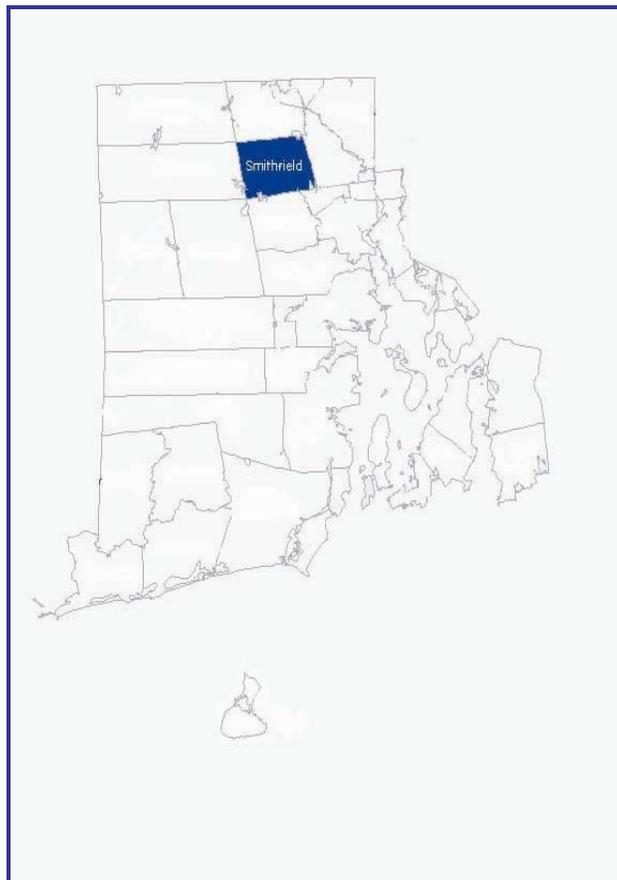


Town of Smithfield
Fiscal 2007 Performance Review
November 2007



Ernest A. Almonte, CPA, CFE
Auditor General

Office of the Auditor General
General Assembly
State of Rhode Island

November 6, 2007

Honorable Members of the Smithfield Town Council

Dennis G. Finlay, Acting Smithfield Town Manager

We have completed a limited performance review of the Town of Smithfield which is a natural extension of our oversight responsibilities with respect to Rhode Island municipalities.

Our report is included herein as outlined in the Table of Contents and includes recommendations to enhance the financial operations of the Town and address other financial related issues impacting the Town that we observed during our review.

Sincerely,

A handwritten signature in black ink that reads "Ernest A. Almonte". The signature is written in a cursive style with a large initial "E".

Ernest A. Almonte, CPA, CFE
Auditor General

Town of Smithfield

Fiscal 2007 Performance Review - Table of Contents

	<u>Page</u>
Executive Summary	1
Objectives	3
Observations and Recommendations	4
Pension Plans and Other Post-employment Benefits	4
Funded Status of Town's Pension Plans	
Police Pension Plan Benefit Calculation	
Elderly Property Tax Relief Program	6
Monitoring of Elderly Tax Exemption Program Eligibility	
Clarification of Terms of Eligibility for Elderly Tax Freeze or Exemption Program	
Reevaluate the Affordability and Existing Eligibility Criteria for the Tax Freeze Program	
Fire Department Overtime Expenditures	10
Staffing	
Cost Benefit Analysis – Consideration of Additional Hires	
Fire Department Contract	13
Contracts	14
Procurement	15
Payroll Processing	16
Renegotiation of Payroll Processing Agreements	
Combining Payroll Functions	
Frequency of Payroll Processing	
Duplicate Payroll Records and Accounts	
Second Town Payroll Account	
Payroll Software Implementation	
School Custodian Detail Assignments	
General Payroll Controls	
Consultant Agreements	21
Healthcare Benefits Administration	23
Healthcare Benefits Waiver	
Eligibility for Health Insurance	
Audit Committee	25
Performance Audit of the School Department	26
Ice Rink	26
Bank Accounts	
Cash Receipts	
Contracts	
Privatization of Snack Bar Concession Services	
Fee for Ice Time	

Town of Smithfield – Fiscal 2007 Performance Review

Executive Summary

We performed a limited performance review of the Town of Smithfield which focused on issues identified by the Town Council and Town Administration that they believed warranted our review. Our objective was to offer constructive recommendations to enhance the efficiency and effectiveness of the Town's financial operations. We did not perform an audit of the Town.

Some of our recommendations require that the Town look at certain common functions like payroll processing, procurement and healthcare benefits administration comprehensively rather than from an individual department perspective. Others involve reevaluating fiscal practices in light of the increasing fiscal pressure facing all Rhode Island municipalities. Finally, some issues, such as pensions, have been long-standing and now require immediate resolution.

The Town's independent auditors have previously commented on the funded status of the Town's self administered pension plans. Additionally, our report issued in July 2007 entitled *Status of Pension Plans Administered by Rhode Island Municipalities* identified these plans as high risk. The Town needs to make progress in implementing specific recommendations to address the pension plan funding issues. In the future, "fiscal notes" should be prepared to demonstrate consideration of the current and long-term aspects of collective bargaining contract provisions.

The Town offers two elderly tax relief programs to property owners--a tax freeze and a tax exemption which are overlapping since most taxpayers benefiting from the freeze also receive the exemption. The Town can improve its monitoring of the tax freeze program by requiring periodic recertification of eligibility requirements (e.g., ownership and residency) and clarifying occupancy requirements included in the ordinance. Further, due to increasing legal restrictions on a municipality's ability to increase property taxes, the Town could explore options similar to those adopted by other communities which attempt to balance the fiscal needs of the Town with the goal of providing elderly tax relief.

The Fire Department should prepare a cost benefit analysis to guide its decision-making regarding the optimal number of employees needed to cover operations yet minimize the amount of overtime costs incurred. Additionally, the Fire Department budgets and accounts for various overtime costs by the underlying cause of the overtime (e.g., firefighters on sick or vacation leave). The Town can enhance its budgeting and reporting of these costs by identifying such costs as overtime expenditures.

We noted instances where the language included in various labor contracts and other Town contracts could be made clearer to avoid ambiguity and multiple interpretations.

The Town should hire an experienced purchasing agent to oversee and centralize the Town's procurement activities. Controls can be strengthened to ensure compliance with purchasing requirements contained in the town charter and ordinances.

Various cost savings and processing efficiencies can be achieved through centralizing payroll functions within the Town and School Department. The Town and Schools separately utilize the same

Town of Smithfield – Fiscal 2007 Performance Review

Executive Summary

vendor for payroll processing but have not consolidated these services under one contract or sought competitive bids. The Town pays its employees on a weekly schedule while the Schools follow a biweekly schedule. Savings can be achieved by adopting a biweekly payroll schedule for all employees. Further, the Town can improve certain payroll processing controls by better segregating key payroll functions and duties.

The Town should adopt a written policy regarding rehiring retired Town employees. The status of two retired employees who were rehired was unclear due to a succession of consultant agreements executed between the Town and the two employees, and their treatment as employees in many respects. The employment agreements covering these two individuals need to be redrafted and the remaining issue regarding their eligibility for participation in the State Municipal Employees' Retirement System needs to be resolved.

There are opportunities for the Town to streamline the healthcare insurance options offered to its employees and provide a uniform payment for those waiving healthcare insurance. The Town should also seek bids for healthcare insurance as one collective plan for all Town employees and investigate self insurance options. Further, the Town should assess its healthcare waiver program periodically to ensure that it remains a true cost avoidance mechanism and represents a net cost savings to the Town. Employee healthcare beneficiary information should also be reconfirmed on an annual basis.

We also recommend that the Town Council form an audit committee to oversee the Town's annual audit process and seek proposals for a qualified firm to conduct a performance audit of the School Department. School operations represent more than 50% of the Town's overall financial operations.

The Town can improve various administrative aspects of its ice rink operations including timeliness of deposit of cash receipts, control over bank accounts, and execution of contracts with vendors. In the future, the Town could improve cost benefit analyses that are prepared to support decisions regarding privatizing operations. The Town could consider increasing the fee it charges for use of the ice rink to be competitive with other area rinks.

