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Operational Review

Dutchess County Resource Recovery Agency

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Executive Summary

Purpose and

Authority:

The Authority Budget Office (ABO) is authorized by Section 27 of the Public Authorities Accountability Act (Act) to review and analyze the operations, practices and reports of public authorities and to assess compliance with various provisions of Public Authorities Law and other relevant State statutes. This includes rendering conclusions and opinions regarding the performance of public authorities and assisting these authorities improve management practices and the procedures by which their activities and financial practices are disclosed to the public. Our operational review of the Dutchess County Resource Recovery Agency was performed in October and November 2009 and was conducted in accordance with our statutory authority and compliance review protocols which are based on generally accepted professional standards. The purpose of our review was to provide an objective determination of the extent of the Agency's statutory compliance, and make necessary recommendations to improve their business practices.

Background

Information:

The Dutchess County Resource Recovery Agency (Agency) was established in 1982 as a public benefit corporation pursuant to Title 13-D of Public Authorities Law to manage the disposal of solid waste in Dutchess County (County). The Agency is governed by a seven member Board and its daily operations are managed by the Agency's Executive Director. The primary source of revenue for the Agency comes from tipping fees, the sale of surplus generated energy, and interest income. For the fiscal year ending December 31, 2008, the Agency generated \$15.6 million in revenue (71 percent from tipping fees), while expenses of the Agency totaled approximately \$18.9 million. Per an agreement, the County subsidizes the Agency's annual operating loss. As of December 2008, the Agency had bonds outstanding of \$35 million.

Results:

Our review found that the County does not enforce its flow control legislation, which directs that all solid waste generated within the County be delivered to the Agency's waste to energy facility. As a result, the Agency is not able to maximize the use of its facility or to generate sufficient tipping fee revenue to meet its operating expenses. Accordingly, the Agency has become increasingly dependent on an annual County subsidy to cover its deficits. We believe the Agency could earn up to \$680,000 in new revenue if its waste to energy plant operated at full

capacity. Further, the Agency's tipping fees at its recycling facility do not recover operating expenses.

While the Agency has taken some steps to comply with the Act, its failure at times to meet its fiduciary duties, adopt certain management practices and internal control procedures, or enforce existing contracts resulted in \$1.2 million in lost revenue or unnecessary operating costs in 2008.

Introduction and Background of the Authority

The Dutchess County Resource Recovery Agency (Agency) was established in 1982 by Title 13-D of Public Authorities Law to finance, construct and operate a waste to energy facility. Construction of the waste to energy facility was financed through the issuance of Agency revenue bonds and New York State Environmental Quality Bond Act grant proceeds. The Agency also operates a recycling facility as part of its solid waste management efforts. The Agency contracts with two separate firms to operate the waste to energy facility and the recycling facility.

According to a solid waste disposal service agreement between the Agency and the Dutchess County (County), the County is to deliver a guaranteed amount of municipal solid waste to each of these facilities. As part of the solid waste management plan, County residential, commercial and public customers are required to separate recyclable materials from solid waste material at the source prior to disposal. The majority of these materials are collected and brought to the two facilities by County-licensed private haulers. The Agency charges these haulers tipping fees when material is delivered to the facilities. These tipping fees totaled \$11 million for 2008.

At the waste to energy facility, solid waste is burned to generate electricity. The electricity is used to operate the facility. The Agency sells any excess electricity produced to the local public utility. Revenue from these sales is shared with the facility operator. In 2008, the Agency turned approximately 144,000 tons of solid waste into \$4.2 million in energy sales. The Agency is also responsible for transporting and disposing of any excess unprocessed waste such as ash or materials recovered from the residue at the end of this process. The Agency has agreements for the transportation and disposal of these materials.

At the recycling facility, recyclable materials are sorted and processed prior to resale to a third party. The Agency also manages a community recycling program which consists of organizing county-wide events for the suitable disposal of hazardous household waste.

The Agency is governed by a seven-member Board. Three members are appointed by the County Executive, three members are appointed by the Chairman of the County Legislature, and one member is a joint appointment subject to confirmation by the Legislature.

The Agency operates on a January 1 fiscal year, and for 2008 the Agency's operating costs totaled \$18.9 million. The Agency's daily operations are managed by an Executive Director. As of November 2009 the Agency had 7 full-time employees. The Agency's administrative costs were approximately \$1.5 million, of which \$638,000 were personal service costs. Agency staff perform

primarily financial management, contract management and administrative support functions, but also operate the truck scales, transport some of the recovered materials and coordinate County recycling programs. The Agency has also entered into various professional service agreements for legal, auditing and independent engineering services.

Another major source of revenue for the Agency is a County subsidy (referred to as the County net service fee). The County makes up any deficit if Agency revenues are insufficient to cover operating costs. For 2008, the County subsidy was \$3.5 million.

The Agency's outstanding long-term debt as of December 2008 was \$35 million. This debt was issued to fund and refinance the construction of the waste to energy facility and various facility improvements that were required to comply with Federal environmental regulations.

Compliance Review Objectives

The Authority Budget Office (ABO) is authorized by Section 27 of the Public Authorities Accountability Act (Act) to conduct reviews and analyses of the operations, practices, and reports of public authorities to assess compliance with New York State laws. Our operational review was conducted to determine the effectiveness of the Agency's operations, as well as provide an objective determination of the Agency's compliance with the Act, Public Authorities Law and other applicable statutes.

