# Firehouse Lawyer

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***Inside This Issue***



# Avoiding Audit Findings

Some of my favorite articles, over the years that I have been publishing this newsletter, have been "recycled" seminar papers or legal opinions written for clients. The following article was a paper delivered at a seminar in the 1990's. Recently, I happened to re-read this paper and was surprised to find that it is still timely, but disappointed to see that some of the same mistakes keep getting made. Read it and see if there is anything for your fire district to be concerned about.

## AVOIDING THE TEN CARDINAL SINS THAT LEAD TO AUDIT FINDINGS

### I. INTRODUCTION

Hopefully, that catchy title caught your attention. Actually, when I dreamed up that title for the seminar, I was not sure whether I could identify ten cardinal sins, or whether there might be a dozen or more. The purpose of this seminar, however, is simply to highlight what seem to be the most common mistakes or areas in which the State Auditor makes adverse findings, that may be embarrassing, (or worse) for a municipal corporation in Washington. The preparation for this particular seminar has been primarily spent in simply reading approximately 100 audit reports on the State Auditor's Office website on the internet. Obviously, given the purpose of the seminar and the title, I have not been looking at audit reports where everything is perfect, and so please do not be confused. Probably 90% of the audits of municipal corporations in Washington include no adverse findings at all. Nonetheless, I felt we could learn from the mistakes of some of the special purpose districts, as well as cities and counties, which have had adverse findings. I have concentrated on audits performed during the last year, so these are not old problems, these are current problems. Finally, lest you think you recognize your district or one of the others in Pierce County in some of the discussion, rest assured that none of the discussion pertains to any fire protection district in Pierce County or its audit. Therefore, without further ado, here are the ten cardinal sins that lead to adverse audit findings.

## II. Ten Cardinal Sins.

### A. Inadequate Internal Controls Over Cash

A common thread in those findings on inadequate internal controls over cash receipts seems to be too few checks and balances. In other words, frequently there are not enough people involved in the handling of cash. The auditor's office and certified public accountants in general often stress the importance of having a different person receiving cash from the person who makes the bank deposit. Furthermore, it is even better to have a third person do the bank reconciliations. We realize that in smaller districts, that may mean the district secretary/administrative assistant receives the money and provides a receipt, the chief makes the bank deposit, and the chairman of the board reviews the bank statement or reconciles it to the deposit slips. Simply by way of illustration, you can see that even in the smallest of districts, there would be enough people to meet the auditor's requirements. However, checks and balances and providing enough people are not the only issue. A simple reminder from the auditor relates to access to cash drawers. Obviously, if cash is kept in a drawer that is accessible to many people or the public in general, it is not at all secure from theft. Just as importantly, even if we disregard theft, the simple fact that more than one person has access to one cash drawer allows for a situation where there really is no internal control. Another obvious suggestion -- if theft does occur, report it promptly so that it is possible to reconstruct the events, and possibly limit the amount of money missing. Another obvious suggestion, to prevent a negative finding, is to procure numbered receipt books and to use them. Finally, with petty cash funds it is absolutely essential to reconcile the accounts frequently and regularly. If the account is used often, then it should actually be reconciled daily. The other procedure that is necessary is to replenish the petty cash fund periodically so that it is brought back to its authorized maximum, whether that be $250.00 or $500.00.

### B. Inadequate Controls Over Other Funds

Many of the same principles discussed above with respect to cash funds, apply just as directly to other funds and property. For example, frequently fire districts have checking accounts for the advance travel fund. Some districts handle checks in other funds, such as burning permit fees, EMS transport billings, etc. It goes without saying that such funds should not be commingled with any other funds. In one audit recently reviewed, the county commingled property seized in a narcotics raid with the funds of the deputy sheriff's association. Similarly, fire protection districts often have volunteer associations or other organizations somehow loosely affiliated with the fire department. It is absolutely essential that the funds and business affairs of the fire district be kept separate and never commingled with the funds of these non-profit associations. Another important concept is the applicability of the daily deposit statute, *i.e.* RCW 43.09.240. Under the circumstances described in that statute, funds received must be deposited daily with the proper depository. Proper documentation and a clear "paper trail" would solve many of the issues that have arisen in the past with respect to checks received. Another check or balance upon misappropriation or embezzlement is insisting upon a restrictive endorsement. Assuming that a municipal corporation had one person receiving checks for deposit and providing receipts to customers and then a different person assembling and making the bank deposit, the second person could review the restrictive endorsements ("for deposit only") on the back of each check prior to deposit. Also, the person who prepares invoices or billings should be a different person from the persons receiving and depositing.

