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County of Erie

NANCY A. NAPLES
COMPTROLLER

December 21, 1998

Ms. Laurie Manzella
Clerk of the Legislature
Erie County Legislature
25 Delaware Avenue
Buffalo, New York 14202

Dear Ms. Manzella:

Enclosed are three copies of the management letter that was issued by Deloitte & Touche LLP in conjunction with the audit of the County's financial statements for the year ended December 31, 1997.

Please be advised that although the management letter is dated June 18, 1998, this represents the date when the auditors completed their field work for the 1997 audit. The letter was only recently released for distribution.

Please see that the enclosed management letters are distributed as follows:

- One copy is to be filed with the Legislature.
- Two copies are for use by the Chiefs of Staff to the Majority and Minority.

Thank you.

Very truly yours,

Nancy A. Naples

NANCY A. NAPLES
County Comptroller

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ERIE COUNTY OFFICE BUILDING, 95 FRANKLIN STREET, BUFFALO, NEW YORK 14202 - PHONE: (716) 858-8400 - FAX: (716) 858-8507

LAURIE MANZELLA
CLERK
LEGISLATURE

Deloitte & Touche

Deloitte & Touche LLP
Suite 250
Key Bank Tower
50 Fountain Plaza
Buffalo, New York 14202

Telephone: (716) 843-7200
Facsimile: (716) 856-7760

June 18, 1998

Honorable County Legislature
County of Erie
Buffalo, New York

Dear Honorable Legislators:

In planning and performing our audit of the general purpose financial statements of County of Erie, New York ("the County") for the year ended December 31, 1997 (on which we have issued our report dated June 18, 1998), we considered its internal control structure in order to determine our auditing procedures for the purpose of expressing an opinion on the general purpose financial statements and not to provide assurance on the County's internal control. Such consideration would not necessarily disclose all matters in the County's internal control that might be material weaknesses under standards established by the American Institute of Certified Public Accountants. A material weakness is a condition in which the design or operation of one or more internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control and its operations that we consider to be material weaknesses as defined above.

We did note other matters related to the County's internal control and certain other accounting, administrative and operating matters. Our comments and management's responses are presented in Exhibit I.

This report is intended solely for the information and use of the legislative board, management and others within the organization.

We will be pleased to discuss these recommendations with you, and, if desired, to assist you in implementing any of them.

Yours truly,

Deloitte & Touche LLP

Deloitte Touche Tohmatsu

FINANCIAL SYSTEMS

During the course of our audit, we noted items related to the County's computer software program, Solutions for Government (SFG), which could be improved. Items noted included:

- ***Accounts Payable Reconciliations*** - we noted that the County experienced difficulty in producing an accounts payable detail report which agreed to the general ledger control account. We were advised that the County had no such difficulty for the year ended December 31, 1996 and that the difficulty was first noted in preparing for the 1997 audit. Apparently an "SFG software upgrade" was installed in 1997 after which a previously acceptable reporting capability was lost. We recommend that the County reconcile accounts payable on a monthly basis. This would improve internal controls over accounts payable and identify errors on a more timely basis.

  Comptroller's Office Response - We have implemented a monthly accounts payable reconciliation of the accounts payable module to the general ledger.

- ***Accounts Receivable Reconciliations*** - we noted that the accounts receivable module did not agree to the general ledger at year end. Upon further investigation, it was discovered that the general ledger accounts receivable control account was not being reconciled on a monthly basis to the detail per the module. A reconciliation was performed at year end. We recommend that the accounts receivable detail be reconciled to the general ledger on a monthly basis. This would improve internal controls over accounts receivable and identify errors on a more timely basis.

  Comptroller's Office Response - We have implemented a monthly accounts receivable reconciliation of the receivable module to the general ledger.

- **Property Tax System** - we noted that the property tax system does not automatically interface with the general ledger system. Throughout the year, many collections were posted to the incorrect accounts. This ultimately led to a year-end reconciliation process. We recommend that the County investigate the potential for interfacing property tax and general ledger systems.

  Division of Budget, Management and Finance Response - The Property Tax System is a stand-alone system with a manual interface to the General Ledger System. The effort required posting all tax transactions to all general ledger accounts is very labor intensive. The approximate three-day year end reconciliation process to post all tax transactions is the most feasible way to solve this situation. The Division of Budget and Management and the Division of Information and Support Services will again investigate the feasibility of automating the posting process.