Compliance Review Scope and Methodology

Our compliance review was conducted in October and November of 2009, and covered selected Agency operations for the period January 1, 2007 through November 2009. Our review focused on the effectiveness of the governing Board and Agency management and the operations of the Agency. Specifically, we reviewed:

- Effectiveness of the Agency's operations
- Revenues, expenditures and outstanding bond obligations
- Internal control structure of the Agency
- Board duties, committee involvement, and independence
- Board member participation in State-approved training
- Policies and procedures required under the Act, Public Authorities Law, Public Officers Law, and State Finance Law
- Policies and procedures indicative of good governance practices
- Procurement, cash and investments practices
- Independent financial audits and other reports
- Transparency of Agency operations
- Adherence with reporting requirements

In addition to reviewing documents and records, we interviewed management, Agency staff, Board members, and County officials; attended a Board meeting; and performed other testing we considered necessary to achieve our objectives. Our report contains recommendations to improve the effectiveness of the operations of the Agency, as well as to ensure the Agency's compliance with Public Authorities Law and other applicable laws. In addition, we have included recommendations for improving corporate governance practices. The results and recommendations of our compliance review were discussed with Agency management and Board members, and their comments have been considered and are reflected in this report where appropriate.

Operational Review Results

Solid Waste Management

The County is not enforcing its existing laws and regulations regarding solid waste management. An effective countywide waste management system generally employs a three-tiered approach. County agreements should provide that all solid waste is delivered to the waste processing facility. Agreements with individual municipalities should also be in place to support the County agreement, and to ensure that solid waste collected by municipalities is included within the waste management plans. Agreements with individual private haulers should also exist to require the central processing of solid waste collected within the County in accordance with the County waste management plan.

We found that the County and the Agency have an agreement stipulating that solid waste within the County is to be delivered to Agency facilities. In return for the disposal of solid waste, the County agrees to subsidize the Agency's operations, if necessary, so that operating costs and debt service payment obligations are met. The County has also adopted laws, rules and regulations for solid waste management, commonly referred to as "flow control". The County's regulations require private haulers to be licensed, and direct the County to designate the facility to be used by the hauler for the disposition of solid waste. If private haulers violate the law or regulations, the license may be revoked.

However, the County does not enforce either its law or its rules and regulations. County and Agency officials justify this lack of enforcement by arguing that the capacity of the waste to energy and recycling facilities must be expanded before flow control can be strictly enforced.

The County estimates the total amount of waste generated annually in Dutchess County, exclusive of construction and demolition debris but including recyclable materials, is approximately 250,000 tons. Of that, about 30,000 tons is estimated to be recyclable material and the remaining 220,000 tons is non-recyclable waste. The Agency has typically processed about 10,000 tons of recyclable material and about 144,000 tons of non-recyclable material annually. The capacity of the waste to energy facility is approximately 164,000 tons. It was realized at the time the waste to energy facility was built that it would not be able to process all of the solid waste generated within the County. According to the agreement with the County, any material that is unable to be processed at the Agency facility may be diverted to a landfill. These statistics indicate that more than 100,000 tons of solid waste is not being delivered to the waste to energy facility in violation of the current County law. Furthermore, we found no records indicating how this additional waste was processed or disposed.

Agency management's position is that flow control cannot be mandated until the Agency can handle all waste in the County. However, we do not believe that is valid, since the Agency was not able to handle all waste when flow control was being enforced in the early 1990s. Further, Agency management indicated that they have been actively pursuing several significant and interrelated issues since 2005, including reinstating flow control, upgrading and expanding the system, implementing user fees, and expanding licensing and enforcement activity. However, the County has not supported or acted on any of these issues and as a result has had to subsidize the Agency's operations. This subsidy totaled \$3.5 million in 2008.

Agency Fee Structure

The Agency is not setting tipping fees at the waste to energy facility at a level sufficient to meet its cost of operations. The Agency's primary revenue source is the fee charged to private haulers for delivering municipal solid waste to the Agency's waste to energy facility. This fee is commonly referred to as a tipping fee. However, since the County does not enforce its existing law and regulations, private haulers often opt to dispose of the solid waste they collect at other locations outside the County, rather than at the Agency's facility. To minimize this behavior, the Agency attempts to set the tipping fees at a rate that is competitive with other facilities, rather than at a rate sufficient to meet its operating costs. During 2009, the Agency set the base tipping fee at \$80 per ton. As further incentive to private haulers, the Agency offered discounted rates to those haulers providing a significant amount of solid waste to the facility, or to increase the amount of solid waste delivered to the facility during typical low volume periods. As a result, some private haulers pay a discounted fee of \$73.75 per ton. Seasonal discounts can bring the actual tipping fee to as low as \$63 per ton. These reduced rates are insufficient to meet the facility's operating costs. The Agency needed a County subsidy of \$3.5 million in 2008 to close its deficit. The Agency's projected deficits for 2009 and 2010 will require an annual County subsidy of more than \$6 million. Agency management indicated that the tipping fee is not set at a level to meet its operating costs due to the lack of flow control enforcement by the County.

Based on its 2008 operations, for every \$1 received by the Agency in tipping fees, the Agency incurred \$1.31 in costs. It paid \$.94 to the contractor for operating the waste to energy facility; \$.21 for disposing of the residual ash; \$.14 for administrative costs; and \$.02 to the contractor for operating the recycling facility. This expenditure gap was not eliminated by other revenue sources.