Overall, the report contains 46 recommendations intended to enhance the Town's ability to provide services in the most effective and efficient manner.

OBJECTIVES

At the request of the Town Council, as approved at its May 15, 2007 meeting, we conducted a limited performance review of the Town of Smithfield.

The scope of our performance review was less comprehensive than a performance audit conducted in accordance with *Government Auditing Standards*. Officials of the Town Council and Town Administration identified issues that they believed warranted our review. We limited our review to these issues. We did not perform an audit of the Town and we have not performed independent tests of the data provided to us by the Town which became the basis for our analysis.

Our objective was to offer recommendations to enhance the efficiency and effectiveness of the Town's financial operations.

OBSERVATIONS AND RECOMMENDATIONS

PENSION PLANS AND OTHER POST EMPLOYMENT BENEFITS

Funded Status of Town's Pension Plans

The Town of Smithfield has a private insurer administer two of its defined benefit pension plans for police department employees hired prior to July 1, 1999 and most fire department employees. The Town's most recent audit report for the fiscal year ended June 30, 2006 indicates that both of these plans were underfunded and one was not contributing 100% of its actuarially determined annual required contribution (ARC). The details are as follows:

Smithfield Police Prior to July 1, 1999

- Unfunded Actuarial Accrued Liability: \$12,529,685
- Funded Ratio: 36%
- Percentage of ARC made in fiscal 2006: 153%

Smithfield Fire Department Employees

- Unfunded Actuarial Accrued Liability: \$1,989,143
- Funded Ratio: 86%
- Percentage of ARC made in fiscal 2006: 72%

Both of these plans were considered at risk in our report issued in July 2007 entitled *Status of Pension plans Administered by Rhode Island Municipalities*. In addition, the Town's independent auditors presented issues related to these plans as the most significant findings in their Letter of Observations and Recommendations for the fiscal year ended June 30, 2006. For the police plan the auditors state:

"It is imperative that all parties involved realize the severity of the problems with this plan. Continued lack of resolution to this problem will cause the plan's financial condition to continue to deteriorate, ultimately resulting in the collapse of this plan within a few years."

For the fire plan the auditors state:

"We are concerned that, unless the Town Council reviews this plan and decides on long-term solutions now, the Fire pension plan will face the same crisis that the Police pension plan is currently facing. We recommend that the Council request the Fire Pension Committee to meet with the actuary to review in depth the current status of the plan, and long term solutions to maintaining the plan's solvency."

The auditors also made a recommendation to the Town regarding Other Post Employment Benefits (e.g., retiree health care) and advised that it should obtain an actuarial study of the present value of the costs of providing post employment benefits. The auditors recommend that once the liability is determined the Town must establish a plan to fund the liability.

The Rhode Island General Law section 45-10-6.1 requires a municipality to prepare a detailed corrective action plan and timetable to address all findings and recommendations resulting from the annual audit. Additionally, when a municipality is making less than 100% of the annual required contribution to a pension plan, General Law section 45-10-15 requires a corrective action plan to address the underfunding of the pension plan.

RECOMMENDATION

1. Implement all recommendations made by the auditors with specific emphasis on the findings regarding pension plans and other post employment benefits due to the significant financial impact these can have on the fiscal stability of the Town.

Police Pension Plan Benefit Calculation

Thirty-five retired Smithfield Police Officers are covered under a group annuity contract between a private insurer and the Town which provides covered police officers and fire fighters with a retirement annuity (pension). This plan, in effect since July 1, 1975, is now a closed plan (with respect to police officers). All remaining active police officers were transferred to the Municipal Employees' Retirement System (MERS) of Rhode Island effective July 1, 2006; as such, no new pension benefits are being calculated under the police officers' closed plan.

The Town was responsible for the calculation of retirees' monthly benefit under the closed police plan. The calculation for the retirees' monthly retirement benefit, per the contract, is based on a percentage of the average annual compensation received in the thirty-six consecutive months in which he received his highest compensation multiplied by the number of years and months of service, subject to a few other specifications. We learned that the Town had been including the payout of accumulated sick and vacation time in the compensation amount used to calculate the pension benefit for the retiree. We believe this methodology used for calculating the retirement benefit for employees hired prior to December 1, 1987 is not clearly supported by the language in the original contract. In 1988, the plan contract was amended to expressly exclude sick leave and accumulated vacation pay from the definition of "compensation" as used in the contract. Article I. Definition 19 of the original contract defines compensation as "compensation for services rendered including overtime and longevity pay". Accumulated sick pay and vacation pay are not expressly included. However, the intent of the original agreement cannot be definitively ascertained.

The inclusion of these termination benefits in the compensation figure used to calculate a retiree's monthly pension entitlement increased the monthly benefit payment substantially. We reviewed the retirement pension calculation for one retiree, a police officer who was hired prior to the 1988 amendment and retired in 2001. This retiree's payout for sick leave alone exceeded \$33,000, and the total payout of all accumulated vacation, sick and compensatory time was \$50,380. Inclusion of this compensation in the pension calculation increased his monthly pension benefit from \$3,125 to \$3,831 per month, an increase of \$706. Extended over the estimated lifetime of a typical retiree, the cost to the Town could range from \$200,000 to \$300,000.

We did not attempt to determine the amount of termination benefits included in each pension calculation nor estimate the cost to the Town for all retired police officers, hired prior to December 1, 1987. However, if other similar instances occurred, the added cost to the Town resulting from this interpretation of the contract could be substantial.

Arguably, the increased monthly pension payments that resulted from the Town's inclusion of payments for accumulated sick, vacation and compensatory time in the base pension computation may have contributed to the large unfunded pension liability that has been a significant concern to the Town and continues to impact the Town's current pension costs. While the Town clarified the specific contract language many years ago and the opportunity to address the individual pension benefits has likely passed, we believe this is a good example of the need to appropriately anticipate the long-term impact of current decisions and related contract provisions. In the future, preparing a fiscal note or other means to demonstrate consideration of the current and long-term aspects of contract provisions is appropriate.

RECOMMENDATION

2. Prepare a fiscal note detailing the impact on contribution rates and funded status of a locally administered pension plan when pension benefits are affected by new collective bargaining agreements. The fiscal note should provide the governing body approving the contract with sufficient information to ascertain the full cost of the proposed collective bargaining agreement.

ELDERLY PROPERTY TAX RELIEF PROGRAM

The Town of Smithfield provides property tax relief to property owners who are over 65 years of age under the property tax freeze ordinance and the property tax exemption ordinance, or both.

The property tax freeze ordinance provides that:

"The Tax Assessor may exempt from taxation and may provide for the freezing of the rate and valuation of taxes on real property situated in the Town which is owned and occupied by any one or more persons over the age of 65 years, regardless of income. Said real estate is not to be taken from the tax rolls and shall be subject to the bonded indebtedness of the Town." (Smithfield Code of Ordinances - sections 321-2(a) and (b))

The following restrictions apply:

- The tax freeze on real property shall apply only to single-family dwellings.
- The property must be owned by the taxpayer.
- The property must be occupied by the taxpayer.

The tax exemption ordinance provides that:

"The tax exemption shall be in an amount not exceeding \$4,000 of valuation and which exemption shall be prorated among the owners of said real property in addition to any and all other exemptions, including the tax freeze to which said person may be otherwise entitled." (Smithfield Code of Ordinances - section 321-2(c))

The following restrictions apply:

- The tax exemption on real property shall apply only to residential dwellings of fewer than four dwelling units.
- The property must be owned by the taxpayer.
- The property must be occupied by the taxpayer.

The ordinance further provides that both the exemption and application of the tax freeze shall be applied uniformly and without regard to ability to pay, and shall be granted upon proof of the following by the taxpayer:

- Age over 65;
- ownership of property for a period of five years prior to the filing of an application for tax exemption and/or tax freeze; (the ordinance was amended effective July 2005 requiring ownership for a period of ten years in order to qualify for the tax freeze.)
- occupancy of same; and
- legal domicile in Town of Smithfield.

The Town asked that we review their elderly tax relief program as they consider changes to program provisions and its administration.

Monitoring of Elderly Tax Exemption Program Eligibility

The Town requires that applicants provide certain documentation to demonstrate their right to the exemption or freeze. However, once determined eligible they are not required to periodically certify their continued eligibility.

