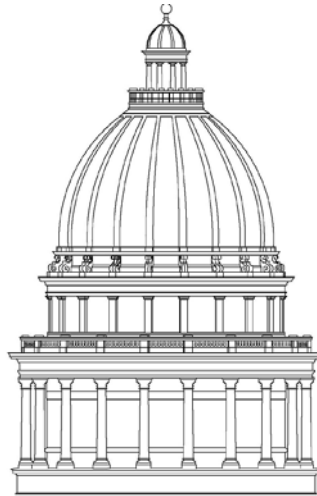


REPORT TO THE  
**UTAH LEGISLATURE**

Number 2017-05



**A Review of  
Best Practices for Internal Control  
of Limited Purpose Entities**

June 2017

Office of the  
LEGISLATIVE AUDITOR GENERAL  
State of Utah





STATE OF UTAH

# Office of the Legislative Auditor General

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## Audit Subcommittee of the Legislative Management Committee

President Wayne L. Niederhauser, Co-Chair • Speaker Gregory H. Hughes, Co-Chair  
Senator Gene Davis • Senator Ralph Okerlund • Representative Brian S. King • Representative Brad R. Wilson

JOHN M. SCHAFF, CIA  
AUDITOR GENERAL

June 20, 2017

TO: THE UTAH STATE LEGISLATURE

Transmitted herewith is our report, **A Review of Best Practices for Internal Control of Limited Purpose Entities** (Report #2017-05). A digest is found on the blue pages located at the front of the report. The objectives and scope of the audit are explained in the Introduction.

We will be happy to meet with appropriate legislative committees, individual legislators, and other state officials to discuss any item contained in the report in order to facilitate the implementation of the recommendations.

Sincerely,

John M. Schaff, CIA  
Auditor General

JMS/lm



# **Digest of A Review of Best Practices for Internal Control of Limited Purpose Entities**

Many public services, such as sewer, water, and fire protection, are provided by separate government entities or districts that offer just one or two services. In this report, we refer to them as limited purpose entities. They include special service districts, interlocal entities, local districts, and independent entities. In Utah, there are nearly 500 such entities that together collect taxes and fees of roughly \$3.5 billion each year. Because they tend to operate behind the scenes, many limited purpose entities do not receive the same level of public scrutiny as city, county and state government agencies. Also of concern is the somewhat hidden nature of potentially several hundred governmental non-profit organizations that are either sponsored by or closely affiliated with government agencies.

## **Chapter II Review of 27 Entities Confirms Concerns in Past Reports**

In recent years, there has been a growing concern for the frequent reports of fraud, waste and abuse among Utah's local districts, special service districts and other, limited purpose governmental entities. These reports, issued by the Legislative Auditor General and the State Auditor, attribute the misuse of funds to weak management controls and poor board oversight. To determine how widespread the problems might be, we surveyed 27 limited purpose entities from throughout the state and concluded that poor governance and weak oversight are common among these local government entities. Of the 27 entities reviewed, we found:

- 16 had missing or weak internal controls
- 13 had a board or staff, or both lacking the qualifications and training necessary to protect against fraud, waste and abuse
- 17 have an organizational culture that does not support good governance and accountability

Unless improvements are made, we believe many of Utah's limited purpose entities will continue to face a high risk of fraud, waste, abuse and poor management.

## **Chapter III**

### **Boards Should Adopt and Implement The Best Practices for Internal Control**

Due to the recent cases of fraud, waste, abuse and mismanagement, we recommend that each governing board evaluate its organization's internal controls. It is the board that must take charge because they are the ones who are ultimately responsible for the success of their organizations. If they leave it to others to maintain control, they may be putting their organizations at risk. Specifically, we recommend that each board consider the following four key requirements of an effective system of internal control.

- The board, executive director and staff need to understand and perform their unique roles
- Each entity needs to adopt a complete set of internal control procedures
- The board and staff need to be qualified and receive ongoing training
- The board and executive director need to set a proper tone of accountability and ethical behavior

See the attached document for a list of the best practices in each of the above areas.

## **Chapter IV**

### **Legislature Should Consider the Best Practices for State Oversight of Limited Purpose Entities**

To improve the control and accountability of Utah's limited purpose agencies, we suggest the legislature consider adopting the best practices for state oversight of limited purpose entities. Specifically, we suggest the following:

- Create a formal state registry of limited purpose entities
- Withhold funds from local entities that do not comply with all state disclosure laws
- Take steps to dissolve entities that are persistently non-compliant
- Encourage counties to take a larger role in promoting compliance by local entities
- Encourage counties to promote greater public awareness of the limited purpose entities in their areas

Finally, Utah's governmental non-profit corporations should be encouraged to follow the same best practices for internal control that limited purpose entities follow.

The following is a list of the best practices that we developed after consulting national sources, such as the Institute of Internal Auditors, and by observing the internal controls used by local entities that are demonstrating effective governance and control over their organizations.

# Checklist of Best Practices for Board Members Of Limited Purpose Entities

<b>Roles of Board and Staff</b>	
See report pages 23 to 27.	
1. The board takes ultimate responsibility for governance of the entity by (1) appointing an executive staff, (2) providing broad policy guidance, (3) authorizing the use of resources, (4) setting goals and expectations, and (5) monitoring results.	<input type="checkbox"/>
2. The board members recognize their role is to be more than just a ceremonial body. They have a responsibility to lead and hold staff accountable for results.	<input type="checkbox"/>
3. The board chair reviews and approves the agenda before each meeting, inviting other board members to propose additional agenda items, if desired.	<input type="checkbox"/>
4. The executive director (a) helps the board draft a set of internal control policies and (b) guides staff as they carry out the board's policies.	<input type="checkbox"/>
5. To protect against fraud, staff duties are segregated such that no one person has control over all parts of a financial transaction.	<input type="checkbox"/>
6. The board appoints a board chair, a treasurer and a clerk.	<input type="checkbox"/>
7. For organizations with an insufficient number of staff to achieve a proper separation of duties, board members serve as treasurer and clerk.	<input type="checkbox"/>
8. The board approves a staffing policy that defines the responsibilities of all those who handle different aspects of the entity's finances.	<input type="checkbox"/>
9. The board is solely responsible for hiring and directing the audit function.	<input type="checkbox"/>

<b>Internal Controls</b>	
See report pages 28 to 33.	
10. The board approves policies that govern the organization and addresses each best practice described in the best practice audit. This would include policies such as a personnel policy, a procurement policy, and records retention policy. A procurement policy is of particular importance with the recent instances of fraud, waste, and abuse that have occurred.	<input type="checkbox"/>
11. The board regularly reviews a report of entity disbursements. The report includes the date, vendor and amount of each expense since the last board meeting.	<input type="checkbox"/>
12. To control credit purchases, purchase cards (or "p-cards") are issued to a limited number of staff. Limits are placed on the dollar amount, type and number of charges made to each card.	<input type="checkbox"/>
13. An independent person with no book keeping responsibilities is assigned to reconcile the bank statement each month with that month's receipts and expenses.	<input type="checkbox"/>

<b>14.</b> The board requires its formal approval of any expenditure above a certain dollar amount.	<input type="checkbox"/>
<b>15.</b> The board requires that two people sign all local entity checks. Before signing, both signers will review and approve the attached requisition sheet.	<input type="checkbox"/>

<b>Recruiting Qualified Personnel</b> Report pages 33 to 37.	
<b>16.</b> Staff avoid recruiting individuals to serve as board members	<input type="checkbox"/>
<b>17.</b> Local entities publicize the opportunity to apply for any elected board seats that will soon be coming available.	<input type="checkbox"/>
<b>18.</b> Local entities follow an open and objective recruiting process when filling staff positions and hiring outside contractors. Hiring relatives or business associates of the board and management is avoided.	<input type="checkbox"/>
<b>19.</b> Board and staff regularly receive the required training in open and public meetings, board governance and other matters applicable to the entity's mission.	<input type="checkbox"/>
<b>20.</b> When in-house expertise is not available to perform special tasks, the entity hires or appoints qualified outside experts.	<input type="checkbox"/>