The Agency is not setting tipping fees at the recycling facility at an appropriate level to recover operating expenses. The primary funding source for the recycling facility is revenue realized from the sale of recycled materials. In fact, for most of 2008 the Agency did not impose a tipping fee on haulers who delivered materials to the facility. However, in the fall of 2008, there was a

significant decrease in the demand for recyclable material. Many private recycling companies which competed with the Agency discontinued operating, resulting in an increase in the amount of material delivered to the recycling facility. This additional volume taxed the capacity of the facility to process and dispose of the recycled material. In an effort to cover costs previously funded through the sale of recycled materials, and to better control the volume of material being delivered, the Agency instituted tipping fees. Based on the recommendations of the contractor, these fees were adjusted periodically -- sometimes as often as monthly. For the 21 month period from January 2008 through September 2009, the tipping fees at the recycling facility ranged from \$0 to \$15 per ton for fiber (paper), and \$0 to \$35 per ton for comingled material. Agency management indicated that the market rate for recyclables drives the behavior of the haulers: when market rates are high, haulers are more likely to market the material themselves. When market rates are low, haulers deliver the material to the Agency's recycling facility. The Agency has chosen to adjust its tipping fees to accommodate this behavior in absence of the enforcement of flow control.

The evidence suggests that this approach neither generated sufficient revenues to cover annual expenses nor had an effect on the volume of materials being delivered. For example, 7,000 tons of material was processed at the recycling facility during the first nine months of 2008, when for most of that period there was no tipping fee in place, while 9,600 tons of material was processed during the first nine months of 2009, when tipping fees were in place.

Lost Revenue

The Agency is losing revenue by not operating at full capacity. The Agency processes more than 144,000 tons of solid waste annually. According to data maintained by the State Department of Environmental Conservation, the facility operates at about 86 percent of its permitted capacity. This data also shows that the average for the ten waste to energy facilities in New York State is 97 percent of the permitted capacity. Furthermore, the two facilities most comparable to the Agency's facility operate at levels above the statewide average. We noted also that during 2008, the facility operated at reduced levels for 8 percent of the total available operating time as a result of insufficient waste being available.

The Agency is authorized to operate the waste to energy facility at a capacity of 164,000 tons. We believe the Agency should be able to process an additional 20,000 tons of solid waste per year without significant impact on the facility's infrastructure or operations. Since county residents and businesses produce approximately 250,000 tons of solid waste annually, this additional tonnage is already being collected but re-routed to other locations, including locations outside Dutchess County. If the Agency received and processed an additional 20,000 tons of solid waste per year, it could receive up to \$680,000 in additional revenue annually. This revenue would result from \$800,000 in new tipping fees

(based on the current \$80 per ton tipping fee, to be shared equally with the operator according to the terms of the agreement), as well as an additional \$130,000 to \$180,000 annually in electricity sales. These new revenues would be offset by the revenue sharing agreement with the facility operator and an estimated \$300,000 cost for disposing of the residual ash.

The Agency is losing significant revenue by failing to monitor its contract for recovered material disposal. As part of the waste to energy facility operating agreement, the contractor is responsible for recovering at least 80 percent of the ferrous material from the waste residue, and marketing the recovered material for resale. The contractor retains ten percent of any revenue received from such sales. The balance is revenue to the Agency. If the material is not sold, the Agency pays the cost of transporting and disposing of this material offsite.

The operating agreement stipulates that it is the responsibility of the waste to energy facility operator to sell the recovered material. However, Agency management described this provision as an option, which the Agency elected not to enforce. Instead in 2001 the Agency opted to contract with another private company for this purpose. This contract called for the Agency to pay the contractor to accept and market the recovered ferrous material. For any recovered non-ferrous material, the Agency does not pay the contractor to transport the material, but in both cases, revenues from the sale of recycled materials were to be shared equally between the contractor and the Agency. The contract was amended in 2001 requiring equipment to be installed that would separate the ferrous from the non-ferrous material. This equipment was to be purchased by the Agency. Five months later, the contract was amended a second time requiring the Agency to pay the contractor to load the material onto rail cars.

Agency management told us that the equipment was never purchased due to a lack of space. Since the equipment to separate ferrous and non-ferrous material was never in place, the Agency did not attempt to distinguish between the amount of ferrous and non-ferrous material recovered for resale. Instead, the Agency just paid the contractor to accept and load the recovered material, without requiring the contractor to share any revenue from the sale of recovered material. In 2008, over 5,700 tons of recovered material was provided to the contractor. The Agency further indicated that in 2008 an interested third party determined that there was insufficient non-ferrous material to warrant separation. We do not believe that this justifies the Agency's failure to enforce the terms of the contract and collect its share of any revenue received from the sale of recovered material.

We determined that an approximate price for recovered ferrous material at the time of the contract was \$77 per ton. This price increased to about \$300 per ton by the end of 2004, and rose as high as \$558 per ton in early 2008. Agency

management provided us with data that supports these prices. Based on these figures, we estimate that the Agency lost up to \$940,000 for 2008 by not enforcing the revenue sharing provision of its contract. Agency management disputes this total, and claims that the lost revenue was about \$269,000. However, their calculation uses a base rate of \$125 per ton, rather than the \$77 per ton that existed at the time the contract was initiated. Also, the Agency's calculation provides for 20 percent of the revenue generated, rather than half of the revenue as called for by the contract. In addition, management indicated that they are in the process of competitively procuring a new contract. Although the Agency is in the process of obtaining a new contract, the failure to act in the best interest of the Agency and collect revenue due to the Agency demonstrates a lack of understanding of the Board's fiduciary duty.