The current Tax Assessor, in an effort to determine continued eligibility of existing taxpayers receiving relief under these ordinances, sent out a "Confirmation of Senior Citizen Exemption" to taxpayers in the early part of 2004. The Town used the confirmation responses to determine if the taxpayers continued to be eligible for tax relief.

We reviewed some of the taxpayer responses received from the 2004 confirmation effort. The form required that the person signing it certify that he or she resides full time at the Smithfield property granted the property tax exemption. We found some instances where the confirmation response indicated that the owner of the property was someone other than the senior citizen eligible for the exemption or freeze. The individual may have been a family member and the senior citizen in this case was said to have a life estate in the property. The owner reported a date of birth that was inconsistent with eligibility for the

elderly tax exemption. This individual attested to the fact that he or she lived in the home but there was no indication that the individual with the life estate was in fact still living in the home.

Additionally, we reviewed records of Smithfield taxpayers currently receiving the elderly tax freeze and noted that several taxpayers had mailing addresses outside of Smithfield or outside of Rhode Island. Upon our inquiry regarding one taxpayer, the Town determined that the individual was ineligible for the elderly tax freeze in Smithfield and notified him accordingly.

In order to ensure that only eligible property owners receive the elderly tax freeze or elderly tax exemption, the Town should require an annual recertification of eligibility to be completed by the elderly property owner.

RECOMMENDATIONS

3. Review mailing addresses for taxpayers receiving the tax freeze periodically. Investigate taxpayers designating out-of-town mailing addresses to determine whether they meet the occupancy requirement.
4. Require all individuals receiving the elderly tax exemption or tax freeze to recertify annually as to their continued eligibility.
5. Explore other options to confirm the residency of taxpayers receiving the tax freeze or exemption including data sharing with the Rhode Island Division of Taxation.
6. Redesign the recertification form to require senior citizens holding a life estate in the property to provide their date of birth and signature confirming that they are currently occupying the home.

Clarification of Terms of Eligibility for Elderly Tax Freeze or Exemption Program

The ordinance provides that a taxpayer must occupy the home in order to be eligible for the freeze or exemption. However, it does not define occupancy in terms of the number of months per year that an individual must reside in the home in order to meet the requirement.

RECOMMENDATION

7. Define the length of time during a year that the home must be occupied by a taxpayer in order to qualify for the tax freeze.

Reevaluate the Affordability and Existing Eligibility Criteria for the Tax Freeze Program

According to the Smithfield Tax Assessor, there are currently 1,177 residents who are afforded a tax freeze resulting in "lost" revenue of approximately \$1.5 million. The total fiscal 2008 tax levy was \$41.9 million (of which \$34.3 million was for real property). Most taxpayers receiving the tax freeze also receive the tax exemption. The Tax Assessor estimates that the senior citizen exemption impacts the Town of Smithfield by approximately \$225,000 with less than \$1,000 of this applicable to those who receive the exemption only.

Due to increasing legal restrictions on a municipality's ability to increase property taxes, Town officials have expressed interest in restructuring the elderly tax exemption to continue to provide equitable tax relief to senior citizens and maintain the fiscal stability of the Town.

We reviewed a report issued by the State Office of Municipal Affairs-Department of Administration on November 15, 2006 entitled Report on Municipal Tax Exemptions and Tax Treaties. They reported that, at that point in time:

- Nine (9) communities in Rhode Island actively offered an elderly tax freeze.
 - Five (5) of these had no income restriction as to eligibility.
 - Four (4) had income restrictions as to eligibility.
- Twelve communities offered tax deferrals with three offering both a freeze and deferral.
- Each of these municipalities had its own unique requirements for tax freezes and or tax deferral.

The Report on Municipal Tax Exemptions and Tax Treaties includes a recommendation to eliminate all tax freezes as a way to improve the statewide equity of the present property tax system in the State of RI.

The neighboring Town of North Smithfield was not included in the report cited above since it just recently adopted an elderly tax freeze based on legislation passed during the 2006 session of the General Assembly. North Smithfield has adopted a tax freeze, which in effect is a tax deferral since the amount of tax revenue that would be lost on the property due to the freeze is deferred so that it can be collected by the Town upon termination of the conditions that make the property subject to the senior tax freeze. North Smithfield also has an income requirement linked to the tax freeze and requires annual recertification of eligibility. These measures attempt to balance the fiscal needs of a municipality with the goal of providing elderly tax relief.

The Town could consider options to revise eligibility criteria as it deems appropriate. The affordability of each option in terms of lost revenue should also be considered. These options include:

- defer property taxes until termination of the conditions that make the property subject to an elderly tax freeze;
- implement an income requirement as part of the eligibility criteria;
- restrict participation in the elderly tax exemption to those not eligible for the elderly tax freeze;
- eliminate the tax freeze as recommended by the State Office of Municipal Affairs; and
- consider alternate elderly tax relief methods such as a flat tax credit, flat property tax exemptions, exemption as a percentage of assessed value, or exemption as a percentage of property tax.

RECOMMENDATION

8. Continue to review options to revise eligibility criteria for the elderly tax freeze while providing equitable tax relief to senior citizens.

FIRE DEPARTMENT OVERTIME EXPENDITURES

We reviewed overtime expenditures in order to obtain an understanding of how overtime is incurred, whether it is calculated in accordance with applicable contract requirements and whether management has reasonable controls to ensure that overtime is:

- paid only when necessary to ensure the health and safety of both the community and firefighters; and
- a more prudent and economical use of taxpayer dollars than hiring additional personnel.

The Town budgets and accounts for Fire Department overtime expenditures in three accounts: *Overtime*, *Sick leave* and *Annual leave*. Most of the expenditures in all three accounts represent overtime (wages compensated at other than straight time - generally time and one-half). However, the Town segregates the expenditures by underlying cause (e.g., the sick leave category is used for a firefighter earning overtime to cover for another firefighter who called in sick). The following table shows how overtime expenditure information is reported in the Town's accounting system.

Fire Department – Fiscal 2007 Overtime and Vacation Days Cashed-In (Unaudited)				
Account Description	Budget	Actual Expenditures	Amount (Over) Under Budget	Percent (Over) Under Budget
Overtime	\$ 175,000	\$ 94,375	\$ 80,625	46.0%
Sick Leave	275,000	420,474	(145,474)	(52.9%)
Annual Leave	<u>250,000</u>	<u>227,876</u>	<u>22,124</u>	8.8%
Total	\$ <u>700,000</u>	\$ <u>742,725</u>	<u>(\$ 42,725)</u>	(6.1%)
Source: Town accounting system and Fire Department				

Fiscal 2007 expenditures in these three accounts totaled \$742,725 of which \$695,339 was overtime and \$47,386 represented accrued unused vacation days cashed in by employees in lieu of taking a vacation day (included in the *Annual leave* account). The latter amount is not overtime and should be segregated from true overtime costs.

We were initially advised that fiscal 2007 overtime expenditures totaled \$94,375 which is the total in just the account entitled *Overtime*. Upon further inquiry we learned that overtime expenditures actually

totalled \$695,339 because additional overtime expenditures were also recorded in the *Sick Leave* and *Annual Leave* accounts.

The Fire Department maintains other detail of its overtime expenditures by underlying cause as summarized in the table below:

<u>Fiscal 2007 Overtime Expenditures by Underlying Cause</u>	
Reason for Overtime Expenditure	Expenditures
Paid to employees for unused compensatory time	\$ 276,558
Paid to employees who work when others discharge vacation	178,130
Paid to employees who work when others discharge other types of leave (such as sick, personal, bereavement, jury duty)	141,716
Paid to employees who are held to work beyond their normal shift	50,909
Paid to employees who are called in to work additional hours	41,621
Total per Fire Department Analysis	\$ 688,934
Expenditures not classified	6,405
Total	<u>\$ 695,339</u>
Source: Fire Department	

The largest overtime payments are for cashing in unused compensatory time. The fire department contract (Article IV, Section 2) provides that a fire department employee who earns overtime may elect to be compensated with overtime pay or compensatory time off. Either option is compensated at the rate of time and one half. Unused compensatory time may be cashed in. Compensatory time that is not discharged as time-off or cashed in by the end of the fiscal year (June 30) is lost.

