying penalties and/or interest on payroll liabilities or accounts payable



Internal Controls

- Material budget overexpenditures on a regular basis
- Lack of cross-training among staff
- Sensitive documents are easily accessible
 - Check stock
 - Passwords
 - Personal data



*OPPORTUNITY is the single biggest
reason that frauds occur
in any sector!!*



Internal Controls

- Signs of potential fraud
 - Staff member that works unsupervised much or most of the time
 - Staff member that refuses to take leave
 - Staff member that insists on getting mail
 - Staff member that begins living beyond their means



Internal Controls

- Where is your exposure?
 - Credit cards and p-cards
 - Petty cash
 - Cash deposits
 - Personal use of unit assets
 - Using unit assets to satisfy personal expenses or debts



Internal Controls

- Establish strong written policies over use of
 - Credit cards and p-cards
 - Town owned assets – vehicles and electronics
- Establish strong operational policies over cash receipts, disbursements, petty cash and account reconciliations
- Work with accounting software vendor to strengthen system controls
- Have staff sign policies as applicable



Internal Controls

- Look for abnormalities in data
- Require monthly reports from finance and ask questions!
- Require auditor make a formal presentation of the audit in open board meeting and ask questions!
- Utilize unit attorney
- Check with SLGFD and SOG staff



Internal Controls

- What do we do if we suspect fraud?
- Are we required to “call in the authorities”?
- What is the exposure for elected officials?



Questions?

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Thank You!

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