In 2008, the Agency did not reduce payments to the operator for failure to meet certain contract requirements, and as of our review has not received over \$250,000 due from the operator. Under the waste to energy facility agreement, the Agency pays the operator service fees, fixed maintenance fees, a share of energy revenue, and allowable pass-through expenses such as utilities, insurance, and applicable sales tax. The contract also includes provisions for adjusting the service fee when the contractor fails to meet performance guarantees specified in the contract. The Agency contracts with an independent engineer to monitor the contractor's performance. The engineer reviews the monthly invoices submitted by the facility operator and determines whether the facility operator is meeting the performance standards identified in the contract. When performance standards are not reached, financial penalties are applied. We found instances where the engineer determined that the operator produced less electricity per ton of waste processed than required by the contract and calculated the amount of the financial penalties to be assessed. Rather than reduce its monthly payments to the operator to capture those penalties, the Agency performs an end of year reconciliation. For 2008, this year end reconciliation determined that the operator owed the Agency \$258,637. However, as of this report's issuance the Agency had neither been reimbursed by the operator nor adjusted its 2009 monthly payments to recover this amount. Board members responded that the Agency is limited to the terms of the contract. Agency management believes it is not in either party's best interest to settle contract penalties monthly, since the monthly engineer reviews are based on estimates and that it is more accurate to rely on year end reconciliations. We disagree. Monthly assessments of penalties based on estimates are practical, assure the Agency does not significantly over pay the contractor, and can still be reconciled at year end.

The Agency has not adjusted its tipping fees to account for the additional costs incurred for allowing private haulers to deliver waste outside normal business hours. We found that the Agency allows private haulers to deliver solid waste outside the normal business hours agreed to in the contract. In 2008, the Agency paid over \$12,000 when the operator opened the facility to accept

solid waste deliveries outside of normal business hours. The Agency has not adjusted the tipping fees charged to those haulers to recover these additional costs, or amended the operating agreement to reflect more accurately its normal hours of operation. Agency management and the Board indicated that these extended hours are a public service to the community and result in additional waste being delivered to the facility, and that the revenue generated more than covers the additional costs. However, it is the responsibility of the Agency to set its fees at a rate that covers the additional costs being incurred.

The Agency is not adequately managing its contract to sell electricity. The Agency has a contract to sell electricity produced by the waste to energy facility to the local public utility. According to the contract, the utility company makes monthly payments to the Agency based on the market rate of electricity, but no less than \$.06 per kilowatt hour. During most of 2008, the market rate for electricity exceeded \$.06 per kilowatt hour. However, the Agency did not require the utility company to make monthly payments at the higher market rate. Instead, the utility company continues to make monthly payments based on \$.06 per kilowatt hour, and pays any difference between the market rate and \$.06 per kilowatt hour later in the year. As a result, revenue that is properly due to the Agency on a monthly basis is delayed, potentially impacting the Agency's cash flow. Agency management agreed to explore receiving market rate payments from the utility company on a monthly basis.

Operating Issues

The Agency Board has failed to adopt a salary and compensation policy as required by Section 2824 of Public Authorities Law. The Executive Director received salary increases without Board approval. The Agency does not have written policies that cover how the Agency is to determine, grant or approve salary increases for staff. The Executive Director indicated that he has full autonomy to set salary levels. Although the number of staff positions has been reduced since 2007, remaining staff salaries have increased by an average of 9 percent from 2007 to 2009. The Executive Director's salary has increased from \$62,000, in 2007, to \$108,000 in 2009. Although the Agency's by-laws state that the Executive Director serves at the pleasure of the Board, we found no documentation that these increases were discussed with or approved by the full Board. The Executive Director and current Board Chair argued that the Executive Director was originally hired at a lower salary because at the time, he was the Board's Chair and continued to hold a full-time private sector position. Once the Executive Director settled into the Agency position full-time there was an understanding his salary would be adjusted accordingly. The Board Chair told us that he authorized this increase, without discussing it with the Board. However, when the Board adopted a resolution to hire the Executive Director it set the salary at \$62,000 per year with no provision for automatic increases. Further, we found no written employment contract for the Executive Director that outlines his responsibilities and benefits.

The Agency is paying overtime to employees in violation of its policy. This policy also does not authorize compensatory time that is being provided to staff. The Agency has a Staff and Management Benefit Plan that addresses time and attendance rules for staff. The plan, which was last amended in 1998, indicates that the Agency does not allow staff to be compensated for working overtime. We found that between 2007 and 2008 the Agency provided overtime compensation to every employee, except the Executive Director. This compensation totaled nearly \$50,000 in that time, or almost 8 percent of payroll. We also found that some staff, in addition to receiving overtime compensation, also received compensatory time, although the Agency does not have a policy authorizing compensatory time. We found two Agency staff earned and were paid for almost 20 days of compensatory time in 2008 and 2009. Although the Agency's policy does not allow for overtime compensation, Agency management indicated that overtime or compensatory time is required under New York Labor laws for non-management employees. We believe the Agency should review and update its policy.

The Agency does not maintain mileage records on its vehicles. Therefore, it cannot report the amount of taxable wages on employee W-2 forms resulting from an employee's use of Agency vehicles, as required by Internal Revenue Code Section 274(d). The Agency owns and maintains two passenger vehicles that are assigned to the Executive Director and the Senior Accounting Clerk. According to the Internal Revenue Code Section 274(d), separate records for business and personal mileage are required for employer-provided vehicles, and the personal use of an employer's vehicle is to be reported as taxable income on W-2 forms. Further, the Internal Revenue Code defines personal use as commuting from a home residence to a place of work. Our review found that these vehicles are used for commuting to and from the Agency; however, the Agency does not maintain mileage records to differentiate business mileage and personal mileage. As a result, the Agency is not reporting this taxable income on the W-2 Forms of those employees to whom the vehicles are assigned, as required by regulations. Agency management claimed that neither of the vehicles is being used for personal use, even though there is no policy in place regarding use of the vehicles. Further, management did not provide any additional records to support this claim. Moreover, this claim is inconsistent with the Internal Revenue Code.