While tracking overtime expenditures in this manner (by underlying cause) may be meaningful to the administration of the fire department, transparency could be enhanced by budgeting and reporting all these expenditures as overtime costs. Consistent and appropriate "labeling" of these expenditures allows better comparison to other Town departments and better isolates overtime expenditures for analysis of optimal staffing levels (to minimize overtime costs)

RECOMMENDATION

9. Clarify and enhance reporting of Fire Department overtime costs and payments for cashing in unused vacation time to clearly identify budgeted and actual expenditures and variances between such amounts. Record budgeted and actual payments for cashing in unused vacation days in a separate budget account.

Staffing

The Fire Department has 54 employees -- 48 uniformed firefighters and 6 civilian staff. Ten administrative staff are located at headquarters and four platoons of 11 staff the Town's three stations around the clock as shown in the following table.

<u>Number of Firefighters by Fire Station</u>				
<u>Platoon</u>	Station 1 Headquarters - Putnam Pike (Note 1)	Station 2 Farnum Pike (Note 2)	Station 3 Log Road (Note 3)	<u>Total</u>
A	6	3	2	11
B	6	3	2	11
C	6	3	2	11
D	6	3	2	11
Total				<u>44</u>
<u>Notes:</u> 1 = 1 civilian dispatcher and 5 firefighters (3 on engine, 2 on rescue) 2 = Engine only, 3 fire fighters 3 = Rescue only, 2 firefighters Source: Fire Department				

When responding to fires, these four platoons are assisted by 8 uniformed firefighters who comprise the administrative staff (chief, deputy chief, etc.). In addition, a group of "Paid on Call" firefighters who are trained volunteer firefighters (not Fire Department employees) may respond to emergencies as requested and are compensated for their assistance.

The four platoons comprising 40 firefighters and 4 dispatchers follow an 8 day work schedule which consists of two consecutive 10 hour days followed by two consecutive 14 hour nights, followed by 4 consecutive days off. The head of the Rhode Island Association of Fire Chiefs advised us that this is a standard schedule used by nearly all fire departments in the State.

Except for one vacant position held for a firefighter on military leave, there were no vacancies during fiscal 2007. The Chief advised us that the department's policy of maintaining minimum staffing (for example per fire apparatus) is in accordance with acceptable safety standards as well as in compliance with the union contract.

Fiscal 2007 Fire Department overtime expenditures totaling \$695,339 represent an average overtime expenditure of \$13,372 for each of the 52 employees who received overtime pay. Of the 52 employees, twenty-seven received more than the average of \$13,372 and twenty-five received less than the average. Overtime expenditures per employee ranged from a high of \$26,658 to a low of \$328. Total compensation (with overtime) ranged from \$91,067 to \$33,403. The Fire Department has a written policy ("equalization policy") governing the assignment of overtime to department personnel to ensure that overtime is distributed to all employees on a fair basis.

Cost Benefit Analysis - Consideration of Additional Hires

The Fire Department's current complement of personnel is just sufficient to meet what it has determined to be its "minimum manning" requirement. Consequently, any leave time (e.g., sick, vacation, military, etc.) used by firefighters or dispatchers requires overtime to maintain a consistent minimum staffing level. Some overtime is expected in 24/7 type operations and up to a certain point, even with

compensation of the overtime hours at time and one-half, can be cost effective due to the incremental benefit costs associated with new hires. Accurately determining the break-even point where hiring additional personnel is more cost effective than incurring overtime costs, is key.

We compared the Smithfield Fire department to two other Rhode Island fire departments which had similar characteristics, such as population size and density, geographic size (square miles) and type of fire resources (full-time fire department). The purpose of the comparison was to determine how similar fire departments handled overtime and how their overtime costs compared to Smithfield's.

Comparison of Overtime Costs for the Smithfield Fire Department to Other Similar Fire Departments					
Fire Department	Employees	Total Personnel Costs – Wages	Overtime Costs	Overtime Costs as a % of Total Personnel Costs – Wages	Additional firefighters scheduled per shift to cover vacancies
Smithfield	54*	\$3,371,243	\$ 695,339	21%	None
North Kingstown	72	\$3,907,256	\$ 731,545	19%	4 per shift
Johnston	92 *	\$6,345,491	\$1,601,260	25%	None
*Smithfield had one vacancy due to military leave and Johnston had 12 vacancies Source: Towns of Smithfield, North Kingstown and Johnston					

North Kingstown routinely schedules 4 additional firefighters per shift so that when a vacancy occurs, one of the four covers the vacancy at regular straight-time wages rather than overtime.

The Smithfield Fire Department has not prepared a cost benefit analysis to determine the point at which hiring additional firefighters may become cost effective. Having regularly scheduled "floaters" to fill vacancies (due to vacation and leave) and to maintain staffing levels at required levels with minimum manning requirements at a straight time rate (rather than overtime pay) may be useful and cost effective. The analysis must appropriately consider which employee benefit costs are fixed (e.g., healthcare) and which are variable (e.g., employer share of FICA) in relation to total wages.

RECOMMENDATION

10. Prepare a formal cost benefit analysis comparing the cost effectiveness of using overtime or additional hires to meet minimum manning requirements. Utilize the analysis to guide budgetary and hiring decisions.

FIRE DEPARTMENT CONTRACT

The Fire fighters contract (Article IV, Section 2: Overtime) provides that a fire department employee who earns overtime may elect to be compensated with overtime pay or compensatory time off in lieu of overtime pay. Either option is compensated at the rate of time and one half. Unused compensatory time may be cashed in. Compensatory time that is not discharged as time-off or cashed in by the end of the

fiscal year (June 30) is lost. During fiscal 2007, expenditures for compensatory time *cashed in* by fire department employees totaled \$276,558.

The following contract language lends itself to multiple interpretations:

“Employees shall have the option of receiving compensatory time off in lieu of overtime pay. Such compensatory time may be taken whenever a qualified fill can be obtained. Compensatory time shall be charged at a minimum of four (4) hours unless such time is approved by the Chief of the Department. It is expressly understood that this provision of compensatory time is granted with the express understanding and agreement that its costs to the Town shall not exceed Six Thousand (\$6,000) Dollars in a fiscal year. Should this provision result in expense to the Town in excess of Six Thousand (\$6,000) Dollars in a fiscal year, the option of receiving compensatory time off in lieu of overtime shall be promptly discontinued by the Town until the commencement of the next fiscal year. All compensatory time accumulated shall be eliminated and paid on June 30 of each year.” {Article IV, Section 2: Overtime (c)}

This language is not clear regarding whether the \$6,000 limitation is per person or an aggregate total for all employees. Accordingly, this language could possibly be interpreted to mean that the cost of all compensatory time for the year is limited to \$6,000 in the aggregate for all employees. Conversely, it could be interpreted to be an annual limit of \$6,000 for each employee.

Fire Department management advised us that this language only applies to instances where an employee has chosen to receive compensatory time off (leave) in lieu of overtime pay and then *discharges such compensatory time off*. The expenditure that is limited to \$6,000 per fiscal year is the overtime paid to the individual who fills in for the person discharging compensatory time off. Such overtime expenditures are limited to not more than \$6,000 for all employees for the fiscal year. Management does not separately track instances of overtime expenditures *incurred when an employee discharges compensatory time off* in order to distinguish it from other overtime expenditures. Accordingly, the Fire Department cannot determine whether it is in compliance with the contract requirement (as interpreted by the Fire Department) that limits such expenditures to not more than \$6,000 annually.

RECOMMENDATIONS

11. Clarify contract language in future firefighter contracts concerning the \$6,000 limitation in Article IV, Section 2: Overtime (c).
12. Monitor compliance with the \$6,000 annual expenditure limitation in Article IV, Section 2: Overtime (c) of the current Fire contract: Track overtime expenditures incurred when an employee works in place of another person who is discharging compensatory time off (leave) to ensure that total expenditures for this classification of overtime do not exceed \$6,000 in a fiscal year.