<b>Tone at the Top</b> Report pages 38 to 40.	
<b>21.</b> The board adopts a code of ethics that clearly states the organization's values and standards of behavior.	<input type="checkbox"/>
<b>22.</b> The board and management seek opportunities to reinforce the organization's ethical standards during staff meetings, training, and newsletters.	<input type="checkbox"/>
<b>23.</b> The board holds everyone accountable, including management, to high standards of performance.	<input type="checkbox"/>
<b>24.</b> The board and executive director avoid using a compensation system and other incentives that encourage employees to take unnecessary risks.	<input type="checkbox"/>
<b>25.</b> The board provides an ethics hotline and adopts a whistleblower policy.	<input type="checkbox"/>



# REPORT TO THE UTAH LEGISLATURE

Report No. 2017-05

## **A Review of Best Practices for Internal Control of Limited Purpose Entities**

June 2017

Audit Performed By:

Audit Manager      Kade Minchey

Audit Supervisor    James Behunin

Audit Staff          Zackery King



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# Chapter I

## Introduction

Many Utahns may be surprised to learn that some public services, such as sewer, water, and fire protection, are not provided by their city or county governments but rather by separate government entities or districts that provide just one or two services. Since so little is known about them, these public entities are sometimes called “ghost governments<sup>1</sup>.” In this report we refer to them as limited purpose entities. In Utah there are nearly 500 such entities that together collect taxes and fees of roughly \$3.5 billion each year.

Because they tend to operate behind the scenes, many limited purpose entities do not receive the same level of public scrutiny as city, county and state agencies. The lack of scrutiny may help explain the many recent reports of fraud, waste and abuse among these agencies. To prevent further misuse of public funds, the Office of the Legislative Auditor General has been asked to examine the internal controls used by Utah’s limited purpose entities and suggest ways to strengthen the oversight they receive.

### Utah Law Allows for Creation of Different Types of Limited Purpose Entities

Also called quasi-governmental agencies, limited purpose entities include the following:

- Special service districts,
- Interlocal entities,
- Local districts,
- Independent entities,
- Some governmental nonprofit organizations.

Each entity has a unique set of characteristics defined in state law. The following material describes each type, from least independent to most independent.

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<sup>1</sup> Adam H. Edelen, Kentucky’s Auditor of Public Accounts, may have been the first to give this label to limited purpose entities in his report Ghost Government: A Report on Special Districts in Kentucky, November 14, 2012.

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**Many limited purpose entities do not receive the same level of public scrutiny as cities and county government agencies.**

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**Cities and counties create special service districts to provide a specific service in their jurisdictions.**

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**Special Service Districts.** Cities and counties create special service districts to provide specific services in their jurisdictions. Each special service district has its own board of directors, although in many cases that board is comprised of the members of the county commission or city council that created it. Special service districts are mainly funded through service fees but some also rely on local property taxes. They also have the power of eminent domain. Special service districts differ from local districts in that they are more linked to the creating governing body and are limited in their ability to make certain policy decisions, such as whether to raise taxes.

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**Figure 1.1 Examples of Special Service Districts.** Special service districts are separate governmental entities created by counties, cities and other local agencies to meet a specific public need such as sewer, water or fire protection services.

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- Alta Canyon Recreation Special Service District
- Cache County Roads Special Service District
- Clinton Sanitary Sewer Special Service District
- Park City Fire Special Service District
- Timberline Water Special Service District

---

**An interlocal entity can be created by a group of local agencies to serve residents across multiple jurisdictions.**

---

**Interlocal Entities.** Interlocal entities are created through cooperative agreements between multiple governmental entities. Interlocal entities' governing boards are typically appointed by and are accountable to the government agencies they serve. For example, the South Valley Water Reclamation Facility is an interlocal entity that operates a sewage treatment facility serving two cities and three sewer districts in South Salt Lake County. The board is comprised of representatives of each member agency. Interlocal entities do not have independent taxing authority but do have authority to enter contracts, incur debt, and purchase property.

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**Figure 1.2 Examples of Interlocal Entities.** To provide public services across multiple jurisdictions, one or more public agencies may create a separate entity called an interlocal entity.

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- Ashley Valley Sewer Management Board
- Grand Water and Sewer Service Agency
- Sanpete Sanitary Landfill COOP
- Unified Police Department
- Utah Telecommunication Open Infrastructure Agency

**Local Districts.** Local districts are autonomous political subdivisions of the state, or political bodies. As independent public entities, local districts have the power of eminent domain and can raise tax rates. Local districts can only be created by a vote of the citizens in the service area which may cut across multiple county and city boundaries. Typically, local districts have elected boards, but may also have some or all of its board members appointed by constituent city or county governments.

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**Local districts are created by a group of citizens, forming a separate government apart from the local city or county.**

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**Figure 1.3 Examples of Local Districts.** Statute describes local districts as “quasi-municipal corporations.” Local districts are separate, independent governmental entities of the state.

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- Hatch Cemetery Maintenance District
- Millard County Fire District
- South Davis Sewer Improvement District
- Utah Transit Authority
- Washington County Water Conservancy District

**Independent Entities.** Independent entities are unique in that they are governmental agencies that are specifically established in statute to meet a specific statewide need. Each has its own source of funding, typically a service fee. Each independent entity has its own board of directors, most of whom are appointed by the governor, while others represent specific constituent groups as designated in statute.

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**Independent entities are created through legislation to address a specific state need.**

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**Figure 1.4 Examples of Independent Entities.** Unlike special service districts and interlocal entities, which are created by local municipalities to address a local need, independent entities are created by the state to address a general public need.

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- Heber Valley Railroad Authority
- Utah Communications Authority
- Utah Dairy Commission
- Utah State Fair Corporation
- Utah State Retirement Office

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**Public, not for profit organizations are usually created by a state or local agency to meet a specific public need through private donations and grants.**

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**Governmental Nonprofit Organizations.** These legal entities provide special public services and are usually created by a state or local agency to meet a specific need. Funding may come from contracts with public agencies, private donations and grants. For example, communities have created nonprofit foundations to promote art, local history, or economic development. Many school districts and colleges have also created nonprofit foundations that provide support services to their schools and students. We are uncertain how many such entities exist in Utah but have identified about 270.

Utah Code 11-13a-102 requires that these entities comply with the state's public disclosure laws, such as the GRAMA Act and the Open and Public Meetings Act if they meet one of two conditions. They must either have (1) one or more public agencies with a controlling interest in the nonprofit entity, or (2) most the entity's funding comes from public sources.

Other types of nonprofit entities are also a concern. Although governmental nonprofit entities may be created by public agencies, not all of them are controlled by their sponsoring public agency. Some are overseen by a board comprised of the agency's constituents and their main source of funding is outside grants and private donations. Even so, these government sponsored entities face the risk for fraud, waste and abuse as do other types of limited purpose entities.



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**Figure 1.5 Examples of Governmental Nonprofit Entities.** Many local governments, school districts and universities have created governmental nonprofit corporations to provide support to their institutions.