The Agency is making payments that it is not obligated to make. The Agency has historically paid the Town of Poughkeepsie (the "Town") an annual payment, known as a Host Community Benefit payment. This payment is in recognition that the Town provides some municipal services to the waste to energy and recycling facilities. The payment is based on the amount of tonnage processed by these facilities in the prior year. In 2008, the Agency paid the Town \$226,794. We found no written agreement between the Town and the Agency requiring this payment. However, the Agency Board has approved these

payments for more than 20 years. Agency management indicated that they questioned these payments beginning in 2006, and in 2009, the Agency Board decided to withhold payment for the waste to energy facility, but continued to make the payment for the recycling facility. Board members indicated that this issue is a priority of the Board, and that the Agency, the Town and outside attorneys are currently in the process of resolving these matters. However, they indicated that this will take some time to fully resolve.

The Agency entered into a contract with an unlicensed hauler and accepted the delivery of waste from a second unlicensed hauler. The Agency contracts with two private haulers to transport the ash residue produced by the waste to energy facility. One of these haulers was not licensed to operate in the County. Agency management believes that this hauler was not required to be licensed since it was acting as an agent of the Agency. However, they indicated that this hauler is now licensed. In addition, we found that another hauler who is not licensed in the County was permitted to deliver waste to the waste to energy facility in 2008 and 2009. Agency management indicated that this hauler's deliveries were small loads of office records that were exempt from County licensing requirements. However, County regulations do not appear to exempt office records from the definition of solid waste, and it appears that the hauler should be licensed to transport this material. Agency management also noted that this hauler attempted to deliver other waste to the waste to energy facility in December 2009, and was subsequently turned away by the Agency and reported to the County. Agency management further indicated that they have observed and reported other unlicensed haulers in the County to County officials; however, according to County officials, the County only issued one violation from 2008-2009. The activity of unlicensed haulers in the County highlights the need for flow control and increased licensing and enforcement activity.

The Agency has used its funds to make more than \$3,000 in payments that appear to be inappropriate. In 2008, the Agency paid approximately \$1,800 to local restaurants for various lunches and dinners and \$560 for bereavement flowers and employee gifts. We also identified credit card late fees, payments to vendors for kitchen supplies and coffee, and a membership to a wholesale store at a total cost to the Agency of \$683. We do not believe that these expenditures were consistent with the mission and purpose of the Agency or constitute an appropriate use of Agency funds. Agency management indicated that the Agency provides food for Board meetings and believes this practice to be appropriate. Although providing refreshments for Board meetings may be an appropriate practice, the payments we identified are not related solely to Board meetings. For example, over \$100 was spent at local restaurants on days when there were no Board meetings. Further, we believe that the Agency should be especially diligent in controlling its costs given that it has an annual operating deficit and must rely on an annual County subsidy.

The Agency is making payments to the waste to energy facility operator for sales tax on purchases that the Agency is not obligated to pay. According to the operating agreement, the Agency pays the sales tax on supplies and equipment purchased by the contractor and needed for facility operations. In addition, the contractor is responsible for keeping the facility neat and clean and providing all labor and materials for the operation, repair, and maintenance of the facility. We found that the Agency verifies the amount of sales tax charged against the invoices submitted by the operator; however the Agency does not determine whether the charges being passed through are the financial responsibility of the Agency under the contract. As a result, the Agency has reimbursed sales tax on items that are not allowable under the contract, such as monthly cleaning bills, pest control and landscaping charges. For example, in April 2008 we found that \$378 (57 percent of the total sales tax) was charged to the Agency for expenses relating to the maintenance and cleanliness of the facility that should have been borne by the operator according to the terms of the operating agreement. Agency management indicate that they will review the appropriateness of sales tax on purchases other than items allowed for in the operating agreement.

Compliance Review Results

Board Duties

Section 2824 of Public Authorities Law requires public authority board members to execute direct oversight of senior management and to understand, review, and monitor the implementation of fundamental financial and management controls and operational decisions of the authority. Further, good governance principles dictate that board members act in good faith and in the authority's best interest, and perform their oversight function consistent with the mission of the public authority and the public's interests. In addition, authorities should conduct business in an environment that fosters transparency and enhanced public disclosure, focuses on accountability, and supports external oversight.

We reviewed Board meeting minutes for the period January 2008 through September 2009 and attended the October 2009 Board meeting. The Board generally meets on a monthly basis. In the 21-month period we reviewed, the Board met 24 times and a quorum was present at all meetings. However, the Agency has not made Board meeting minutes available on its web site.

Based on the minutes and the meeting we attended, it appears that the Board is sufficiently informed so as to engage in discussions of the Agency's financial, operational and performance data, including discussion regarding methods to increase the amount of waste delivered at its waste to energy facility. As part of these discussions, the Board has also questioned certain Agency payments. While these discussions are valuable, we found that the Board is not always exercising its fiduciary responsibility over Agency operations, and is not always diligent in its equally important responsibility to exercise oversight of management. We found that the Board failed to address or curtail instances of poor contract management, the lack of effective institutional controls, missed revenue opportunities and inappropriate expenditures.