The BARS Manual should be followed. There should be at least one person well-trained in the requirements of the BARS Manual with respect to the handling of cash and other legal tender. There are regular classes, and a wealth of

information on the State Auditor's website concerning the BARS Manual.

**C. Open Public Meetings Act Violations**

As part of nearly every annual state audit, the auditor will be looking at minutes of meetings. One of the primary things they are looking for relates to illegal executive sessions. In numerous seminars, we have circulated a "cheat sheet", which is our shorthand reference for a memorandum listing the legitimate reasons for adjourning into executive session. Any seminar attendee who wants a copy of the cheat sheet should bring that matter to the attention of the teacher. This particular audit finding points up the necessity of using such an approach. If the chairperson uses the cheat sheet at the time of adjourning into executive session, then they will be quoting directly from the statutory subsection authorizing that particular executive session. Then, assuming that the district secretary or other responsible person accurately records in the minutes what the chairperson says with respect to that reason, then the state auditor will find what we want in the minutes. The auditor will find a direct quote from the statute and probably would have no reason to question the matter further. Obviously, however, you do need to ensure that nothing other than proper subjects, within the scope of the reason given, gets discussed at the executive session. It is very possible for someone to file a complaint with the state auditor, alleging that a district has been guilty of open meetings act violations. In that event, the auditor's inquiry might well go beyond a mere review of the minutes and include interviews. If that occurs, and interviewed people reveal that the executive session went beyond the scope of that alluded to in the minutes, then no amount of documentation can protect you from an adverse finding. Therefore, be advised that executive sessions should stay on track. Believe it or not, one of the most common audit findings even in recent years is a failure to follow the open meetings act with respect to executive sessions, or even a failure to take minutes. Given the amount of training/education on the requirements of the open public meetings act in Pierce County in recent years, we would not expect any of our fire protection district clients to experience a negative finding with respect to meetings.

**D. Public Bid Law Violations**

Another area that is strictly scrutinized by the State Auditor is that of compliance with the public bid laws. Case law in Washington teaches us that the primary purpose of all public bidding laws is to ensure that the public gets the best possible price with respect to the public purchase of equipment, supplies and public works projects. Fairness in competition between bidders is only a secondary purpose. In other words, the primary protected group is the public. The secondary protected group is the bidders. We believe that, with respect to fire protection districts, the attitude of the personnel involved in purchasing must be a presumption that the public bid laws apply. Always looking for an exception or a way around the public bid law will ultimately lead to a finding. The sole-source exception should be seen as just that, a rare rather than a routine occurrence. In our experience, fire protection districts in Washington have not found the small works roster process to be particularly practical. Therefore, the dollar threshold for the beginning of applicability of the public bid laws is rather low in the case of fire protection districts. The amount in question is $2,500.00 when the project relates to remodeling or construction pertaining to a fire station or other public lands. When the matter involves purchase of equipment, vehicles, supplies, or the like, and does not involve real property, the threshold amount is $5,000.00. (*Editor's note: You can see this was written before the thresholds were raised, but the point that follows remains valid to some extent.)* In today's economy, these are very small numbers. By comparison, in the water district statute, the