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- Granite Education Foundation
- Highland City Arts Council
- Six County Economic Development District
- Utah High School Activities Association
- Weber State University Foundation

### **Nearly 500 Limited Purpose Entities Expend More Than \$3.5 Billion per Year**

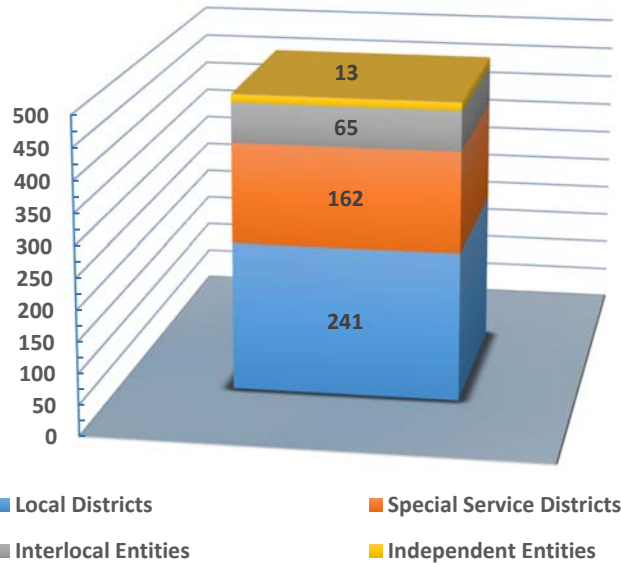
We were unable to determine exactly how many limited purpose entities exist in Utah (discussed more in Chapter IV). Some have not been filing financial statements with the Office of the State Auditor. Some do not receive tax revenue so they aren't known to the State Tax Commission. As a result, we do not know how many limited purpose entities may have avoided detection by the state agencies charged with providing regulatory oversight. We believe the list of agencies maintained by the Office of the State Auditor is perhaps the most complete. This list shows 481 limited service entities in Utah that together spend about \$3.5 billion each year. This information is provided in Figures 1.6 and 1.7.

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**There are nearly 500 limited purpose entities in Utah that spend about \$3.5 billion each year.**

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**Figure 1.6 Estimated Number of Limited Purpose Entities by Type.** The State Auditor has identified 481 limited purpose entities in Utah. About half are local districts.



Source: Office of the State Auditor

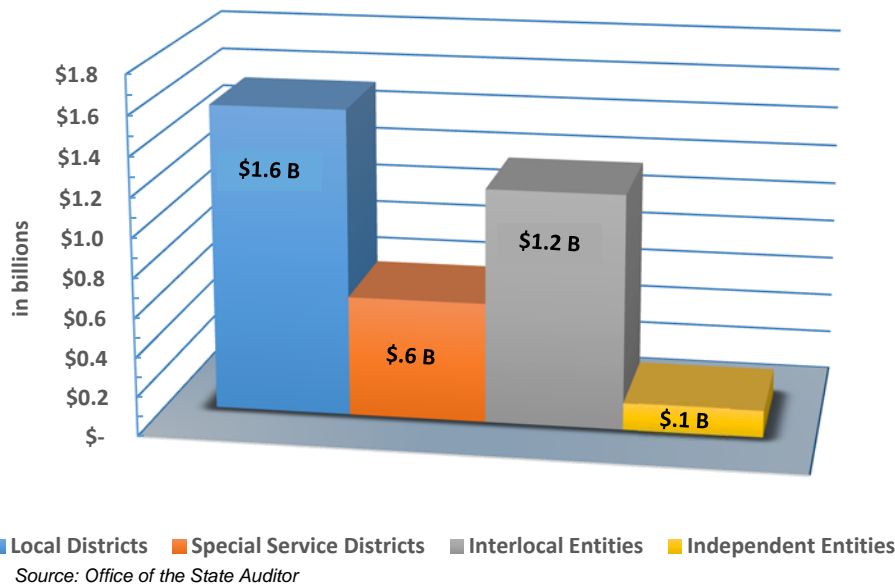
About half of all limited purpose entities are local districts which operate independently of other local governments.

About 50 percent of all limited purpose entities in Utah are local districts (blue). Special service districts (orange) make up about 34 percent, interlocal entities (grey) represent about 13 percent, and independent entities (yellow) are 3 percent of all limited purpose service entities in Utah. Reports provided by the Lieutenant Governor’s office, the Tax Commission, and county governments show there are at least another 101 entities not appearing on the State Auditor’s list.

Figure 1.6 also does not include governmental nonprofit entities because currently no reliable method exists to identify them. Based on our review of the nonprofit corporations registered with the Utah Department of Commerce, about 270 such entities are sponsored by or are closely affiliated with a public agency.

Utah’s limited purpose entities also spend a substantial amount of public funds that are mainly generated through tax dollars or direct service fees. As shown in Figure 1.7, total annual expenditures by limited purpose entities are about \$3.5 billion.

**Figure 1.7. Estimated Dollars Spent by Entity Type.** An estimated \$3.5 billion dollars are expended by limited purpose entities in Utah.



Approximately \$1.56 billion is expended by local districts (blue) per year, or about 45 percent of all estimated expenditures for limited purpose entities statewide. Special service districts (orange) spend about \$611 million per year, or about 17 percent of total spending. Interlocal entities (grey) spend \$1.19 billion annually, or about 34 percent of total estimated funds. Independent entities (yellow) spend \$137 million per year, or about 4 percent of statewide spending by limited service entities.

### Scope and Objectives

We were asked to review the level of oversight provided to governmental entities that are collectively described as limited purpose entities. The concern is that the hidden nature of these entities has allowed most of them to avoid public scrutiny that cities and counties receive. We were asked to examine the management controls used by a sample of these entities and, based on our results, identify best practices currently in use. Our objective has been to provide a list of best practices to limited purpose entities' governing boards and general managers for their consideration as methods to strengthen oversight and reduce the risk of fraud, waste, and abuse.

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**Limited purpose entities receive most of their funding through property taxes and service fees.**

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**Our goal is to provide a list of best practices that can be considered by the governing board of each limited purpose entity.**

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Chapter II summarizes the problems described in past audits of limited purpose entities and describes the results of our recent review of 27 entities. Chapter III provides a list of best practices for boards and general managers to consider. Chapter IV identifies additional best practices that the Legislature should consider to strengthen state and county oversight of these entities.

## **Chapter II**

# **Review of 27 Entities Confirms Concerns in Past Reports**

In recent years, there has been a growing concern for the frequent reports of fraud, waste and abuse among Utah's local districts, special service districts and other, limited purpose governmental entities. These reports, issued by the Legislative Auditor General and the State Auditor, attribute the misuse of funds to weak management controls and poor board oversight. To determine how widespread the problems might be, we surveyed 27 limited purpose entities from throughout the state and concluded that poor governance and weak oversight are fairly common among these local government entities. Of the 27 entities reviewed, we found:

- 16 had missing or weak internal controls.
- 12 had a board or staff, or both lacking the qualifications and training necessary to protect against fraud, waste and abuse.
- 17 show a weak commitment to control and accountability.

Unless improvements are made, we believe many of Utah's limited purpose entities will continue to face a high risk of fraud, waste, abuse and poor management.

### **Reports of Fraud, Waste and Abuse have Raised Concern about Board Oversight**

During the last three years the Legislative Auditor General and the State Auditor have conducted 20 audits of limited purpose entities. Of those, eight reports describe cases of fraud, waste and abuse of public funds. Another twelve describe instances of weak controls, and poor policies and procedures. Nearly every report concluded that improvements in board governance was needed.

### **Recent Reports Attribute Problems to Weak Internal Controls and a Lack of Board Oversight**

In recent years there have been eight reports of fraud, waste and abuse of public funds among limited purpose entities in Utah. The

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**During the past two years, eight audit reports described instances of fraud, waste and abuse of public funds.**

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audits described below were conducted at seven limited purpose entities and one governmental nonprofit corporation. Each report raises concern about the ability of the board of directors to maintain control over their organization.

**Figure 2.1 Recent Audits Describe Instances of Fraud, Waste and Abuse.** Since May 2015 the Legislative Auditor General and the State Auditor have issued eight reports describing cases in which funds have been used inappropriately.