Board members disagree that they have missed inappropriate expenditures being made by the Agency, and cite the current efforts being made to challenge the payments made to the Town as support. However, this report provides numerous examples of ineffective Board oversight, including the payments to the Town, which have been made historically although no written agreement exists to require the payment or establish the basis for payment.

Additionally, we noted that the Agency's proposed 2010 budget was reviewed by the Board's Finance Committee in September and October 2009, presented to the full Board in October 2009, and discussed again in November 2009 by the

Finance Committee. However, the budget had still not been adopted by the Board at the time of our review.

Also, an inspection of the waste to energy facility was performed by an independent engineer in September 2008 and it appears that the report was completed in December 2008. Although the findings of this report were reviewed with the Board as part of the monthly engineer's report the formal report has not yet been presented to the Board, and there was no indication that the Board has inquired as to the reason for its delay. Finally, as previously noted, the Board approved payments to the Town of Poughkeepsie despite the lack of a formal agreement or legal basis for doing so.

Good governance practices suggest that public authority board member duties and responsibilities should be clearly defined, so that board members understand their roles and are better able to effectively perform their governance responsibilities consistent with the mission of the public authority. We found that the Authority has established by-laws identifying the responsibilities and duties of members and officers. However, although the Board has established an Audit Committee, Governance Committee, Personnel Committee, a Planning Committee, a Facilities Recycling Committee, a License Advisory Committee and a Finance Committee, the by-laws do not identify these committees or cover their roles and responsibilities. Agency management indicated that the by-laws will be revised to include the committees.

Board Member Terms

Section 1047-c(1) of Public Authorities Law stipulates that after serving two consecutive terms, a Board member is not eligible for reappointment unless there is a three year interval. Board members may continue to hold office until their successors are appointed. We believe that two current Board member appointments are questionable, and may have been made in violation of the Agency's enabling statute. We found that one Board member, who was first appointed in 1992 and was reappointed to a second term that ended in 1997, has continued to serve on the Board. Another Board member, who was first appointed in 2002 and was reappointed to a second term that ended in 2007, was reappointed to a third term by the County Executive in 2008. Since the appointing authorities never nominated replacements for either board member, their continued service on the Board effectively circumvents the three year moratorium requirement. The Agency indicated that these Board members legally held their positions in 2009 because one member is a holdover and the other did not complete a second three year term. The Agency holds the position that, in stating 'served as a member for two consecutive three year terms', the enabling legislation indicates that the entire three year term must be served for the restriction to apply. And, since the individual did not serve as a Board member for every day of the second three year term, he continued to be eligible

for reappointment without a three year interval. However, we do not agree, as the enabling legislation has no provisions regarding the "completion of a second three year term". Instead the enabling legislation is specific regarding eligibility for reappointment after a three year interval.

Use of Executive Session

Section 105 of Public Officers Law limits the purposes for which a public body may conduct an executive session. Such purposes include discussions regarding proposed, pending, or current litigation; the medical, employment, or financial history of a particular person or corporation; or the proposed acquisition, sale, or lease of real property when publicity would substantially affect the value of such property. During the scope of our review, a total of 24 Board meetings were held during which the Board entered executive session 10 times. We found that the Board limits the use of executive session to only authorized purposes, in accordance with Public Officers Law. Agency management indicated that the Board enters executive session primarily to discuss personnel, employment and litigation issues with counsel.

Training

Section 2824(2) of Public Authorities Law requires all individuals appointed to the board of a public authority to participate in State-approved training regarding their legal, fiduciary, financial and ethical responsibilities within one year of appointment. We found that six of the seven Board members have met State-approved training requirements, and that the Board member who has not attended mandatory training has been on the Board more than four years.

Audit and Governance Committees

Section 2824(4) of Public Authorities Law requires authorities to establish an audit committee and a governance committee. The audit committee is to be responsible for recommending a certified independent accounting firm, establishing the independent auditor's compensation and providing direct oversight of the authority's independent audit. The governance committee is to be responsible for reviewing corporate governance trends, keeping the Board informed of best practices, updating the authority's corporate governance principles and advising appointing authorities on the skills and experiences required of potential Board members.

The Board established an Audit Committee in January 2008. Although the committee has developed a charter that adequately addresses its responsibilities, we found that the charter also includes certain provisions that do not apply to Agency operations. For example, the charter states that the Audit Committee is required to review reports provided by the Inspector General,

although the State Inspector General does not have jurisdiction over the Agency. The charter also states that the Audit Committee is to review reports from the Agency's internal auditors, even though the Agency does not have an internal auditor. Moreover, although it appears that the Audit Committee has met with the independent auditor, it does not appear that the Committee is fulfilling other duties outlined in its charter. Specifically, we found no indication that the Committee took any steps to inquire whether management had conducted an assessment of the effectiveness of the Agency's internal controls, or required management to complete the assessment for its review. Agency management agreed to delete the irrelevant references in the Audit Committee Charter.

The Board also established a Governance Committee in January 2008 but that the committee did not meet during 2008. The committee has developed a charter that adequately addresses the committee's responsibilities, and has met twice during 2009 to discuss compliance with the Public Authorities Law and the Act. Board members responded that the Governance Committee had met eight times during 2008 and 2009. However, there were meeting minutes provided for only two of the meetings held in 2009, and no minutes of any meetings in 2008.