INTERNAL CONTROL MATTERS

Several items came to our attention that may assist the County in further improving internal control over assets and in minimizing the risk of potential loss. Specific items noted include:

- ***Tax Information Reporting for Uniform Allowances*** - we noted that the County provides uniform allowances for County Sheriffs. The County utilizes a "nonaccountable plan" type in that the County pays its employees $750 without requiring the employee to account for how this money is spent. These amounts should be included in gross income and reported as wages or other compensation on Form W-2. Additionally, such amounts are subject to withholding and payment of employment taxes. The County has not appropriately included such amounts in gross income.

  We recommend that the County report uniform allowances in accordance with the Internal Revenue Code. This can be accomplished by either reporting such an allowance on Form W-2 or, alternatively, by requiring employees to account for allowances. The penalty for noncompliance with these regulations could be significant. Further, we recommend the County consider a more thorough review of its payroll reporting system and applicable requirements.

  Division of Budget, Management and Finance Response - The Division of Labor Relations has advised all unions involved that the County has a "nonaccountable plan", and as such the amounts will be included in gross wages or other compensation on Form W-2.

- ***Employee Handbook/Code of Conduct*** - in implementing Statement on Auditing Standard No. 82 "Consideration of Fraud in a Financial Statement Audit" (effective on or after December 31, 1997), we noted that the County's Employee Handbook had not been updated since 1988. A Code of Conduct is contained in the Handbook. We also noted that there is no procedure in place to ensure that employees have read and understand the Handbook.

  We recommend that the County update its Employee Handbook. We also recommend that the County require each employee to sign a statement annually indicating that they have read and that they understand the contents of the Handbook.

  Department of Personnel Response - The Erie County Employee Handbook has recently been revised. The Handbook will be ready for final printing and distribution very soon. The County requires all employees to sign a statement indicating receipt of the employee Handbook. It is their responsibility to read the Handbook and ask any questions they may have concerning the content. The Department of Personnel will be discussing with the Division of Labor Relations the recommendation to have all employees' sign a statement indicating they have read and understand the contents of the Employee Handbook.

- ***Unrecorded Cash*** - During our testing of cash accounts we sent confirmations to various banks requesting a listing of all bank accounts using the County's federal identification number. We noted that a few accounts established by departments of the County use the County's federal identification number; however, such accounts do not appear on the County's Treasurer's Group of Accounts.

  We recommend the County add these accounts to the Treasurer's Group of Accounts.

  Comptroller's Office Response - We will follow the recommendation to add the accounts to the Treasurer's Group of Accounts. The County's federal identification number has been properly used by the County departments involved.

- ***Disaster Recovery Plan*** - While the County has developed a "disaster recovery plan" relating to its computer systems, it does not appear that the Plan is regularly tested. Additionally, the Plan could be expanded (i.e. step by step recovery procedures, LAN-WAN details, identification of specific processors for Unisys, Health Systems, etc.). Depending upon the severity of the disaster, the possibility exists where information services could be unavailable for a significant and unacceptable period of time. The County should consider expanding and annually testing its disaster recovery plan.

  Division of Information and Support Services Response - The County will consider expanding and annually testing its disaster recovery plan.

DEPARTMENT OF SOCIAL SERVICES MATTERS

The County annually expends over 50% of all General Fund resources on the area captioned in its financial statements as "Economic Assistance and Opportunity". This category generally represents the social service programs which are overseen by the County. While many of these costs are mandated, the significance of these costs demands that the County control and accurately account for such to the extent possible. Items noted include:

- ***Sanctions*** - The County has identified a significant potential liability relating to various Department of Social Services "sanctions". These sanctions represent disallowed aid (which may be recouped by New York State at a later date) due to error or inadequate or untimely documentation related to social service case files or automated systems. The County has successfully challenged and reduced similar sanctions in the past and has represented its intent to vigorously refute the pending claims. We encourage this effort and suggest additional attention/staffing be designated to continue efforts to reduce pending sanctions.