**Past reports often attributed the misuse of funds to weak management controls and poor board oversight.**

<b>Mapleton Irrigation District</b>	<b>May 2015</b>
<ul style="list-style-type: none"> <li>• "Finance officer stole between \$103,093 and \$116,797... by issuing checks to herself as the payee, ...to a company she owns ... [and] to her credit card company for payments on her personal credit card... ."</li> </ul>	
<b>East Duchesne Water District</b>	<b>December 2015</b>
<ul style="list-style-type: none"> <li>• "The district must address a conflict of interest... . Specifically, the district's manager-secretary does most of the district's construction work himself. Because he is also a private contractor, he leases his own personal equipment to the district at a predetermined rate."</li> </ul>	
<b>Southwest Utah Public Health Department</b>	<b>March 2016</b>
<ul style="list-style-type: none"> <li>• "The Department employees who are Foundation Board members transferred [department] funds to the Foundation without the Department Board's knowledge."</li> <li>• "Funds [were] transferred from Department to foundation in ...an attempt to circumvent fund balance limitations found in Utah Code 11-13-512."</li> </ul>	
<b>Utah Local Government Trust</b>	<b>July 2016</b>
<ul style="list-style-type: none"> <li>• "Questionable expenditures for the Board [included] ...iPads ...golf ...a professional baseball game, ... food and entertainment... ."</li> <li>• "Excessive per diem expenditures."</li> <li>• "Improper gifts to local government officials and employees"</li> <li>• "Excessive CEO compensation ...of \$432,231."</li> </ul>	
<b>Utah Communications Authority</b>	<b>August 2016</b>
<ul style="list-style-type: none"> <li>• "...over \$800,000 of purchases using UCA credit cards for personal use [were attributed to] ...internal control weaknesses in multiple areas" ... ."</li> </ul>	
<b>Economic Development Corporation of Utah (EDCUtah)</b>	<b>October 2016</b>
<ul style="list-style-type: none"> <li>• "... improper credit card transactions ...were made by a former EDCU executive... ."</li> <li>• "Poor financial management led to revocation of the entity's tax-exempt status."</li> </ul>	
<b>Unified Fire Service Area</b>	<b>January 2017</b>
<ul style="list-style-type: none"> <li>• "Illegal actions resulted in improper incentive award payments."</li> <li>• "...two former board members unilaterally "approved" \$81,000 in incentives for the former UFA Chief ... ."</li> <li>• "... the former clerk received incentive awards totaling \$22,000."</li> </ul>	
<b>Utah League of Cities and Towns (ULCT)</b>	<b>January 2017</b>
<ul style="list-style-type: none"> <li>• "Former CFO embezzled ULCT funds by charging personal expenses to a ULCT credit card."</li> <li>• "Various personal expenses were improperly charged to the director's ULCT credit card."</li> </ul>	

The Government Accountability Office defines fraud as an illegal act of obtaining something of value through deception. Waste is the inefficient use of public funds, usually due to mismanagement, but not as the result of an illegal act. Abuse is defined as the improper use or misuse of authority or position, especially when it benefits one's personal interests or those of a friend or family. Abuse does not necessarily involve violation of law. The recent audits have raised concern for the frequency with which fraud, waste and abuse have been reported.

**Other Audits Have Identified Weak Board Oversight and Missing Internal Controls**

In addition to the eight audits describing fraud, waste and abuse, another 12 audit reports described the need for improved board oversight and management controls. Figure 2.2 describes the major findings in four reports.

**Figure 2.2 Four Examples of Audit Reports Describing Weak Oversight and Missing Internal Controls.** During the past three years, 12 audit reports raised concern about the oversight and management of limited purpose entities. Four examples are shown.

<b>Kane County Recreation &amp; Transportation SSD</b>	<b>April 2017</b>
<ul style="list-style-type: none"> <li>• "Excessive compensation for board members"</li> <li>• "the R&amp;T Board hired the wife of a board member to serve as R&amp;T's secretary... ."</li> <li>• "Failure to adopt a purchasing policy"</li> </ul>	
<b>Utah High School Activities Association (UHSAA)</b>	<b>February 2014</b>
<ul style="list-style-type: none"> <li>• "UHSAA's current policy handbook is vague and lacks details concerning the overall classification process."</li> </ul>	
<b>The Utah Fund of Funds</b>	<b>August 2014</b>
<ul style="list-style-type: none"> <li>• "Overreported its economic impact"</li> <li>• Included inconsistent job creation and tax revenue information in its annual reports"</li> </ul>	
<b>Weber-Box Elder Conservation District</b>	<b>November 2015</b>
<ul style="list-style-type: none"> <li>• "District failed to effectively evaluate and identify its reservoir as the most likely cause for flooding [of nearby homes]"</li> </ul>	

Although the problems described in these reports are less serious than fraud, they do raise concerns about weak board governance and poor management controls.

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**Fraud is an illegal act of obtaining something of value through deception.**

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**Waste is when public funds are used in an inefficient manner, usually due to mismanagement.**

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**Abuse is a term used to describe improper or misuse of authority or position.**

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**In addition to the 8 audit reports describing fraud, waste and abuse, 12 audits reported weak oversight of limited purpose entities.**

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## **Lack of Oversight and Management Control Are Common Themes in All 20 Past Audits**

The common underlying causes for the problems detailed in the past 20 audits of limited purpose entities are poor governance and poor management control. Some specific governance and management control issues described in these reports are listed in Figure 2.3.

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**Figure 2.3. Past Audits of Limited Purpose Entities Often Described Similar Problems.** The most common problems found in our review of the past 20 audits of limited purpose entities are shown in order of frequency.

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**Past audits of limited purpose entities have uncovered some consistent themes.**

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- 1) Weak transparency and accountability
- 2) Weak board oversight and control
- 3) Lack of adequate planning, policies and procedures
- 4) Lack of adequate accounting and financial controls
- 5) Lack of in-depth and regular cost analysis to aide management in decision making
- 6) Lack of adequate training and understanding of applicable laws
- 7) Questionable expenditures by board and/or management

Each of the above concerns can be attributed to a lack of effective governance. Ultimately, it is the board of directors who is responsible to ensure these items are addressed.

## **Most Entities in a Recent Survey Need Stronger Oversight and Internal Controls**

We conducted a survey of internal controls used by 27 limited purpose entities. We found 21 with at least some internal control weaknesses leading to the conclusion that a majority of limited purpose entities in the state can improve their oversight and internal controls. Unless corrective action is taken in these areas, we believe Utah's limited purpose entities will continue to face a serious risk for fraud and mismanagement.



## **We Examined Oversight and Controls at 27 Limited Purpose Entities**

Our limited review focused on the internal control systems used by 27 limited purpose entities in 12 counties. The sample included small, medium, and large entities, in rural and urban areas, offering different services such as animal control, culinary water, fire protection, and waste management.

The objective of our survey was to answer three questions:

1. Did the organization have adequate internal controls?
2. Did the organization have personnel qualified to carry out those controls?
3. Did the organizational culture support good accountability and control or did they disregard the importance of sound internal controls?

To answer these questions, we attended meetings of the board of directors to observe the interaction between board and staff. We also interviewed board members and key staff. Finally, we reviewed any written policies, procedures and other internal documents the entity could provide.

Although we found several well-run organizations, our overall conclusion is that 21 of the 27 entities studied had some degree of weakness in at least one of the three areas. Some had weak or missing control procedures, some lacked qualified personnel, and some organizations showed a lack of commitment to following the state's transparency laws and to maintaining strong oversight and control. We found nine entities with weaknesses in all three areas. Figure 2.4 summarizes our findings:

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**Our survey of 27 limited purpose entities showed that most entities were at risk for the same type of fraud, waste and abuse as described in past audit reports.**

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Most surveyed entities had weak internal controls, poorly qualified personnel or an organizational culture weak on accountability and control.

**Figure 2.4 Results of Our Review of 27 Limited Purpose Entities.** 16 entities were found to have weak internal controls, 13 lacked personnel with the necessary training and qualifications, and 17 showed a weak commitment to controls and accountability.

Of 27 Entities* in the Survey Sample:	
<b>16</b>	<b>Entities had Weak or Missing Internal Controls</b> <ul style="list-style-type: none"><li>• Poor separation of duties, or</li><li>• Board did not monitor finances, or</li><li>• No board-approved policies and procedures.</li></ul>
<b>13</b>	<b>Entities had Board and Staff Lacking the Needed Training and/or Qualifications</b> <ul style="list-style-type: none"><li>• Board and staff lacked members with a background in management, finance and accounting, or</li><li>• Board members had not received the required training.</li></ul>
<b>17</b>	<b>Entities Showed Weak Commitment to Control and Accountability</b> <ul style="list-style-type: none"><li>• Board showed reluctance to ask executive director challenging questions, or</li><li>• Board and staff showed sidestepped state requirements for limited purpose entities, such as the public notice and open meetings requirements.</li></ul>

\*Eight entities were weak in all three areas, the others in one or two areas.