Policies of the Board

Section 2824(1) of Public Authorities Law requires Board members to establish policies regarding the salary and compensation of senior management, adopt a code of ethics, establish a whistleblower protection policy, and adopt a defense and indemnification policy. The Agency's Governance Committee has drafted a whistleblower policy, an anti-harassment policy and an ethics policy, but these have yet to be adopted by the Board. As previously stated, the Board has not established an employee salary and compensation policy, nor has it established policies over the use of Agency vehicles or credit cards. The failure to establish these policies has contributed to the operational weaknesses we identify in this report. Agency management indicated that the Board is continuing to review various operating policies, and has adopted the whistleblower policy.

Procurement Guidelines

Section 2824(1) of Public Authorities Law requires board members to establish written policies and procedures for the procurement of goods and services. We found the Agency has established procurement guidelines that specify thresholds for the competitive selection of contracts, but do not adequately address the procedures to be followed to review and approve procurements. Further, the Agency does not maintain a list of its procurement contracts. Such a list is an essential management tool for maintaining accurate and complete information on all active contracts, and for monitoring expenses paid to outside vendors, organizations and businesses. We noted that, in its 2008 Annual Procurement Report to our Office, the Agency reported it had only

one active contract. However, our review found that the Agency has 34 active contracts valued at more than \$13 million for professional services such as legal, auditing and engineering services and for the hauling and disposal of trash and recovered materials (i.e. metals).

We reviewed five of these contracts to determine whether the Agency complies with its procurement guidelines. We found that three of the contracts were awarded consistent with the Agency's procurement guidelines; two of these were competitively bid and one vendor was selected from a list of available State contracts. However, the contract for legal services was initially awarded by the Agency in 1993 and had no specified end date. The Agency spent over \$130,000 under this contract in 2008. Although the Agency's procurement guidelines indicate that professional service expenditures of more than \$5,000 per year will be selected under a request for proposal process, there is no indication this was ever done. Also, the Agency had a recovered material disposition contract in effect from 2001 to 2009 that was not awarded through a competitive procurement process. In 2008, this contract cost the Agency more than \$114,000. The Agency is currently requesting proposals for a new recovered material disposition contract.

Agency management stated that it will ask the Board to modify the current procurement policy, including the provision requiring selection of professional services of more than \$5,000 under a request for proposal process. While we agree that the procurement policy should be reviewed and revised, we believe that the current professional services selection requirement is appropriate. Competition generally provides management with the greatest assurance that goods and services of the desired quality are being obtained at the lowest possible price and not influenced by favoritism. Agency management also indicated that the retention of legal counsel without an RFP is a common and acceptable practice. While this may be common, it is not viewed as acceptable: a recent audit of a local public authority conducted by the State Comptroller's Office was critical of that authority for continuing to use certain professional services providers year after year without seeking RFPs.

Investment Guidelines

Section 2925 of Public Authorities Law requires all authorities to establish guidelines to govern investment practices. These guidelines should instruct officers regarding the investing, monitoring and reporting of funds, require that an independent audit of investments be done annually, and require that it be reviewed annually by the Board. The Agency has established investment guidelines which govern specific agreements for the collateralization and security for bond issuance proceeds. We found that the Agency's independent auditor conducted an annual audit of investments and reported that the Agency is in compliance with its investment guidelines.

Property Disposition

Section 2896(1) of Public Authorities Law requires public authorities to adopt guidelines for the use, awarding, monitoring, and reporting of contracts for the disposal of property, and to annually publish a report listing property disposed of during such period, including the price received and the name of the purchaser for all property sold. The Agency's real property consists of the waste to energy facility and administration building and approximately 35 acres that surround the facility. The Agency has established property disposition guidelines that meet the requirements of Public Authorities Law and govern the disposition of real and personal property and posted these guidelines on its web site.

Internal Control Assessment

Section 2800(2) of Public Authorities Law requires authorities to assess and report on the effectiveness of their internal control structure and procedures. An effective system of internal control is necessary to provide the Board with reasonable assurance that resources are safeguarded and that transactions are executed and recorded in accordance with management's authorization and statutory requirements. Internal controls are the policies, practices and guidelines adopted by the authority that, when followed, provide reasonable assurance that staff understand and properly carry out their responsibilities, and that the authority effectively carries out its mission. Failure to establish proper controls could expose the Agency's resources to loss or improper use.

We found that the Agency appears to have effective controls governing its scale operations, which is the essential point of control over the tipping fee revenues. However, we found that there are other significant control deficiencies that need to be addressed. As indicated throughout this report, the Agency lacks written policies and procedures governing its operations. Further, we identify several examples of inappropriate or excessive expenditures, and indicate the need for improved management and monitoring of contracts. These issues have not been identified or remedied by Agency management or the Board, since management has never conducted an assessment of its internal control structure and the Board has not met its fiduciary responsibility to provide appropriate oversight of management and require this assessment. Agency management indicated that they will recommend an assessment of the Agency's internal control systems to the Board.

Transparency

Section 2800(1)(b) of Public Authorities Law requires local authorities to make information accessible to the public to the extent practicable through the use of the authority's Internet web site. This information is to include the mission, current activities, and financial data, including the current year

budget. The Agency has established a public web site and posted its current year budget and audited financial statements along with other public information regarding its recycling and waste disposal events and activities. However, the Agency's web site does not have other information pertinent to the operations of the Agency as required by the Act. Agency management indicated that a full update of the Agency's web site will be undertaken.