public bid law threshold is $50,000.00. With respect to avoidance of audit findings, probably the most important tip in this area is adequate documentation. I would not recommend any purchase above the threshold amounts without full compliance with the public bid law, unless the fire district has an attorney opinion, in writing, in the procurement file. Therefore, if you feel you have a legitimate case for a "sole source" procurement, or a legitimate claim that you must make an emergency purchase, you need extensive documentation or you are flirting with an audit finding. To be absolutely sure, you would need to consult with the State Auditor's Office, but it is usually adequate to have a written opinion letter or at least a brief memorandum from the district's attorney. Given the conservative and cautious nature of most attorneys (especially this one) dealing with an exception to the Public Bid Statute, it would seem a fairly safe course to file the attorney opinion letter and then proceed. Surprisingly, those fire district personnel who have been complying with the Public Bid Law as a matter of course, do not find it that difficult to follow the statutory procedures. For example, the advertising requirement of RCW 52.14.120 is not nearly as stringent as some advertising provisions.

## E. Ethics Violations

RCW 42.23.030 prohibits municipal officials from having an interest in contracts that they administer. The full statutory text is included in the appendix. The term "municipal officer" is certainly not limited to elected officials and basically applies to all employees who might be involved in contract administration. The statute has several very specific exceptions and a few general ones. One of the general exceptions is in RCW 42.23.030(6) which allows contracts in which officers are indirectly or directly benefited up to a maximum of $1500.00 in any calendar month. In the case of optional code cities, such as Raymond, the limit is inapplicable but an annual limit of $9,000.00 is applicable. The recent case of City of Raymond v. Runyon, illustrates the ethical dangers of trying to utilize this exception in something other than a strict sense. Frankly, auditors look very carefully at any contracts in which fire commissioners or other municipal officers have any direct or indirect interest. There is also a statutory provision, RCW 42.23.040, which protects against liability if a municipal officer has only a remote interest in a contract with his or her municipal entity. A copy of that statute is in the appendix as well. You will note that this particular statute will not protect you if you are engaged in any influence or attempt to influence another officer with respect to execution of such a contract.

## F. Architectural and Engineering Services

There is an often overlooked statute, which requires certain procedures to be followed with respect to the procurement of architectural and engineering services. We were able to find a few negative audit findings with respect to violations of this statute. The statute is not that difficult to comply with, and probably these were simply oversights. While not strictly a public bid law, this is a statute that requires a certain process to be followed and does not dictate any particular result. Essentially the statutory scheme allows a municipal corporation to prepare an annual summary of their needs for architectural and engineering services, or in the alternative, allows the municipality to simply prepare a request for proposals whenever they are in need of such services. For example, if a district had a progressive building program and planned to build several stations over several years, they could simply prepare an RFP for that building program and state that the proposals would be for architectural and engineering services that might stretch over several years and several stations. We feel that would be in compliance with the statute. Alternatively, if a district simply does not how many projects (or whether there will be any)

to expect in a given year, that district could simply do an annual announcement. While violations of this statute are infrequent, it seems so easy to prevent it that it seems unfortunate for there ever to be a finding on this particular statute. RCW 39.80, or selected sections thereof, is included within the appendix.

### G. Inadequate Documentation

A sort of generic finding that can occur with almost anything is simply a lack of adequate documentation. There are various documents you are expected to gather in order to have a smooth audit. If you do not have evidence of insurance or original invoices and vouchers, or contracts and agreements, you can expect the auditor's office to be difficult to satisfy at best. At some point, if you simply do not have the documentation, they will have no choice but to conclude that a statute has been violated. For example, in the case of one drainage district audit that we reviewed, there was an adverse finding simply because they did not keep minutes of all their meetings. Without the minutes to prove that the meetings were held on the regularly scheduled date, and that the Open Meetings Act was complied with, the auditor had no choice but to make a finding.

### H. Repeat Findings

One of the items on the "auditor's checklist" is to review the status of the prior year's findings and recommendations. So be forewarned. Before you begin an audit, one of the first things you should look at is your most recent audit to reacquaint yourself with any findings and recommendations made in that last audit. Surprisingly, a number of the audit reports I reviewed for various municipal corporations in the last few months included repeat findings. The districts, counties and cities that had weak internal controls still had not completely rooted out all of their problems. The feeling is inescapable that once a district or municipality is on the "auditor's list" they will give you extremely strict scrutiny with respect to your accounting and record-keeping practices. Therefore, pay particular attention to areas where you have had findings in the past.