The following describes some of the most common weaknesses found.

### **Sixteen Limited Purpose Entities Need Better Management Controls**

We asked each entity to describe some of the internal controls used to protect assets, to accomplish its goals and comply with the law. We found that 16 of the 27 entities in our study (59 percent) had missing or weak internal controls.

**Poor Separation of Duties is a Common Problem.** Segregation of financial duties is widely recognized as a crucial internal control. Our survey found that 14 of 27 entities had a poor separation of duties. The employee who prepares bank deposits should not be the person who reconciles the bank statement. In fact, state law requires that each local and special district board designate one person to serve as the treasurer and another to serve as the bookkeeper or clerk. But merely appointing two people to fill those positions may not be sufficient. The board needs to make sure that the staff assignments are

To reduce the risk of fraud, entities should make sure no single employee has control over all parts of a financial transaction.

segregated to the point that no one individual has so much control over the finances that they can defraud the organization.

The following are four examples:

- One independent entity reported that all financial tasks were handled by one part-time accounting clerk. This employee counted the cash in the register, prepared and made deposits, wrote checks, reconciled the bank statement, and kept the books.
- A sewer and water district in one rural community had one administrative staff person who handled all accounting and finance tasks. Her duties included those of both clerk and treasurer.
- The treasurer/bookkeeper for a rural fire district is the wife of the fire chief. This relationship raises concern about the clerk's ability to independently provide adequate financial controls.

**Boards Do Not Monitor Entity Finances.** Boards should periodically review individual expenditures to verify that they are appropriate and consistent with the approved budget. Most entities provide the board with a list of disbursements each month. However, six boards did not receive this information on a regular basis. For example:

- A recreation district in Salt Lake County reported that the board received a general summary statement of the quarterly expenses but is not asked to review a list of individual disbursements.
- The general manager of a mosquito abatement district said he did not normally give the board a chance to review the list of disbursements, but he would provide that information if they asked for it.

**Nine Entities Lacked Board-Approved Policies and Procedures.** One primary way a board can provide guidance is by approving a formal set of policies and procedures. In fact, state law requires boards to adopt policies regarding procurement, personnel, and the Government Records Access Management Act (GRAMA). We identified eight entities for which the boards had not established

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**Some boards can provide better oversight by periodically reviewing a list of recent disbursements.**

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**By drafting a set of formal policies, the board can give direction and improve its control of an agency.**

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policies in all the required areas. Some entities said they had drafted policies but could not locate them. Two examples follow.

- When we asked a sewer district in Salt Lake County if we could review their board approved policies, they said they didn't have a formal set of policies they could show us. If they ever had a need to find out what policies might have been approved, they said they would need to review their past board meeting minutes.
- Board members of a small water and sewer district said they did not think they needed formal policies because they only had one employee.

### **Thirteen Entities Lack Qualified Board and Staff**

A limited purpose entity may have the required internal controls in place, but still be at risk if staff and board members lack the training and expertise needed to implement those controls. Of the 27 surveyed entities, six did not have a single board member with any training or experience in governance, finance or accounting. We also found that 11 of the 27 had at least some members who had not completed the required board training. Finally, we found some entities whose staff, in our opinion, did not possess the training or qualifications necessary to implement the organization's internal controls.

**Boards Lack Members with Governance, Finance and Accounting Background.** Utah's limited purpose entities provide critical public services. Each board of trustees is responsible to oversee the use of public funds and to safeguard public resources. Ideally, each board of trustees should have at least some members with training and experience in governance, finance and accounting. However, we found that some entities lack board members with training or experience in these areas. This lack of expertise may explain why some boards have difficulty providing strong oversight and control over their entities.

**Entities have difficulty finding qualified people willing to serve on the board.** One reason some entities suffer from weak oversight is that they struggle to find anyone willing to serve on the board. During our review of 27 limited purpose entities, we asked board members whether they were elected or appointed to their positions. Many told us that although their seats are elected positions, they did not participate in an election because there were only as many candidates

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**Ideally, each board should have at least a few individuals who understand the basic principles of accountability and internal control.**

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**Some limited purpose entities find it difficult to find qualified people willing to serve on the board.**

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as there were available seats. Some also told us that the district's executive director invited them to sit on the board. The lack of candidates, and the need for executive directors to recruit board members, raises concern about the board's level of accountability to the public and further perpetuates the "hidden government" or "ghost government" stigma surrounding limited purpose entities. Some examples follow:

- The board of a water and sewer district in northern Utah reported that in the past twelve years, they had twelve different people serve on its three-member board. A recently vacated board seat was just recently filled after district's only employee went door to door asking people if they might be willing to serve on the district board. In our view, the lack of a stable and qualified board is the cause for many of the district's current challenges.
- After it was discovered that all three board members of a water and sewer district were all found to be non-residents and therefore not eligible to serve, the county commission had to find individuals willing to serve on the board. Eventually, the three commissioners appointed themselves "temporarily" with two other local residents to form a new five-member board. After having served for more than one year, the commissioners still have not found individuals in the local district who are both qualified and willing to serve on the board.

**Staff Are Poorly Qualified to Implement the Entity's Internal Controls.** We found some local districts and interlocal entities staffed by individuals who are not well qualified to operate an independent public agency. In our view, their limited knowledge of management controls, budgeting, and accountability is the primary reason the entity is not using best practices for avoiding fraud, waste, and abuse.

- We visited an independent entity whose director had a great deal of marketing experience but no public-sector experience. While successful at increasing the entity's customer base and revenues, the director is not using many basic internal controls to protect against fraud, waste and abuse.
- A troubled water and sewer district decided to replace its treasurer/clerk. She had failed to keep proper records and had not been submitting the required reports to the state and

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**Some limited purpose entities are also at risk because they do not have staff who understand organizational controls and accountability.**

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**One solution to the lack of qualified board and staff is to require that they participate in the many training opportunities that are available.**

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federal agencies. The CPA tasked with rectifying the financial records told us he could not reconstruct past account balances because of the records' poor condition. Based on the CPA's assessment, we question whether the former treasurer/clerk was qualified to keep the district's books.

**Many Boards Members Have Not Received Required Training.** It would be unreasonable to expect everyone serving on a local board to have expertise in accounting and internal controls. This is why state law requires newly elected or appointed board members to participate in a special training course. State law also requires annual training in the Open and Public Meetings Act. The Utah Association of Special Districts (UASD) has an annual conference where this training can be obtained. When requested, the UASD and the state auditor will also conduct local training events.

At 12 of the 24 limited purpose entities in our survey sample (3 were governmental nonprofits), we found one or more board members who had not received all required training. Some were unaware of the training requirements while others knew but neglected to comply. All board members need this training. Some examples follow:

- The board members of a rural fire district said they did not know training was required and were surprised to learn that it is available on-line.
- We asked the board members of a recreation district if any had received the new board member training. One board member immediately produced the certificate she received upon completing the on-line training. However, there were other board members who did not even know there was a training requirement.
- The general manager at one local district told us they don't attend the Utah Association of Special Districts Conference (UASD) because it was too expensive, and that they disliked the on-line training provided by the State Auditor because it was "too simple" and "not informative."
- We were told three sewer district board members refused to participate in the required training. Their lack of training

became evident during a board meeting when one member asked if there is a legal limit on a size of the district's fund balance, a topic often covered at the UASD's annual conference. Apparently, the general manager also did not know the correct answer. He incorrectly told the board there was no legal limit on the size of the district's fund balance.

### **Some Entities' Organizational Culture Does Not Support Internal Control and Accountability**

Although some organizations have strong internal controls and highly qualified staff, they may still be at risk if the organization's culture does not support good governance and accountability. For this reason, we tried to gage the level of each entity's commitment to good governance. Of the 27 entities in our survey, 17 (63 percent) demonstrated some lack of commitment to proper accountability and control.