CONTRACTS

Employees of the Town of Smithfield are covered under five (5) collective bargaining agreements and school employees are covered under three (3) collective bargaining agreements. The Town has also entered into numerous other written contracts with employees, vendors, pension providers, etc. We referred to these contracts in making determinations and recommendations regarding policies and

practices in the Town. In some instances we found the contract language to be ambiguous, contradictory, or subject to multiple interpretations. We noted this issue in the firefighter's contract (see preceding section entitled *Fire Department Contract*, the police pension plan contract (see report section entitled *Pension Plans and Other Post-employment Benefits*) and in various consultant agreements prepared by the Town (see report section entitled *Consultant Agreements*).

The Town should strive to draft contract language that is as clear as possible and not subject to multiple interpretations. This is particularly important when contracts span many years and personnel change thereby limiting opportunities for clarification of intent. Ambiguity makes it difficult for the Town to monitor its own compliance with contract terms and for parties to the contract to understand their own rights and responsibilities.

RECOMMENDATION

13. Utilize language in collective bargaining agreements and other contracts that is clear, easy to understand and not subject to multiple interpretations.

PROCUREMENT

All purchases of goods and services are required to be made in accordance with the requirements established in the Town Charter (Article V, Section C-5.18 Purchasing) and the Code of Ordinances (Chapter 81, Purchasing Policy). These documents delineate competitive bid requirements and purchases considered to be sole source or emergencies.

We reviewed three large dollar purchases of goods or services authorized by the Town Council as documented in the minutes of Town Council meetings held between January 1 and June 30, 2007. We found that the Town should strengthen controls to ensure compliance with its purchasing requirements. Examples of procurements that did not comply with the Town's purchasing requirements follow:

- On May 1, 2007, the Town Council authorized the *sole source* purchase of an ice resurfacing machine at a cost of \$86,770 (\$101,270 less trade-in of \$14,500). The Town Code of Ordinances (Chapter 81 Purchasing, Section 81-7 D (1) Sole Source) provides that a contract may be awarded without competition when the purchasing officer determines, in writing, that there is only one source for the required item. Documentation for this procurement included price quotes obtained from two vendors who manufacture and sell ice resurfacing machines. Accordingly, this transaction was inappropriately designated a sole source procurement.

Further, the Town Charter (Section C-5.18 (b)) provides that "No purchase of ... equipment ... whose costs shall exceed an amount set at the annual Town Financial Meeting, shall be authorized except after competitive bidding....". The amount of \$10,000 was authorized for fiscal 2007 by vote at the annual Town Financial Meeting. This requirement is also included in the Town Code of Ordinances. Accordingly, the Town Charter and Town Code of Ordinances require a competitive bid process when purchasing equipment costing more than \$10,000.

- Purchase of a \$70,000 van for the Town's senior center was not made through a competitive procurement. Documentation for this purchase indicated that a new van was needed to replace an older van which had more than 157,000 miles and was becoming increasingly unreliable. Although the van was already scheduled for replacement and included in the Town's capital improvement plan, the purchase was designated an emergency. Section C-5.18 (c) of the Town Charter requires that, when making an emergency purchase, the Town should obtain three or more verbal quotations followed by written confirmation and the purchase shall be made on the basis of the lowest feasible quotation received. Documentation for this purchase did not include evidence of three or more verbal quotations or written confirmation of any quote other than the awarded quotation.
- The Town obtained quotes from 2 electrical contractors to install a generator for the Public Works Department. The quotes were \$11,545 and \$11,100. After the Town asked the lowest quote contractor to review his price, the contractor reduced his price to \$9,900 and was awarded the contract. Since the Town could have reasonably estimated the contract price to be near or above the competitive bid threshold of \$10,000, it should have followed a competitive bid process in accordance with the Town Charter and Purchasing Ordinance. Upon inquiry, we were advised that this was considered an emergency procurement which, pursuant to the Town Charter, would have required three quotes before making an award.

Purchasing duties are currently split among various Town departments. The Finance Department handles purchase orders and contracts; the Town Clerk's Office retains bid files, and individual departments maintain other supporting documentation. The School Department business office handles all school purchases. Compliance with the Town's purchasing requirements as well as the overall efficiency of the procurement function, could be enhanced by centralizing all purchasing activities and hiring an experienced purchasing agent. Management advised us that the Town is currently interviewing applicants for a part-time purchasing agent position.

RECOMMENDATIONS

14. Strengthen controls over procurement activities to ensure compliance with requirements contained in the Town Charter and ordinances.
15. Hire an experienced purchasing agent to oversee and centralize the Town's procurement activities.

PAYROLL PROCESSING

The Town and School Department perform all payroll functions separately and utilize different payroll accounting systems. Both entities utilize the same external payroll processing service, but under separate agreements with differing terms. In fiscal year 2007, the overall expense to the Town for payroll processing was \$73,094 of which \$50,895 and \$22,199, respectively, was expended by the Town and School Department.

We observed various opportunities for the Town to potentially reduce costs and enhance the efficiency of its payroll processing activities.

Renegotiation of Payroll Processing Agreements

Neither the School Department, nor the Town could produce a signed contract for their current payroll servicing. Both the School Business Manager and the Town Finance Director have indicated that the contract for payroll services has never gone out to bid and no attempt has been made to renegotiate the fee structure or contract terms with their current vendor since their initial signing over a decade ago. The Town Finance Director advised us that other vendors have, at times, provided informal quotes to provide payroll processing services to the Town.

RECOMMENDATION

16. Seek competitive bids for payroll processing services to ensure that the Town and the School are benefiting from competitive pricing for the services required.

Combining Payroll Functions

Both the Town and the Schools use the same payroll service provider but contract as separate entities. The Town Finance Director and the School Business Manager have not explored going out to bid for payroll services for both the Town and Schools as one contract. Although the current vendor pricing structure differs for each entity, both include some fixed costs such as delivery fees and report fees, and some costs that are driven by the number of checks or vouchers processed each pay period and the number of "earnings records" or files maintained on each system. The majority of the cost is in this second category. Additionally, the two entities each pay quarterly and annual fees for various reporting and recordkeeping services.

We believe there are significant potential costs savings to be derived from combining the payroll processing services under one vendor contract. It is likely that various fixed fees could be reduced and other fee reductions could be negotiated on a larger combined contract. The Town should work with their current vendor to determine the feasibility of trying to combine the two payroll accounts into one.

Both the Town Finance Director and the School Business Manager have indicated that they would be willing to explore the possibility of combining the payroll functions. There is concern, however, that the complicated nature of payroll deductions, longevity and other provisions of the numerous collective bargaining agreements involved would make payroll processing and recordkeeping too cumbersome on a single account.

RECOMMENDATION

17. Consider the feasibility of combining the Town and School payroll functions.

Frequency of Payroll Processing

The Town of Smithfield issues payroll checks to Town employees weekly while the Schools follow a bi-weekly pay schedule. Many other municipalities and school districts, as well as State government

process payroll bi-weekly. The Town Finance Director does not believe that the Town is under any contractual obligation to pay employees weekly. We reviewed the five (5) collective bargaining agreements that cover Town employees and also the employment agreements for the five (5) Town employees who have individual employment contracts with the Town and noted no provisions addressing frequency of pay. Considerable cost savings could be achieved by simply switching the Town to a bi-weekly pay schedule. Payroll processing fees ("per item" fees) would be reduced since the number of checks issued would be reduced by 50%. In addition the effort required to process payroll could be substantially reduced. Currently, the Town payroll clerk spends approximately three out of five days preparing, entering and processing payroll. Overall, the effort required to process payroll biweekly would be significantly less than the effort required for a weekly payroll schedule.

RECOMMENDATION

18. Change all payroll processing to a bi-weekly schedule.

Duplicate Payroll Records and Accounts

On the Town payroll, numerous employees are duplicated in the vendor payroll system for recordkeeping convenience. At the recommendation of the Town's independent auditor, the Town ended the practice of issuing 1099 forms for employees who worked for the Town but also received "other compensation" for detail assignments, attendance of meetings, etc. The Town began processing these payments through the payroll. However, instead of including them in the employees' regular weekly paycheck, under an "other" category, the Town set up an extra "employee record" for each of these employees. In fiscal year 2007 this added at least 11 extra "payroll records" to the file, and increased all payroll costs that are driven by the number of employee files or checks issued. According to the Town payroll clerk, they were set up this way so that she could easily separate the wages that are subject to pension contribution from those that are not.