### I. Accountability for Assets

One of the items that auditors look for is proper tracking or accountability of fixed assets in particular. Unlike consumable supplies or inventory, fixed assets should remain in use during their entire useful life. You should also be able to account for them and if you do not have an adequate system of internal controls tracking the purchase, disposal, and/or useful life of such fixed assets, you could get a negative finding. Ideally, we recommend that fixed assets be indelibly marked in some manner to deter theft or pilferage. Small tools, and other portable items, have a nasty habit of disappearing. Employee theft or pilferage, unfortunately, is a major cause of loss of such personal property items. Even small items of equipment or furniture have been known to disappear. While an indelible marker showing that the property is for district use only is not a panacea, it does show your intent to avoid such theft. Some are reluctant to indelibly mark such property, because eventually it may be surplused and sold. That should not be a concern, as it is not that difficult to obliterate district markings at the time of declaring property surplus and getting rid of it. It goes without saying, of course, that such property should also have a clear paper trail showing acquisition, when it is placed in service, and when it is surplused, destroyed, lost, or otherwise taken out of service. While this is not a frequent area of inquiry, we note that tracking of fixed assets is on the auditor's checklist as one of the things they should be reviewing.

**J. Commissioner Compensation**

Another potential "hot button" could be commissioner compensation. While there have not been very many adverse audit findings in recent years in fire protection districts, we must realize that the statute has just been amended, allowing increased compensation monthly and annually. Because there is somewhat more money involved, and commissioners may take advantage of the increase, we can expect slightly increased scrutiny in the next year or so on this issue. If commissioners are waiving any compensation for services, please remember that the signed written waiver should be on file before the month in question. There should be adequate documentation for any day on which compensation for services is claimed, or an adverse finding can be expected.

**K. Cellular Phone Contracts**

While I have not seen any evidence of this in adverse findings contained on the website, I have heard that the State Auditor is giving stricter scrutiny to cellular phone arrangements. As we all know, the cellular phone providers give preferred government rates to emergency service providers such as fire protection districts. The preferred rate also applies to any person connected in any way with the fire protection district. Any discussion of audit findings would be incomplete if it made no reference to Article 8, Section 7 of the Washington State Constitution. This particular law has long been the favorite of the State Auditor's Office. It prohibits any gift or loan of credit by a municipal corporation in Washington to the aid or benefit of any person except for the poor and infirm. Therefore, it is reasonable for the auditor to question whether there is a gift involved because most of these cellular phones are used partly or entirely for personal use. We have reviewed numerous cellular phone arrangements for many of the different fire districts in Pierce County and they are quite a bit different, but have certain common elements. While the vendor may desire a guarantee by the governmental entity, that does not mean that the governmental entity cannot secure commitments from the users to indemnify the fire district from any loss. If you do not have in place a solid agreement requiring the user to reimburse the district, and even going beyond that to create an indemnity fund, then you run the risk of a negative audit finding. All it would take is a several hundred dollar loss on a cellular phone contract for an auditor to question the way your program is set up. There have been a few "close calls" in Pierce County in recent years, and so districts without a solid cellular phone policy should talk to those districts that have them, or talk to counsel, about setting up a better program. Probably a similar comment could be made concerning pagers that are provided by fire districts for members of their departments. These are almost as widely used as cellular phones and could get considerable personal use as well.

**III. Conclusion**

It has been brought to my attention that there are only seven cardinal sins in the strict sense of the word. As expected, the number of typical findings to avoid was not enough to entitle this program by reference to a "Baker's Dozen", but was considerably more than the "Seven Cardinal Sins". Perhaps we should have entitled it the Ten Commandments. Oh, I guess there were eleven. In any event, I believe we have accomplished our purpose, which is to advise you which are the most common problems referenced in the audit reports where findings have been made. What we are attempting to do is to alert you as to those particular weaknesses that the auditor is looking for in a typical audit. Perhaps we should emphasize a preventive approach or an educational approach. With respect to training and education, there is a good training program on the BARS Manual, which sets forth a system of accounting that the auditor expects all municipal corporations in Washington to follow. A preventive

approach could include a compliance audit by the attorney, and/or a CPA, prior to commencement of your audit.