To assess each entity's organizational culture, we considered the questions that introduce the following discussions.

**Is the Entity Committed to Following Statutory Requirements Governing Limited Purpose Entities?** We found that a fair number of entities are not complying with the state laws governing transparency and financial management. For example, 7 of the 27 entities in our survey did not give the required notice of meetings on the Utah Public Notice website. Another seven did not file annual financial statements within the 180-day requirement. We observed four boards that appeared to be conducting some of their business in a private setting, contrary to the intent of the state's open and public meetings laws. Four entities had fund balances that exceeded statutory limits. Noncompliance in these areas sends the message to staff that it is not always necessary to comply with the rules. The following are three additional examples:

- We attended a special district board meeting at which the board approved the use of \$100,000 to refurbish the county courthouse. That action was concerning because its purpose was not among those included in the district's charter.
- One local district holds regular committee meetings of the board to discuss sensitive matters away from public view. They believe the meetings can be closed to the public because the

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**Some limited purpose entities' actions have led us to question whether their organizational culture supports accountability and control.**

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**By not following state laws governing limited purpose entities, some boards may be sending the message to staff that it is not always necessary to comply with the rules.**

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**Some boards demonstrate a rather passive attitude towards their oversight role, giving too much deference to the executive director.**

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committees do not comprise a quorum of the full board. Even if not technically a violation, such meetings violate the intent of Utah's Open and Public Meetings Act that public entities "conduct their deliberations openly."

- During a water and sewer district board meeting, we observed the board turned off the recording device to allow an "off the record" discussion about certain information they did not want the community to hear.

**Is the Board Fulfilling Its Oversight Responsibility?** The quality of board oversight is one of the more difficult internal controls to measure and evaluate. It is one of the "soft" controls that, according to the Institute of Internal Auditors, requires auditors rely more on observation and interviews than other auditing methods that produce quantifiable data.

Our approach was to observe the interaction between the board and staff during board meetings, to interview board members regarding their responsibilities and to review meeting minutes, agendas and board policies. Based on our interviews and observations, some boards demonstrated a rather passive attitude towards their oversight role, giving too much deference to the executive director. They seem to assume it was the director's job, not theirs, to make sure the organization is well managed and uses proper internal controls. Some examples follow.

- During a board meeting of a mosquito abatement district, we observed a rather passive board that hardly said anything during the meeting. The entire time was taken up by the executive director instructing the board. Unlike other boards we observed, this board did not engage in a healthy back and forth discussion of important matters facing the district. The board simply seemed disengaged.
- One water district has no staff other than a part time clerk. Instead the district operations are handled by employees of the public works department of the city it serves. The chairman of the district board seemed overly deferential to the city's public works director. The chair said he relies on the public works director to tell him what to do.



## **Limited Purpose Entities Need to Strengthen Oversight and Management Controls**

Based on our study of 27 limited purpose entities, we have concluded that the problems with weak board oversight and poor management controls are not limited to those entities that have been audited in the past. Instead, our study suggests there is a widespread need for these entities to strengthen internal controls. Chapter III, describes some best practices for good governance and accountability. We believe that by adopting these practices limited purpose entities can reduce the likelihood they will face fraud, waste and abuse others have experienced in recent years.

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**Our review suggests the problems with weak board oversight are widespread and that most limited purpose entities need to strengthen their internal controls.**

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## **Chapter III**

# **Boards Should Adopt and Implement the Best Practices for Internal Control**

As discussed in Chapter II, due to recent cases of fraud, waste, abuse and mismanagement, we recommend that each governing board evaluate its organization's internal controls. We believe the board must take the lead because they are ultimately responsible for the success of their organizations. If they leave it to others to maintain control, they may be putting their organizations at risk. Specifically, we recommend each board consider the following four key requirements of an effective system of internal controls:

- (1) The board, executive and staff need to understand and perform their unique roles,
- (2) Each entity needs to adopt a complete set of internal control procedures,
- (3) The board and staff need to be qualified and receive ongoing training,
- (4) The board and executive director need to set a proper tone of accountability and ethical behavior.

This chapter describes some of the specific best practices that can be used to develop each the above four areas. A checklist of these best practices can be found in Appendix A.

### **The Board, Executive and Staff Need to Understand and Perform Their Unique Roles**

The board, executive director and line staff each play an important role in maintaining control of an organization. They each represent three separate lines of defense against fraud, waste and abuse. If one of those lines of defense fails, it weakens the defense system and puts the organization at risk. The following describes each of their roles.

#### **The Board Must Govern**

An effective, engaged board is one of the most important lines of defense against fraud, waste and abuse. Boards govern effectively when they provide clear policy guidance and hold staff accountable for

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**The board, executive director and staff represent three separate lines of defense against fraud, waste and abuse.**

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results. The design and use of the organization's internal controls is one area in which each board should develop policies and monitor performance. This responsibility cannot be delegated to staff. The following are some of the best practices each board should consider:

**Board Members Must Recognize that they are the Ones Who are Ultimately Accountable for an Organization's Success.** Often, when public agencies have become victims of fraud, waste and abuse, we have found a passive, disengaged board of trustees. While the executive director and staff perform critical roles, the statute clearly states that the board is ultimately accountable for the success of the organization. *Utah Code* 17B-1-301 enables each board of directors of a local district to "exercise all powers...necessary to accomplish the purposes of the district." Similar powers are normally given to the boards of interlocal entities and independent entities when they are created. Special district boards may be given similar powers as well, but at the discretion of the governing body creating the district.

**The Board Must be More than Just a Ceremonial Body.** To be an effective governing body, a board of trustees needs to do more than simply perform a ceremonial role. Too often we have encountered boards that act as if it's their job to be cheerleaders of the organization and its staff. To show their support they tend to rubber-stamp staff decisions. In our view, these "cheerleader" boards risk losing control of their organizations. Instead, the board needs to establish high expectations, ask hard questions of staff and hold them accountable for results.

**The Board Chair sets the Agenda.** One indicator that the board is in charge is that the board chair takes responsibility for setting meeting agendas. If staff set the board meeting agenda, too much time can be spent addressing the more immediate concerns of staff rather than the board's need to establish long term goals, draft policies and to monitor results. Certainly, staff should be asked to propose agenda items, but before a meeting agenda is posted, the chair should prioritize agenda items and allow other board members to add any items they may want to discuss.

**The Governing Board Focuses its Attention on its Core Functions.** An effective governing board focuses its efforts on five responsibilities: (1) hiring an executive director, (2) providing broad policy guidance, (3) overseeing the use of financial resources, (4)

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**Boards that view themselves as cheerleaders for staff risk losing control of their organization.**

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setting goals and expectations, and (5) monitoring results. To the extent they perform these tasks effectively, the board can provide an organization with the broad guidance it needs to control its use of funds and accomplish its goals.

A water and sewer district in Salt Lake County may be the best example we found of a board and staff who know their roles and work effectively together. Even though the district has a capable executive director and a highly trained staff, they don't dominate the board. Although the board might feel justified in deferring most decisions to their capable staff, we found that the board demands a regular reporting on the use of funds and on the progress made in achieving its operational goals. At the same time, the board gives the executive director enough space to do his job.

### **The Executive Director Carries out the Board's Policies**

A second line of defense is provided by an executive director who helps the board draft a set of internal controls and then implements the internal controls once they have been approved. It should always be clear that the executive director works for the board, and carries out its policies, not the other way around. The following describes the best practices that executive directors should consider:

**The Executive Director May Draft Internal Control Policies for the Board to Consider.** Although the policy making function belongs to the board, the executive director can support the board's efforts by identifying policy options the board should consider and then by describing the advantages and disadvantages of specific internal controls. The wording of any policy should be sufficiently broad to give the executive some leeway in deciding how exactly they are to be executed.

**The Executive Director Guides staff as they Carry out the Board's Internal Control Policies.** Once the board approves a set of policies, the executive is responsible for making sure that the policies and goals are carried out using whatever resource limitations placed on him by the board. With regard to internal controls, it is the job of both the executive director and the board to make sure the controls are working as intended.