In addition to the multiple payroll files, many employees receive multiple payroll checks in the same week for various types of compensation outside of their regular salary. For example, the Town payroll for the period ended July 7, 2007 had 236 employees yet 289 checks or direct deposit vouchers were issued. This increases payroll processing costs since the number of checks or vouchers issued is the key cost driver. A similar situation exists for the School system payroll. For the payroll period ended May 25, 2007 there were 396 employees yet 470 checks or direct deposit vouchers were issued. There were 35 employees who had two separate employee accounts on the payroll and 74 employees who received more than one check in the pay period.

RECOMMENDATION

19. Eliminate duplicate employee payroll accounts and limit the number of additional checks issued each week for the same employee.

Second Town Payroll Account

The Town maintains a second Company Payroll Account with the payroll vendor to pay one retiree one paycheck per month, incurring unnecessary monthly, quarterly and annual fees associated with maintaining the separate account. The cost associated with maintaining this extra account to process the

one monthly check and issue the one 1099R for fiscal year 2007 was \$1,443. The account was originally set up as the result of litigation between the Town and the retired employee but the Finance Director does not know if there is any legal restriction that would prevent them from changing this practice.

RECOMMENDATION

20. Consult the Town Solicitor to determine if the Town is legally bound to pay the retiree through a payroll service, rather than by a Town check. If they must use a payroll service the Town should consult with their payroll service provider to determine the feasibility of adding this retiree to their regular payroll, rather than maintaining a second payroll account.

Payroll Software Implementation

In January 2007, the Town purchased and implemented a new payroll software program that it eventually abandoned seven months later. The new software purchase and unsuccessful implementation added \$10,500 to the Town's payroll processing costs over the seven month period from January 2007 through July 2007. The costs included initial set-up fees, license fees and monthly processing fees that were significantly higher than the previous payroll system.

These costs may have been avoided had the Town performed a more thorough assessment of its payroll needs and performed a cost/benefit analysis before switching to the new program. Implementing the payroll changes was both costly and time-consuming for both the payroll clerk and for the affected departments. Additional resources were utilized converting back to the old system when the Town decided to abandon the new software program.

RECOMMENDATION

21. Perform a more thorough needs assessment when considering software or information technology system changes to avoid unnecessary and excessive costs.

School Custodian Detail Assignments

Outside organizations renting school facilities for meetings and events are required to pay for a custodian to be on hand during the rental period, per the *Smithfield School Department, Use of School Facilities* policy. Presently, these extra custodian shifts are scheduled through the School Department Office, but payments for the services are paid directly to the custodians by the outside groups. Outside organizations must complete a Smithfield School Department, *Use of Building Form* that serves as the building permit. This five-part form lists the name of the organization, the building, date and purpose of the request and the fees to be collected and is signed by the Superintendent of Schools. The form expressly states that the organization should "present the permit to the janitor with payment for his services". This practice differs from the manner in which the Town pays other Town employees who work "detail" assignments.

When outside organizations pay to have a Town police officer or firefighter at a private function, the payments for service are made directly to the Town. The police officer or firefighter receives payment for the detail work through the Town's payroll process. School janitors doing detail work to cover Town functions, such as voting, are currently paid in the same manner. We believe school custodians providing

janitorial coverage for outside organizations renting school buildings should be paid through the Town or School's payroll process.

RECOMMENDATION

22. Compensate school janitors performing special work details through the School department's payroll process rather than requiring janitors to receive payment directly from the outside organization.

General Payroll Controls

The Town can improve its controls over payroll processing by segregating certain duties, formalizing various policies and procedures and also better documenting supervisory review and approval of key payroll activities.

Payroll is processed weekly by the payroll clerk, who compiles the payroll data from summary sheets forwarded to her from each department and signed by the department manager. Some departments require employees to punch time cards while manual timesheets are completed by other employees. All back-up documentation, including any time cards or time sheets, is retained at the department level. The payroll clerk receives only the summary document and enters the data into the computerized payroll system for processing.

The Town has a Human Resources Manager who works closely with the Town Manager and Finance Director on hiring and personnel issues and who usually notifies the payroll clerk when employees are to be added to the payroll. However, sometimes the new hire information or payroll change information is provided by the Town Manager's secretary or from the Police Department if it is concerning police personnel. Personnel files for the police station are maintained by the Police Department and occasionally, documentation for new employees hired is forwarded directly to payroll without going through HR or the Town Manager. Notice to the payroll clerk that an employee should be removed from the payroll is often by word of mouth or e-mail, and occasionally, the payroll clerk herself follows up with department managers to find out if someone has been terminated, when they have not reported any work hours for a few weeks. The Town Manager does not review or sign-off on changes or additions to the payroll.

When payroll checks are delivered to the payroll office, checks are given to department managers for distribution to their employees. This policy allows the same person who provides the summary of payroll data each week, access to the payroll checks. These duties should be segregated.

The Town does not have a policy and procedures manual for payroll functions

RECOMMENDATION

23. Create a payroll policy and procedures manual (for both the Town and School Department) that includes controls over hiring and termination. All personnel files should be kept in one location.

24. Require the Town Finance Director to review and sign-off on the payroll register each pay period. The Town Manager should review additions and changes to the payroll and periodically review the weekly payroll register.
25. Segregate key payroll functions and duties.

CONSULTANT AGREEMENTS

The Town of Smithfield executes employment agreements and consultant agreements with some individuals who are not covered under collective bargaining agreements. These contracts delineate the duties and services the individual will provide the Town, the hours to be worked, compensation to be paid and benefits to be granted. We were made aware of five "Employment Agreements" and three "Consultant Agreements" which are currently in effect. Individuals who sign Employment Agreements are generally considered by the Town to be contract employees; individuals who execute Consultant Agreements are considered by the Town to be independent contractors.

We discovered that the three individuals that were providing service under these Consultant Agreements were on the Town's payroll and were being afforded many of the same benefits granted to Town employees. Each was receiving a Town paycheck from which state and federal taxes, FICA and TDI were withheld. Additionally, each was enrolled in the State Municipal Employees' Retirement System with employee contributions withheld and the Town making a contribution on their behalf, and each received one or more benefits such as personal days, payment in lieu of personal days or payments in lieu of health benefits.

Two of the individuals who have been working for the Town under Consultant Agreements for six and eight years respectively, are retired Smithfield Police Officers and are collecting a police pension and retiree health benefits through the Town. The documents we reviewed indicate that both of the retired police officers were initially brought on as independent contractors to provide computer consultant services to the Town on an "as needed" basis. Some time later, each was given a job title, added to the payroll and enrolled in the State Municipal Employees Retirement System consistent with status as an employee. These changes appear to have been made without benefit of a formal hiring process, without a bid process, and without the re-drafting of contract terms at the time of the changes or thereafter. At the time of our review, the Consultant Agreements in effect for all three individuals, still expressly identified them as *independent contractors with respect to the Town, and not an employee of the town.*

Decisions regarding the employment status of all three of the individuals were made by a succession of Town Managers. The status of these three individuals was never fully transparent to all levels of Town Administration. The Town Council believed they were independent contractors. The Town Payroll Clerk considered them employees. The Finance Director and Human Resources Administrator believed they should be classified as employees, but were aware of the contradictory language in the Consultant Agreements. The Town Manager who executed the most recent "consultant agreement" for one of the retired police officers in July 2007, stated that he was not aware that the three individuals were on the Town's payroll or enrolled in the Town's pension plan when he signed the renewal of the Consultant Agreement.

As a result of questions raised during our review, this issue was brought before the Town Council on September 4, 2007. When presented with the details regarding the two retired police officers, the council initially voted to remove the two men from the payroll. They did not take any action on the third consultant. When one of the police retirees retained legal counsel to address his impending removal from the Town's payroll, the Council rescinded its directive until the legal matter could be fully researched.

On October 23, 2007 the Town's own legal counsel provided our office with a written legal opinion on the issue stating that, after reviewing the pertinent documents, it appears that the three are in fact employees under the common law definition of employee and that, accordingly, it is the Town's intent to continue to treat these individuals as employees and keep them on the payroll until the term of their contract expires or is otherwise terminated.