Annual Report

Section 2800(2) of Public Authorities Law requires authorities to prepare an annual report disclosing information related to their operations, management, and finances, and to submit this report within 90 days of the end of the fiscal year. The Authority has filed its 2008 Annual Report with the Authority Budget Office using the Public Authorities Reporting Information System (PARIS). However, certain information was found to be reported inaccurately. For example, the Agency indicated in PARIS that Board and committee meeting minutes, by-laws, procurement guidelines and operations and accomplishments are available on its web site, but this information is not available, contrary to the certification made by the Agency.

Budget Report

Section 2801 of Public Authorities Law requires local authorities to submit budget information to several entities sixty days prior to the start of their fiscal year. The Agency submitted its 2009 Budget Report in PARIS and posted 2009 budget information on its web site. The Agency also submitted its 2010 Budget report in PARIS. Its 2010 report includes preliminary data since the final budget had not been approved by the Board by the November 1 filing date. The preliminary budget has not been made available on the Agency's web site.

Financial Disclosure

Section 2825(3) of the Public Authorities Law requires board members, officers, and employees of local public authorities to follow financial disclosure policies established by the County Board of Ethics for the county in which the local public authority has its primary offices. Dutchess County Local Law No. 7 of 2000 requires the Agency's Executive Director to submit annual financial disclosure forms with the County Board of Ethics. We found that the Executive Director has submitted financial disclosure forms with the County in accordance with this local law for the period covered by our review.

Independent Audit

Section 2802(4) of Public Authorities Law states that the certified independent public accounting firm performing the Authority's audit shall be prohibited from providing audit services if the lead audit partner has been the lead auditor in each of the five previous years for the authority.

We found that the Agency has retained the same independent auditing firm since 1997, but that the lead audit partner was changed in 2007 to comply with the requirements of Public Authorities Law.

Compliance Issues Summary

Board Terms

The reappointment of two Agency Board members to three consecutive terms violated the Agency's enabling legislation, Section 2047-c(1) of Public Authorities Law.

Training

One member of the Board has not attended State-approved training, as required by Section 2824(2) of Public Authorities Law.

Policies of the Board

The Agency Board has not adopted a code of ethics, salary and compensation policies, as required by Section 2824 of Public Authorities Law.

Procurement

The Authority did not receive competitive quotes for the selection of its metals contract, as required by the Agency's procurement guidelines.

Internal Control Assessment

The Agency has not assessed and reported on the effectiveness of its internal control structure and procedures, as required by Section 2800(2)(a)(8) of Public Authorities Law.

Transparency

The Agency is not making appropriate information on its operations and governance practices available to the public on its web site, as required by Section 2800(2)(b) of Public Authorities Law.

Governance Recommendations

To Dutchess County Officials:

1. Enforce the County's flow control legislation and waste management rules to require solid waste haulers to deliver all solid waste collected within the County to the Resource Recovery Agency.
2. The County Executive and County Legislature should follow an appointment process that conforms to the Agency's enabling statute.

To the Agency:

1. Establish tipping fees at the waste to energy and recycling facilities at rates sufficient to cover the Agency's net operating costs. Reevaluate the practice of offering reduced tipping fees to certain haulers or adjusting the fees to account for seasonal fluctuations.
2. Increase the amount of solid waste received to maximize the use and efficiency of the waste to energy and recycling facilities and to maximize the revenues generated from tipping fees.
3. Monitor the terms of the contract for recovering material from the waste to energy facility to ensure that the appropriate amount of revenue generated is shared with the Agency, in accordance with the terms of the agreement. Take actions to recover revenues from prior periods that were not provided to the Agency.
4. Enact penalties and cost recoveries on a monthly basis for the waste to energy facility operator, rather than reconciling all items at year end.
5. Consider implementing a higher tipping fee for solid waste deliveries that occur outside the facility's designated hours of operation.
6. Require the local public utility to make payments to the Agency on a monthly basis for all revenues due from excess electricity generated.
7. Adopt a written salary and compensation policy applicable to all staff and management, and ensure that the Agency's current overtime policy is consistent with its operating practices.
8. Adopt a vehicle use policy, and maintain mileage records on Agency vehicles to be able to report personal use of Agency vehicles as a taxable benefit, as required by Internal Revenue Service Codes.
9. Ensure that valid written agreements are in place to support payments made, and monitor all written agreements to verify that the terms and conditions are being met.

10. Ensure that every company contracted to transport solid waste or residue or that delivers solid waste to Agency facilities has an appropriate license.
11. Eliminate the use of Agency funds for inappropriate expenditures, such as employee lunches, dinners, and gifts.
12. Adopt a credit card use policy and improve management practices to ensure that credit card bills are paid timely to avoid late charges.
13. Review the charges included as pass through costs by the waste to energy facility operator to ensure that sales tax is paid only for items that are appropriate charges, in accordance with the contract terms.
14. Revise the by-laws to detail the powers and duties of the Agency's various committees.
15. Ensure that the Audit Committee is performing the duties outlined in its charter, specifically its review of management's assessment of the Agency's internal control structure.
16. Adopt a code of ethics.
17. Revise the current procurement policy to adequately address the procedures to be followed to review and approve procurements, and maintain an accurate and complete list of all active contracts.
18. Ensure that all professional service contracts are competitively selected, and review current contracts to ensure the Agency is getting the best price for its services.
19. Conduct an assessment of the Agency's internal controls and address potential control deficiencies.
20. Post complete and accurate information on the Agency's operations and accomplishments to its public website and PARIS.
21. Adopt and submit its annual budget sixty days prior to the end of the fiscal year and make it publicly available on the web site.