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**The executive director's main responsibility is to carry out the board's policies.**

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**There should be a segregation of duties such that no employee has so much control over a financial transaction that they have an opportunity to defraud the organization.**

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**Very small districts may choose to have their board members serve as clerk or treasurer.**

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## **Financial Tasks Must be Divided Among Staff**

Another line of defense (some describe it as the first line of defense) is a staff who carry out the entity's internal controls with a high degree of integrity. Two of the most critical staff functions are that of the treasurer and clerk – positions that must be appointed by the board. The following are some of the best practices for making sure staff act as an effective line of defense against fraud, waste and abuse.

**Staff Duties are “Segregated” Such That No One Person Has Control Over All Parts of a Financial Transaction.** To prevent employees from having the opportunity to misuse funds, it is critical that certain financial management tasks be divided among different employees. For example, the person who receives cash payments should not also be asked to prepare a bank deposit. Those responsible for purchasing should not also be assigned to pay the bills.

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### **Figure 3.1 Even Small Entities Can Properly Segregate Duties.**

Although this Water and Sewer Improvement District has just one part time employee and a three-member board, it has still managed to create a proper segregation of duties. One board member is the chair, another is the clerk, and the third is the treasurer. Their only employee makes most of the purchases. The four review all district expenditures each quarter.

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**Board Appoints a Treasurer and Clerk.** Local districts can achieve a separation of duties in part, when the board carries out its statutory duty to appoint a clerk (*Utah code* 17B-1-631(1)) and treasurer (*Utah code* 17B-1-633(1)). Similar requirements are found in the statute applicable to interlocal entities and it makes sense for independent entities and for most special service districts to have separate people performing the role of clerk and treasurer. The following describes the duties of these two officers:

## The Clerk's Duties

- Attend meetings and keep a record of the proceedings
- Maintain financial records.
- Prepare checks after determining that the claim:
  - Was authorized by the board or financial officer,
  - Does not over expend the budget, and
- Present a financial report at least quarterly to the board.
- May not sign a single signature check.

## The Treasurer's Duties:

- Sign checks after determining that sufficient funds are available.
- Maintain custody of all money.
- Deposit and invest all money in accordance with the State Money Management Act.
- Receive all public funds and money payable to the district.
- Keep an accurate, detailed account of all money received.
- Issue a receipt for money received

**Board Adopts a Policy Defining the Responsibilities of the Treasurer and Clerk.** Ideally, the board should adopt a formal policy that creates the positions of treasurer and clerk and describes their specific duties (consistent with the statute above). For example, the policy might specify which staff are authorized to perform tasks such as to authorize payment, sign checks, handle cash and make deposits.

One of the fire districts we visited provides an excellent example of how a board can adopt a set of staff policies directing the proper segregation of duties. Under the direction of the board, the district employees prepared a series of policies describing the separate duties assigned to the treasurer, clerk and other staff who handle the entity's finances. Other policies were adopted describing procedures for handling cash and checks, expenditures and accounts payable, capital expenditures, payroll and fund balance. After the policies were reviewed by the state auditor and the district's outside auditor, they were formally approved by the board as district policy.

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**One of the board's responsibilities is to appoint someone to be the clerk and someone else to be the treasurer.**

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**Internal controls are the policies, procedures, and practices used to make sure an organization achieves its goals and that its resources are protected and used as intended.**

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**The most effective boards, use their policy making authority to direct and control staff activities.**

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## **Each Entity Needs to Adopt a Complete Set of Internal Control Procedures**

Internal controls are defined as the “process ...designed to provide reasonable assurance regarding the achievement of objectives relative to operations, reporting and compliance.” In other words, it includes all the policies, procedures and practices used to help an organization achieve its goals. It is the responsibility of the board of directors to make sure an effective set of internal controls are adopted. Both the board and the executive director are responsible for making sure they are working effectively. The following are some of the best practices currently used by local entities:

### **The Board Adopts a Set of Written Policies**

A minimum, each entity should have a board approved personnel policy, a purchasing policy, and records retention policy. In addition, if they wish to have a meeting conducted remotely through an electronic device, they must have a policy describing how that process must be conducted. A template for such policies can be found at the website of the Utah Association of Special Districts (<http://www.uasd.org/members-area.php>). Some of the better run districts we observed have board policies requiring the use of specific financial management practices such as those described in this chapter. Ideally, the policies should be kept in a format that is readily available to staff or board members wishing to review them.

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### **Figure 3.2 When Asked, Local Districts Should be able to Produce Their Board Policies.**

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A set of board approved policies are of little value if they are not easily accessed. When asked about the district policies, this general manager of a sewer district was able to readily produce them.





## **The Board Reviews the Expense Detail on a Regular Basis**

The board has a duty to regularly review a local entity's finances. One best practice is to periodically allow the board to review a list of recent expenses by vendor and amount. Typically, staff will include this information in the packet of information provided to board members prior to each monthly board meeting. During the board meeting, members are given an opportunity to ask questions regarding any item for which they may have concern. Districts with a large number of expenses each month might also provide a second list showing those expenses exceeding a certain amount, such as \$15,000. Figure 3.3 offers a positive example of a disbursement report given each month to the board of a sewer district in Salt Lake County.

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**The board should be allowed to review past expenses and ask staff to explain any for which they have questions or concerns.**

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**Figure 3.3 A Sewer District in Salt Lake County Provides the Board with a Monthly List of Disbursements.** The figure shows one page from a payment approval report provided to the board each month.

SEWER DISTRICT		Payment Approval Report		Page: 17	
		Report dates: 10/8/2016-11/7/2016		Nov 10, 2016 09:44AM	
Vendor Name	Invoice Number	Description	Amount Paid	Date Paid	
NAPA AUTO PARTS	956325	WHEEL BEARING HUB FOR PU-34	229.38	11/08/2016	
NAPA AUTO PARTS	956325	HEAD LAMP FOR TV-4	9.35	11/08/2016	
Total 5191:			1,240.44		
<b>5231</b>					
NEVEREST EQUIPMENT	2105	VA35050134A EM KILL SWITCH FOR JT-16	141.85	10/26/2016	
NEVEREST EQUIPMENT	2105	SHIPPING & HANDLING	20.00	10/26/2016	
NEVEREST EQUIPMENT	2120	VERISIGHT PRO PUSH CAMERA W/200' CABLE	9,600.00	11/08/2016	
NEVEREST EQUIPMENT	2120	SHIPPING	234.00	11/08/2016	
Total 5231:			9,995.85		
<b>5311</b>					
NORTH DAVIS SEWER DI	2016-033	MERCURY BY FLORESCENCE FB WITH DIG	100.00	11/08/2016	
NORTH DAVIS SEWER DI	2016-033	MERCURY BY FLORESCENCE WITH DIGESTION	100.00	11/08/2016	
Total 5311:			200.00		
<b>5321</b>					
O.C. TANNER	931697821	5 YR SER RECOG JERRY LINDEMAN & GORDON	2,537.80	10/26/2016	
O.C. TANNER	931697821	SHIPPING & HANDLING	32.20	10/26/2016	
O.C. TANNER	931801126	5 YR SERVICE RECOGNITION 8 EMPLOYEES	10,294.28	10/26/2016	
O.C. TANNER	931801126	SHIPPING	111.07	10/26/2016	
Total 5321:			12,975.35		
<b>5341</b>					
OFFICE DEPOT	868887529001	BLACK UNIBALL 207 PENS	16.14	10/17/2016	
OFFICE DEPOT	868887529001	BLACK ENERGEL PENS	27.06	10/17/2016	
OFFICE DEPOT	868887529001	TONER CARTRIDGE MEGHAN	112.46	10/17/2016	
OFFICE DEPOT	868887529001	PUSH PINS	2.97	10/17/2016	
Total 5341:			158.63		
<b>5412</b>					
OPEN AIRE SCREEN PRI	8204	SVSD 2016 UNIFORMS	5,210.29	10/26/2016	
OPEN AIRE SCREEN PRI	8204	JBWRF 2016 UNIFORMS	3,966.05	10/26/2016	
OPEN AIRE SCREEN PRI	8204	PRETREATMENT 2016 UNIFORMS	733.70	10/26/2016	
OPEN AIRE SCREEN PRI	8204	UPCHARGE FOR XXL/XXXL	163.50	10/26/2016	
OPEN AIRE SCREEN PRI	8204	UPCHARGE FOR XXL/XXXL	163.50	10/26/2016	
OPEN AIRE SCREEN PRI	8237	SVSD 2016 UNIFORMS (ALVARO ISEAS ORDER)	145.00	11/08/2016	
OPEN AIRE SCREEN PRI	8237	JBWRF 2016 UNIFORMS (ADD. ORDERS)	64.00	11/08/2016	
Total 5412:			10,446.04		