Although confusion regarding the appropriate classification of these individuals has been alleviated there may be other related issues that still require consideration. Since the Town participates in the Municipal Employees' Retirement System administered by the State, we asked the Executive Director of the State Employees Retirement System (ERS) to clarify the rules regarding members' participation in more than one pension plan funded by the municipality. He referred us to Rhode Island General Law 45-21-8 regarding membership in the system. This section states that:

"Any employee of a participating municipality as defined in this chapter, who becomes an employee on and after the effective date of participation, shall, under contract of his or her employment, become a member of the retirement system; provided, that the employee is not receiving any pension or retirement allowance from any other pension or retirement system supported wholly or in part by a participating municipality, and is not a contributor to any other pension or retirement system of a participating municipality. "

The Town records indicate that the three "contract employees" described above participate in the Municipal Employees' Retirement System. However, we were advised that two of the individuals are also collecting a pension as retirees of another plan that the Town funds but is not administered by the State. Their status as retired employees receiving a pension supported by the Town appears to preclude membership and participation in the MERS. We recommend that the Town obtain a ruling from the State ERS regarding the applicability of this law to the employees in question.

The Town Solicitor's letter also raises other legal and public policy issues for the Town's consideration. He questions whether (1) the MIS Services provided by the two retired police officers should have gone out to bid, pursuant to state law and the Town's purchasing policy, (2) the positions should have been posted by the Town as outlined in the hiring procedures in the Town's personnel ordinance, and (3) the broader question of the fiscal prudence of hiring two part-time employees to handle the Town's MIS/IT needs, rather than one full-time employee, when gross salaries and fringe benefits are taken into consideration.

By circumventing normal hiring practices in its treatment of these individuals and failing to follow its own hiring procedures outlined in the Town's personnel ordinance, the Town has exposed itself to a potentially costly and circuitous process to rectify the improper hiring practice involving these three individuals. This issue highlights the need for the Town to adopt written policies regarding hiring retired employees. The policy should address all relevant considerations including any limitations on rehiring, participation in pension plans, the required hiring process and their classification if rehired. Further, employment agreements and consultant agreements should be reviewed by all appropriate parties (e.g.,

Town Solicitor, Town Manager, Finance Director and Human Resource Director) before execution to ensure that all appropriate matters have been considered.

RECOMMENDATIONS

26. Re-draft the current Consultant Agreements to conform to the Town's recent determination of the workers status as contract employees rather than independent contractors.
27. Adopt a written policy regarding the practice of re-hiring retired Town employees.
28. Request a ruling from the State Employees Retirement System regarding the membership of rehired Town retirees in the state-administered Municipal Employees' Retirement System. Incorporate rules regarding retirement plan participation into the written Town policy on the rehiring of retirees.
29. Ensure employment agreements and consultant agreements have been reviewed by all appropriate parties, including the Town solicitor, before execution.
30. Adopt a written policy regarding Employment Contracts and Consultant Contracts and the Town's methodology for determining whether an individual is an employee or an independent contractor.
31. Ensure that hiring practices comply with the Town's hiring policies as outlined in the Town Personnel Manual. Ensure that existing policies adequately address the legal and public policy issues raised in the Town Solicitor's letter, including the question of whether these positions should have gone out to bid pursuant to state law, why the positions were effectively filled without following hiring procedures outlined in the Town's Personnel Ordinance, and the broader question of whether the hiring of two individuals to work part-time providing MIS/IT services was fiscally prudent.

HEALTHCARE BENEFITS ADMINISTRATION

The Town and the School Department provide premium based healthcare insurance to employees and their dependents through the same healthcare insurance provider. However, there are thirteen healthcare contracts covering Town, fire, police and school employees, each with specific requirements concerning health insurance coverage. Most contracts specify the insurer and a specific health plan. For example, the fiscal 2007 fire contract specifies that coverage shall be either a certain higher level Blue Cross Healthmate Coast to Coast plan with a chiropractic rider or a Healthmate Coast to Coast base plan. We also noted that the share of the premium required of the employee varies among the various collective bargaining units.

The School Business Manager advised us that the School Department seeks bids annually for healthcare coverage. The Town Finance Director advised us that the Town does not seek bids (for Town, fire and police employees) because other healthcare insurance providers are not interested due to the fragmented coverage groups within the Town.

The Town should consider streamlining its healthcare insurance options and offer a single health plan with uniform benefits for all employees (Town, fire, police and schools) which can be incorporated into all labor contracts. Any specific riders, such as the chiropractic rider currently provided to firefighters, could also be offered as an add-on to the basic plan with separate costs for just the rider. Combining all employees into one plan should allow the Town to obtain more competitive pricing for its coverage and elicit interest from other healthcare insurance providers. Ensuring competitive pricing for the Town's health insurance coverage is important since annual healthcare insurance costs increase at a rate that is higher than the Town's ability to raise property taxes and is a significant budget item.

In addition, the Town should investigate the option of linking its coverage to the State of Rhode Island's contract with United HealthCare. That contract allows Rhode Island municipalities to benefit from the same negotiated contract terms as the State's contract for its employees. Additionally, the Town has utilized premium-based healthcare coverage for its employees but has not investigated whether self-insurance options may be more cost effective.

The Town has multiple labor contracts, all with different end dates. Accordingly, since healthcare insurance coverage is a negotiated benefit included in the labor contracts, any changes in coverage would likely need to be negotiated over the years, with a view to achieving a single health plan. The cost of benefits to the employer and employees can still be negotiated separately as part of each union contract.

RECOMMENDATIONS

32. Move toward streamlining healthcare insurance options for all Town employees (including school employees) to enhance opportunities for competitive pricing and administrative efficiency.
33. Investigate linking the Town's healthcare coverage to the State of Rhode Island's contract and explore other self-insurance options for employee healthcare coverage to obtain cost savings.

Healthcare Benefits Waiver

The Town and School Department provide employees with an additional payment when they elect to waive healthcare coverage. The individual benefit provided to School Department employees is \$4,500 for waiver of medical coverage and 50% of the annual cost of the dental insurance premium. The benefit provided to Town employees waiving health insurance is a flat amount of \$2,000. Waiver expenditures totaled \$535,610 for fiscal 2007 including \$501,610 for 111 school employees and \$34,000 for 17 non-school employees.

Healthcare waiver payments are believed to represent a net cost savings because the waiver payment is typically less than the premium payment required had the employee participated in the healthcare plan. The difference between the waiver payments offered by the Town and School Department is significant and, consistent with the goal of streamlining healthcare insurance coverage plans and options, should be uniform.

The Town should also periodically assess its healthcare insurance waiver program to ensure that it remains a true cost avoidance mechanism and represents a net cost savings to the Town. The net cost savings calculation can be impacted by the number of married couples who both work for the Town and

whether the Town's coverage is premium or self-insurance based. The Town could consider providing no waiver payment in the case of two married individuals both working for the Town.

RECOMMENDATIONS

34. Move toward offering a uniform payment to all Town employees who opt to waive healthcare insurance coverage. Consider eliminating the waiver payment in the case of two married individuals both working for the Town.
35. Assess the healthcare waiver payment program periodically to ensure that it remains a true cost avoidance mechanism and represents a net cost savings to the Town.

Eligibility For Healthcare Insurance

The Town's healthcare insurance provider performs an annual update of employee records and, based on responses received from participants, alerts the Town to employees whose marital or dependent status has changed. The Town relies on Blue Cross to alert them to necessary changes and does not attempt to update employee status or dependent changes on its own. The Finance Department indicated that due to the size of the Town, it learns of changes in marital status or deaths and then follows-up to confirm the details with plan participants.

RECOMMENDATION

36. Implement formal procedures to confirm employee healthcare insurance beneficiary information on an annual basis.

AUDIT COMMITTEE

The Smithfield Town Council is the legislative body of the Town vested with various powers of a financial nature under the Town Charter. The Town Council should pass an ordinance establishing an audit committee, potentially supplemented with public members with specific financial expertise, charged with the following responsibilities:

- select the independent auditor for the Town's financial statement audits;
- monitor the progress of the financial statement audit;
- evaluate the results of the financial statement audit;
- ensure that control weaknesses and legal compliance violations identified in the course of the financial statement audit are promptly and effectively remedied;
- serve as a direct communication link between the Council and the independent auditors; and
- monitor the adequacy of the governments internal control structure on an ongoing basis.