  Equal in importance to refuting the current sanctions is implementing processes to deter/avoid future sanctions. A genuine effort by the County to correct the underlying cause for existing errors will enhance the County's position in efforts to avoid future penalties. Further thoughts and recommendations include:

  - Some of the errors noted appear to be repetitive. Others appear to derive from deficiencies inherent in New York State mandated systems. We suggest that further study and analysis of individual causes for such sanctions will provide information on additional actions that could be taken (e.g. - training/awareness of staff on appropriate completeness of documentation) to strengthen existing case review and quality assurance processes so as to minimize future penalties.

  - The County may wish to accelerate its evaluation of current staffing levels and "work flows" as they relate to these sanctionable items. Such an evaluation should ensure that staffing levels are consistent with organizational objectives and that staff are being properly utilized so as to obtain administrative cost-effectiveness. We recommend that the job assessment and job activity analysis currently being conducted receive priority attention from management.

  Comptroller's Office Response - The Comptroller's Office will initiate an effort to monitor the performance of the Department of Social Services.

  The effort will be designed to demonstrate whether or not the Department of Social Services is in compliance with state and federal government guidelines.

Department of Social Services Response - Approximately one-half of the reserve relates to a federal audit of Title IV-E foster care cases covering the period 1986-1988. While the audit was actually conducted in 1991-92, notification of the audit results was not provided until 1997. The Department has identified the cases involved, most of which are long since closed, and continues to prepare its case-specific challenges to the indicated disallowances. Because these cases are ten or more years old, specific corrective action on them is largely irrelevant. The Department has an ongoing quality assurance process and continues to sample its cases for corrective action purposes. The Department is confident that the issues resulting in legitimate disallowances in these old cases are appropriately addressed and properly documented in its current IV-E foster care cases.

The remainder of the sanction reserve relates to computer data entry which records the completion and timeliness of a variety of case actions into problematic and fragmented State computer systems. These disallowances, known as 153-d sanctions, result from State computer edits of data entered into the system which flags items as "overdue". There are multiple problems related to these system-generated fiscal sanctions. Items are flagged, for example, for failure to record actions no longer required due to changes in regulation. Items are also flagged because the system has no capability to record the action date; it only records the data entry date and assumes that it is the action date. The realities of casework are that system entry is often saved up and batched as time permits.

The root cause of these sanctions, however, has little to do with staffing levels and everything to do with the fact that local districts have been burdened by multiple layers of manual (paper documentation) and automated reporting requirements incrementally imposed upon them by Federal and State regulations over a period of many years. Unfortunately for local districts, little thought was given either to coordinating or to integrating the reporting requirements and systems so as to enable caseworkers to practice effective casework and keep up with the demands of complex, burdensome, duplicative, unsynchronized and fragmented reporting systems.

Erie County's difficulty in fulfilling all Child Welfare reporting requirements in "real time" is not unique; many other local districts in New York and other states have been equally challenged. The Federal government has recognized that overwhelming documentation requirements related to Child Welfare cases have burgeoned to a point where there is a nationwide inability to maintain currency with all reporting requirements and to also effectively perform the casework that is the subject of all the reporting.

In recognition of the need to streamline and connect mandated reporting systems, the Federal government initiated parallel efforts in two (2) areas, namely the Statewide Automated Child Welfare Information System (SACWIS) and the Adoption and Foster Care Analysis and Reporting System (AFCARS). A major goal of these efforts is to automate and integrate reporting systems and reduce the unreasonable burden placed upon casework staff which frustrate even the best efforts to maintain currency within the present environment of multiple, duplicative and fragmented reporting systems.

Unfortunately, the State's implementation of SACWIS, known as "Connections", has been highly problematic. It actually requires more caseworker time to support, and its lack of reliability in critical areas has meant that the County has had to reinstitute its own local system to compensate for the "Connections" deficiencies. This means that caseworkers have now become burdened by yet another inefficient system.

In spite of these problems, the Department has undertaken significant systems revisions to make SCTD sanction diskettes usable for corrective action and has dedicated a staff member to coordinate SCTD review and response. Corrective action is taken as a result of this process. The Department has also completed a review of operations and staffing in the Services Division with the twin goals of caseload reduction and sanction avoidance. The 1999 budget request addresses the most critical added staffing needs with a number of initiatives.