## ERRATA

The Firehouse Lawyer made an error last month. I noticed recently that I cited the annexation bill incorrectly. For the record, I was discussing Engrossed Substitute Senate Bill 5808, which became Chapter 60 of the Laws of 2009, and will be codified in the RCW in Titles 35 (cities) and 35A (optional municipal code cities). I referred to it wrongly as a House bill.

## SHOULD YOU VOLUNTEER AT THAT ATHLETIC EVENT?

A recent discussion I had with a chief medical officer, who volunteers at triathlons such as the Ironman in Hawaii, prompted this article. If you are an EMT or paramedic who would like to volunteer in the "medical tent" at athletic events, such as triathlons, marathons, or USA Weightlifting meets, you may want to consider your legal rights and protections first.

A good article in the March Journal of EMS (see www.jems.com) by attorneys from Page, Wolfberg & Wirth, LLC—an EMS law firm of national reputation—points out that in the U.S., we lack clear liability protections for emergency medical providers. While many states have "Good Samaritan" or "qualified immunity" laws, the protections and details vary from one state to another. For example, Washington State has a qualified immunity law for such medics who provide medical care in the course of their employment, so that they are immune from liability, except for gross negligence. But what if they volunteer to serve as medics for the triathlon, managed by the USA Triathlon Association, and it has nothing to do with their employment? Then only the Good Samaritan Law applies; its protections may differ from the qualified immunity law. Volunteer workers in the medical tent are advised to carefully check their local state laws prior to volunteering.

I also liked the tips that the attorneys provided in the article, including (1) always stay within your scope of practice, i.e. an EMT is not authorized to engage in invasive procedures such as IV, but a paramedic is; (2) stay within the medical protocols adopted in your local area; (3) seek input from your medical director when in doubt and (4) as always, fully and accurately document your assessment and care of every patient.

I have seen the USA Triathlon Association Medical Guidelines; they support this cautionary approach. Under "Liability, Insurance and Race Waivers" that set of guidelines starts out: "Although medical service is provided on a volunteer basis for emergency conditions, the Good Samaritan Laws may not be applicable in all settings." (Well, that's reassuring!) It continues: "The Federal Volunteer Protection Act of 1997 covers only not-for-profit events/organizations and may have exemptions." (So that may well be worth reviewing.) It also states: "USAT insurance coverage does not include medical liability for medical personnel. As each individual's medical liability policy differs, it is advised that medical personnel discuss extension of their coverage on an event-specific basis." (In other words, the association's policy does not cover you as an additional insured, so you had better have your own malpractice policy.)

Obviously, coverage may be purchased on a single event basis. The guidelines state: "Individual insurance policies may already include coverage for outside medical activities such as marathon/triathlon medical tent coverage on a volunteer basis. Options may be available to obtain extension of liability coverage on a single event basis and these costs should be included under the race budget assigned to medical coverage." So it appears that the management of the risks of potential negligence liability is made the responsibility of the event director, rather than the national organization. As long as this allocation of the risks is clearly understood, and the volunteers attend to their own protection, at least the participants understand who is responsible for what.

The USA Triathlon Association also expects all volunteers, including medical tent volunteers, to sign a "Volunteer Consent, Release & Waiver of Liability" form, which purports to waive or release any and all claims for injuries they might themselves suffer in connection with volunteering. Maybe I am just too cynical, but does all of this seem like a series of disincentives to volunteering at such events? Is it time for all such athletic associations and event organizers to "get on the same page" and to provide incentives to volunteer, such as insurance coverage and/or indemnification, because the immunity and Good Samaritan Laws may not be adequate? If I were an EMT or paramedic, I would think twice before volunteering at such athletic events, under the current confusing or downright discouraging situation. At the very least, I would clarify what coverage is available to me before proceeding.

End of sermon for this month.

## DISCLAIMER