RECOMMENDATION

37. Establish an audit committee to oversee the Town's annual audit process from procurement of the auditors to approval of the Town's corrective action plan for recommendations resulting from the audit.

PERFORMANCE AUDIT OF THE SCHOOL DEPARTMENT

The School Department has an operating budget of approximately \$30 million for the fiscal year ending June 30, 2008 which represents over 50% of the combined operating budget for the Town. As a result the school department represents a major portion of the Town's overall financial operations. The Town should obtain a performance audit of its School Department to determine if the School department is operating efficiently, effectively and economically and to provide recommendations to improve operations and achieve cost savings.

RECOMMENDATION

38. Solicit bids for a qualified firm to conduct a performance audit of the School Department.

ICE RINK

Bank Accounts

The Ice Rink maintains three bank accounts. One is the ice rink operating account which is under the control of the Town Treasurer who signs checks. The other two bank accounts – one for the snack bar and one for the skate shop and other activities - are under the control of the Ice Rink manager who signs all checks written from these two accounts. In January 2007, the Town's independent auditor recommended the following in their fiscal 2006 management letter:

- the latter two accounts should be under the direct control of the Town Treasurer;
- all checks should be signed by the Treasurer rather than the Ice Rink manager;
- the Treasurer's office be the mailing address for these accounts;
- the bank reconciliations should be prepared by the Treasurer's office; and
- the ice rink bookkeeper not be an authorized signature for these accounts.

During fiscal 2007, the mailing address for these latter two accounts was changed to the Town Hall and the Treasurer's office began preparing monthly bank reconciliations. In addition, authorized agent signatures were changed, i.e., the Ice Rink bookkeeper was removed and the Town Treasurer was added as an authorized signature. However, we scanned all checks returned with the bank statements during the 6 months ended June 30, 2007 and found that the Ice Rink manager continued to sign all checks issued.

We found that the Town no longer needs the snack bar account because the Town awarded a contract to privatize the snack bar concession beginning in the fall of 2007. The Skate Shop account is principally used for advertising receipts and certain other ice rink receipts and disbursements. The Skate

shop represents a small portion of the total account receipts and disbursements. We believe these receipts and disbursements should be processed through the operating bank account which is under Town control.

RECOMMENDATION

39. Close the bank accounts for the snack bar and skate shop and maintain one bank account under the control of the Town Treasurer. Require the Town Treasurer to sign all checks.

Cash Receipts

Ice Rink receipts totaled \$733,511 during fiscal year 2007 per the Town general ledger. Receipts are deposited by ice rink personnel *weekly* and reported to the Town Finance Department *quarterly*, for recording in the Town general ledger. The Town should deposit receipts intact *daily* and report receipts to Town Finance Department *weekly*. The Town should reconcile the Ice Rink's record of receipts and the Town's general ledger on a monthly basis.

RECOMMENDATIONS

40. Deposit receipts intact, daily, and report receipts to the Town Finance Department weekly.
41. Reconcile receipts between the Ice Rink and Town general ledger monthly.

Contracts

We found several weaknesses in the way contracts were processed. On April 20, 2005, the Ice Rink entered a five year agreement with a beverage vendor to provide beverages for the snack bar and an aggregate payment to the Ice Rink totaling \$15,000 over the life of the agreement, payable in annual installments of \$3,000. The Ice Rink reports the annual payments to the Town as advertising revenue. This contract was signed solely by the Ice Rink Manager on behalf of the Town. The Town should strengthen control over contracts by requiring that the Town Manager or Finance Director also sign contracts binding the town.

RECOMMENDATION

42. Require the Town Manager or Finance Director to sign contracts on behalf of the Ice Rink in addition to the Ice Rink manager.

The Ice Rink entered into an agreement with a vendor to provide game/vending machines at the Ice Rink. The contract was awarded following a competitive bid process and approved by vote of the Town Council. However, a formal contract document was not created. Instead, the Town is relying on the bid data submitted by the vendor.

RECOMMENDATION

43. Draft a formal written contract document for vendor agreements.

As of August 28, the contract for ice rink concession services, which was to be effective September 1, 2007, had not been executed. Management advised us that this occurred because the contract was awarded to a vendor who did not have an appropriate food service license from the Town of Smithfield. This omission was not discovered until after the contract was awarded. This requirement was not part of the selection criteria for making an award.

On September 18, 2007, the Town Council voted to approve a Victualling license for the vendor pending compliance with all state regulations and local ordinances and final approval by the Rhode Island Department of Health. The vendor began providing concession services in October 2007.

RECOMMENDATION

44. Ensure that licensing requirements are addressed in future bid solicitations. Issue contracts timely once a bid has been awarded.

Privatization of Snack Bar Concession Services

In August 2007, the Town Council voted to privatize the snack bar concession located in the Town ice rink. The contract was awarded to a vendor who began managing the snack bar in October 2007. Management advised us that this decision was based on its desire to discontinue involvement in operating the snack bar and the results of a Town prepared cost benefit analysis that indicated that it would be more beneficial to privatize the snack bar rather than have the Town (Ice Rink Enterprise Fund) continue to operate it.

We reviewed the Town's analysis for a Town operated concession and found that it was not adequate because it overstated sales revenue (even though it was not based on increasing sales prices) and did not consider all costs. For example, the Town's analysis showed estimated sales revenue of \$78,205 and estimated expenses for the purchase of inventory and direct labor totaling approximately \$72,085 resulting in an estimated profit of \$6,120. However, this analysis did not include indirect labor (which we calculated to be approximately \$7,900) and overhead costs (such as heat, electricity, water, sewer, insurance, maintenance and depreciation) which the Town did not calculate. The additional cost of \$7,900 for indirect labor reduced the Town's estimated profit of \$6,120 to an estimated loss of (\$1,780) before overhead costs.

In contrast, our review found that estimated sales revenue for a Town operated concession totaled approximately \$62,500 and estimated expenses for the purchase of inventory, direct labor and indirect labor totaled approximately \$65,000 resulting in an estimated loss of (\$2,500). Our analysis also did not include any provision for estimated overhead costs (such as heat, electricity, water, sewer, insurance, maintenance and depreciation) and we did not calculate such costs because based on an estimated loss of (\$2,500) before any allocation of overhead costs, one may conclude that it made sense to privatize the snack bar operation.

In the future, the Town should prepare a realistic cost-benefit analysis when considering privatizing a public operation. Such information is needed in order to determine whether to privatize or keep an in-house operation, and, if privatizing, to determine which contract bid yields sufficient revenue to cover any costs which remain the Town's responsibility and whether the Town is getting a fair deal. For example, the Town estimated that it would receive \$14,400 (minimum bid) of revenue from a vendor operated facility. Of

this total, \$1,500 would be used to cover the estimated cost of electricity and \$12,900 would be net contract revenue for the ice rink to cover other overhead costs. However, the Town does not know whether this amount is sufficient to cover other overhead costs because it did not calculate such costs.

RECOMMENDATION

45. Prepare cost benefit analyses that reflect realistic revenues and all associated costs for an in-house operation when considering privatizing any in-house operation.

Fee for Ice Time

We compared the fee charged for ice time by the Smithfield Municipal Ice Rink and other ice rinks in the area and found that Smithfield charges less than other area rinks. During fiscal 2007, Smithfield charged \$140 per hour while other ice rinks charged between \$175 and \$200 or more per hour. The Town increased the fee to \$150 per hour effective September 1, 2007. However, this is still considerably less than the fee charged by other area rinks.

Management advised us that a goal has been to keep the fees for ice time low for Town residents. However, the ice rink is used by leagues from both inside and outside the Town. For example, the ice rink is used by the RI Hockey Coaches Association and the RI Interscholastic League. It is the home ice for the Smithfield Figure Skating Club, the Northern Rhode Island Vikings and the varsity hockey teams for five high schools (Smithfield, Johnston, North Providence, Ponaganset and Scituate).

The ice rink enterprise fund is intended to be self-supporting and should generate revenue to cover all the expenses of maintaining and operating the ice rink. However, the town should charge competitive fees for ice time to ensure that it recovers all costs of operating the ice rink including depreciation of the rink facility and related equipment.

RECOMMENDATION

46. Consider increasing the fee for ice time to a rate that is competitive with area rinks.