The Department has already taken and will continue to take steps to aggressively challenge both the Federal IV-E and State 153-d sanctions on a case-by-case basis, and expects to be successful in significantly reducing these potential disallowances in the fair hearing and/or appeal process.

- ***Accruals*** - During our testing of the accruals, it was noted that there was inadequate management review for certain complex year end accruals within the Department of Social Services. Upon discussion with client personnel and review of accrual balances, we noted that there were errors included in December 31, 1996 accruals. These errors were subsequently discovered and corrected by County personnel during 1997. This creates a mismatching of expense to the appropriate County fiscal year.

We recommend a more systematic management review of all significant social service accruals on an annual basis due to the complexity of many calculations and the dollar impact of the accruals.

Department of Social Services Response - Implementation by New York State of the Family and Children's Services Block Grant (FCSBG) in 1995 capped revenue on foster care payments, foster care and adoption administration, preventive services, child protective services and independent living. There had previously been separately identifiable revenues from these programs which were driven from the prescribed New York claim forms. Accounting for these programs has been extremely complicated because the State reimburses the County on the basis of a fixed, capped, monthly block grant allocation which is completely unrelated to the detailed claims the State requires the County to continue to submit. Further, the State no longer provides final settlement data related to these detailed claims so that disallowances for claims over the block grant ceiling can be translated into adjustments to accounts receivable.

In short, State claiming policy requires the County to submit claims which will never specifically be settled, and County accounting policy requires the Department to establish receivables, which will not specifically be realized, based on these claims. The capped FCSBG monthly payment that is received is not specifically claimed (there is no State claiming procedure to do so) nor recorded as a receivable, and it does not directly correspond to the claims and receivables which are. This results in an ongoing, significant and time-consuming reconciliation problem for the Department, and requires extremely complicated accounting/accrual procedures.

At the time of the 1997 year-end close, the Department had been accruing for three years of FCSBG program expenses, claims and revenues. It decided on the basis of its own reconciliation spreadsheets (there were no final settlements or reconciliations by New York State) to close out 1995 and 1996. In the course of doing so, an error in the 1996 year end accrual was discovered by the Department that was corrected in 1997.

The 1996 year end accrual error was undiscovered by management at year end 1996, and despite the fact that these particular accruals and associated receivables were also specifically examined by the County's independent auditors, KPMG Peat Marwick LLP, the calculation error was not detected.

The Department agrees that there should be more than routine management review of year end accruals with the most complex calculations and most significant dollar amounts. A more systematic review process will be instituted in 1998, consistent with the time available for review between the time accruals are prepared and the final year end close.

POTENTIAL COST SAVING OPPORTUNITIES

The following item requires additional research, but we feel it may have potential to provide cost savings to the County:

- ***Dental Coverage*** - we noted that the County provides dental benefits to County employees through the use of a private insurer. Since there are generally yearly maximums on these types of claims (which thereby limits the amount of risk assumed), this may be an opportunity to self-insure and potentially save money.

We recommend that the County perform an analysis of the claims paid from loss experience reports vs. premiums paid. This analysis performed over a period of time would provide a baseline estimate of potential savings.

Department of Personnel Response - We will be getting loss experience for the County GHI dental program and complete an analysis of the claims paid vs. premiums paid, as well as the additional cost of staff additions to administer the program and/or the hiring of a "Third Party Administrator" to handle the claims service.

REGIONALIZATION

The County has announced intentions to promote regionalization and cooperation among the various municipal entities within the County. Certain types of services could be consolidated with efficiency and cost savings realized. The County in some cases may be best suited (based upon experience, expertise and availability of personnel) to act as a central service point. Services that could be consolidated at the County level include:

- ***Workers' Compensation*** - The County and many of the other local governments within the County are self-insured for workers' compensation. The consolidation of claims paying processes and various other administrative functions may generate cost savings. Additional cost containment may be realized from:
  - the ability to put more effective claim review and challenge processes in place
  - the ability to establish countywide rehabilitation and back-to-work programs

  Division of Budget, Management and Finance Response - The County Attorney's office will look into the potential of expanding its self-insured Workers' Compensation program to include other municipal governments in Erie County.

- ***Investing of Idle Funds*** - The County is one of the few municipalities in Western New York that maintains a full time, professionally staffed cash management function. The appropriate management of cash is an important and time consuming function. Additionally, the pooling of available cash of all local governments in Erie County may provide investment purchasing power.

Comptroller's Office Response - Recent New York State legislation was enacted which allows municipalities to enhance their cash management and investment functions by forming investment cooperatives.

The Office of the County Comptroller coordinated a cash management training program for municipalities in Erie County in which the details of the new legislation was explained. We offered to facilitate the establishment of a regional cooperative investment program, an offer which is currently being evaluated by local governments.

OTHER MATTERS

Popular Reporting - The County publishes an extremely professional and voluminous comprehensive annual financial report. Unfortunately, the majority of residents do not understand current governmental reports. The Government Finance Officers Association has suggested that governments should consider enhancing the communication process by producing Popular Annual Financial Reports (PAFR). A PAFR may be utilized as a tool to better inform the County's residents concerning financial status and particular items of financial concern by being easier to understand than the comprehensive annual financial report. PAFR's also often include non-financial information designed to make these reports useful for public relations purposes. We suggest the County consider implementing Popular Reporting.

Comptroller's Office Response - We are considering the implementation of popular reporting.

We have recently written to 32 municipalities across the country requesting copies of their most recent popular reports. Our mailing list was derived from the Government Finance Officers Association (GFOA); our request was for the names of municipalities which have received awards from the GFOA for their Popular Report submissions.

YEAR 2000

The approach of the Year 2000 presents significant issues for many financial, information, and operational systems. It is estimated that the majority of the systems in use today are not able to appropriately interpret dates after December 31, 1999, because such systems allow only two digits to indicate the year in a date. For example, such systems are unable to distinguish January 1, 2000, from January 1, 1900. This shortcoming is very common and can have pervasive and adverse consequences on the operations of the entity and the integrity of information processing. Financial and operating data may be affected and the effects of inaccurate dates may not be obvious.

We made limited inquiries about the possible impact of the Year 2000 on the County's operations and information systems at various times between April 29th and June 18th. Outlined below are our limited inquiries and management's responses.

a. Has a written high-level plan that outlines the County's procedures for the Year 2000 issue been developed? Has the plan been reviewed by senior management? Was a copy (or appropriate summary) provided to the audit committee? Does the plan include an estimate of the total costs of the Year 2000 project? When was the last time that estimate was updated?

   Division of Information and Support Services Response - There currently is a high level Year 2000 plan for the Data Processing Department to address all critical taxpayer services. The department heads are responsible for their respective areas to ensure Year 2000 compliance. These department heads are responsible for reporting status to the County Executive or his designee. The Data Processing Department does gather summary data on the software compliance status of the various departments for reporting to Senior Management. The County has been working on this initiative for the past 5 years.

b. Has the County identified and scheduled a sufficient number of personnel and processing resources to address the Year 2000 issue and to accomplish all of the objectives set forth in the County's Year 2000 plan? Does the plan describe the resources that are needed? Have the costs of these resources been included in the County's budgets?

   Division of Information and Support Services Response - The County Executive and Legislative branches have allocated funding for the plan. The Data Processing Department is coordinating the effort on behalf of the County Executive. Additionally, the department heads are responsible for their respective areas to ensure Year 2000 compliance.

c. Does the plan include a timetable of expected completion dates for various phases of the project (i.e., key milestones)? Are the County's Year 2000 activities on schedule?

   Division of Information and Support Services Response - Data Processing personnel believe that their plans are on schedule.

d. Does the plan include a process for preparing (or updating) a comprehensive inventory of financial, informational, and operational systems? Has this inventory been completed? If not, when will it be completed?

   Division of Information and Support Services Response - A comprehensive inventory of financial, informational, and operational systems critical to taxpayer services has been completed.

e. When will all of the systems that are critical to the operations of the County be identified? Has this date been included within the written plan?

Division of Information and Support Services Response - The Data Processing unit has identified critical software systems and either has or is in the process of making them compliant. The Data Processing unit believes sufficient time and resources have been spent identifying non-data processing systems that could effect critical taxpayer services.

f. What is the County's plan for fixing critical systems that are negatively impacted by the Year 2000 (e.g., code renovation, replacement, upgrade, development of "work-arounds")? Has this been documented in the Year 2000 plan?

Division of Information and Support Services Response - Critical systems will be repaired through a combination of code renovation, third party vendor software upgrade or software replacement.

g. When do you expect all critical systems to be Year 2000 compliant? Has this date been documented in the plan? What percentage of the County's critical systems is now Year 2000 compliant? Are there critical or noncritical systems that may not be completed by the required completion date? For every critical system with Year 2000 problems, is there a detailed project plan for resolving the problems or for replacing the system; have required personnel and processing resources been estimated; and have experienced project managers and technical staff been assigned? For every critical system with Year 2000 problems, is there a detailed schedule for problem resolution or system replacement; does the schedule include the required and expected completion dates, measurable milestones, and expected performance metrics; and does project progress, as measured by achieved milestones and actual metrics, suggest that the project will be completed on time?

Division of Information and Support Services Response - The County expects that all critical systems will be compliant by the Year 2000.

h. What procedures are in place to determine that the systems of your key vendors, service providers, customers, and unconsolidated subsidiaries and joint ventures in which you have a material investment are Year 2000 compliant? Are these procedures documented in the plan? What percentage of your key vendors, service providers, customers, and unconsolidated subsidiaries and joint ventures has been subject to these procedures? What were the results of those procedures? When will these procedures be completed for all of your key vendors, service providers, customers, and unconsolidated subsidiaries and joint ventures in which you have a material investment? Has this completion date been documented in the plan?

Division of Information and Support Services Response - The Data Processing unit believes sufficient time and resources have been spent ensuring that the systems of key vendors, service providers, the Hospital and Nursing Home are or are in process of becoming Year 2000 compliant.

i. What procedures are in place to mitigate the County's risk of litigation and noncompliance with government regulations as a result of Year 2000 operating problems or product/service failures? Have these procedures been documented in the plan? Has the County's general counsel reviewed the plan?

Division of Information and Support Services Response - The County believes it has been and continues to mitigate the risk of litigation and noncompliance through the Year 2000 activities discussed above, including documentation of Year 2000 remedial work, appropriations for Year 2000 corrections, contacts with third party suppliers and management commitment to addressing the Year 2000 problem.

j. What contingency plans are in place, or planned, if systems fail to function properly? Have these plans been tested or challenged for feasibility? Are there critical and unique high-volume systems for which a contingency plan may not be possible?

Division of Information and Support Services Response - There is currently no contingency plan in place.

k. Who has oversight responsibility for this Year 2000 project? How do they fulfill this responsibility (e.g., interim status reports, exception reports that identify departures from schedules early enough for corrective action)? Who verifies the accuracy of the reporting to this oversight body (individual)?

Division of Information and Support Services Response - The Director of the Data Processing Department has oversight responsibility for the data processing aspects of the Year 2000 issue. Summary reports as to status are prepared. The Deputy County Executive is responsible for non-data processing issues.

l. Are senior management and the audit committee kept up to date on your Year 2000 activities and the results of those activities? When was the last communication to senior management? When was the last communication to the audit committee?

Division of Information and Support Services Response - While the Director of the Data Processing Department has regular access to the County Executive, there is no formal documentation supporting regular update meetings.

m. Has the Year 2000 impacted current or prior-year operations? Has the Year 2000 impacted current or prior-year management or financial reporting?

Division of Information and Support Services Response - One instance has occurred with the system that tracks protection orders. The system was found not to accept dates past the Year 2000 when an order of protection with a three year life (up to the year 2001) was attempted to be processed. The software has subsequently been fixed.

n. What Year 2000 issues cause you the most concern?

Division of Information and Support Services Response - Final conversion of the CPS Event tracking system, and New York State's ability to be Year 2000 compliant in a timely manner.

Although such inquiries are not required by generally accepted auditing standards, we have made such inquiries because we believe that senior management and the audit committee should recognize the potential seriousness of the Year 2000 issue. We have not performed any procedures, however, to test the accuracy and completeness of the responses we received to our inquiries described above. Accordingly, we have no findings and express no opinion as to the sufficiency of the County's assessment of the potential impact of the Year 2000 issue or its plan, or the status of the County's planned actions.