### Use Purchase Cards instead of Credit Cards

The misuse of entity credit cards has been a common problem in recent years. For this reason, some entities have begun using purchasing cards (or P-Cards) to control credit purchases by employees. P-Cards are obtained through a state contract with US Bank. Many entities have also begun to limit the number of credit

**Entities should control credit card spending by limiting the number of credit cards issued to employees and by requiring receipts to support each purchase.**

cards issued to employees. Of course, any purchase, whether with a credit card, check or cash, should be supported by a receipt.

One advantage of using a P-Card is that limits may be placed on the dollar amount of each card transaction and on the number of transactions per day. The P-Card also allows the account holder to block certain merchant category classification (MCCs) to prevent the card from being used for purchases at unauthorized vendors such as a jewelry store or liquor store.

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**Figure 3.4 A Waste Disposal District in Northern Utah uses P-Cards to Control Expenditures.** The district obtained its P-Cards through a state contract with US Bank.

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Using the P-Cards, a waste disposal district in Northern Utah has placed limits on the amount of each purchase, the type of purchase (no alcohol or jewelry for example) and the total amount charged each month. Also, no cash withdrawals are allowed using the P-card. The receipt for any purchase made on a P-Card must be attached to an authorization form that describes the vendor, the purpose of the purchase and the account to which it must be charged. Monthly P-Card statements are reviewed by the executive director.

### **Reconcile the Bank Statements Each Month**

An independent person with no book keeping responsibilities should review each month's receipts and expenses and then reconcile those amounts to the ending monthly balance recorded in the entity bank statement. It is also good to verify that all checks are accounted for. Each check should either be listed in the bank statement or, if voided, retained on file. A sample of checks should also be reviewed to see if they are made out to appropriate vendors and properly authorized by the procurement officer.

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**Purchase cards can be used to limit the amount and type of purchases as well as the total amount spent during a month.**

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For example, each month, the clerk at a fire district in Northern Utah prepares a reconciliation report showing that the accounting records are reconciled with the bank statements. This document is then provided to the Chief and a board member (who also serves as treasurer) who confirm that the accounting records reconcile with the bank statement.

### **Require Board Approval For any Expenditure Exceeding a Certain Dollar Amount**

Many local entities require staff to obtain formal board approval of expenditure above a certain dollar amount. The purpose of the requirement is to provide an added level of oversight to major expenses. Such expense items are usually presented during a board meeting and authorized through a formal vote of the board. The board might also require staff to provide additional information regarding the purchase so they can weigh the costs and benefits.

Of all the entities we visited, the one with the lowest limit on expenses without board approval is a fire district in Southern Utah. They require board approval for any expenditure exceeding \$1,000. At the high end of the range, a water and sewer district in Salt Lake County allows staff to make purchases of up to \$150,000 without separate board approval. The most common practice is to set the limit at \$50,000, though the limit should reflect the size of the organization and the board's risk tolerance level.

### **Require Two Signatures on all Checks.**

Another best practice is to require that two people sign all checks written against a local entity's account. Local entities with an annual budget less than \$50,000 should require that one of the signatures be provided by a board member. To provide an additional separation of duties, a district may choose to not allow the general manager to sign checks but assign that responsibility to two other staff. Although the general manager may still review and authorize expenditures. Boards may also want to adopt a policy prohibiting anyone from signing a check payable to themselves.

Each check should also be accompanied by a purchase order or a requisition sheet describing the purpose and the account to which the purchase will be charged. Ideally, before any check is signed, the budget officer will verify that funds are available to cover the purchase.

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**Requiring staff to seek formal board approval for large expenses gives the board an additional opportunity to make sure entity funds are used wisely.**

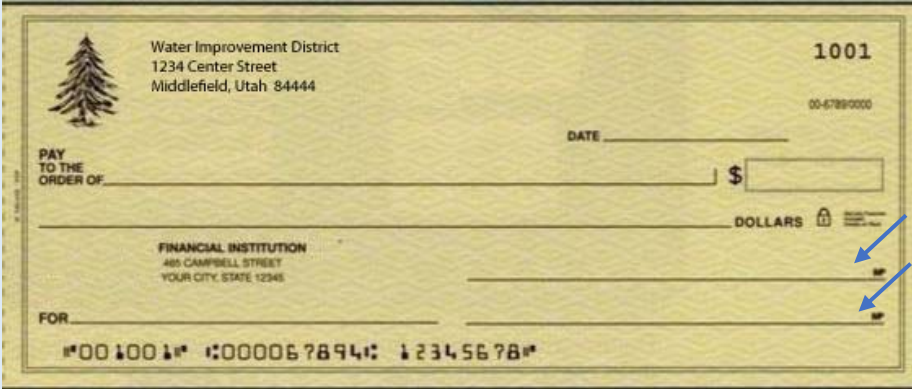
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**Entities should require that two signatures appear on each check. Small districts should require that one of those signatures be a member of the board.**

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**Figures 3.5 Many local entities require two signatures on all checks.** Requiring two people to sign each check provides an added level of protection against fraud.



### **Board and Staff Need to be Qualified and Receive Ongoing Training**

Even if all the necessary internal controls are in place, a local entity may still be at risk if it does not have a board and staff capable of administering those controls. We recommend that limited purpose entities do three things to make sure they have the most qualified board and staff possible.

- First use an objective process to fill positions on the board and to hire employees.
- Second, require board and staff to keep up their training by participating in conferences and certification programs.
- Third, rely on outside experts when problems arise that are beyond the expertise of the full-time staff.

### **Use an Objective Process to Fill Vacant Board and Staff Positions**

We were impressed with the professionalism and skill of many of the board members and staff operating Utah’s limited purpose entities. What is troubling are the reports of people recruited by the executive director to serve on a board in an uncontested election. We question whether such board members can be truly independent. Also troubling are reports of board members and executive directors hiring themselves as employees of the local entity. Because limited purpose

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**Without a qualified, well-trained staff, it may be difficult to implement a system of internal controls.**

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**Staff should avoid being involved in the process of recruiting or selecting someone as a board member.**

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entities are units of government, it is essential that board and staff positions be filled using an impartial selection process designed to identify the most qualified person available.

**Staff Should Avoid Recruiting Individuals to Serve as Board Members.** In many communities, people seem to have little interest in serving on the board of their local limited purpose entity. Often, elections for board seats are cancelled because only one individual has filed as a candidate. Some districts report having had difficulty finding anyone who is qualified to fill a vacant board seat. Some of the board members we interviewed said they were asked by the district's executive director to fill a vacant seat on the board. Our concern is that rather than the board selecting its executive director, we may have executive directors who are selecting their board members.

The code of ethics followed by the Utah City Management Association offers guidance that could also be applied to executive directors of a limited purpose entity. The standard that city managers must follow is that they “Refrain from participation in the election of the members of the employing legislative body.” We believe the same standard also applies to executive directors of a limited purpose entity.

It is not the executive director's responsibility to fill vacant positions on the board. Instead, **Utah Code 17B-1-306** states that when there are no candidates for a vacant seat on a local district board, the remaining board members must appoint someone to fill the vacancy. The same process is used to fill a vacancy on the board of a special district.

**Local Entities Should do more to Publicize the Availability of Open Seats on the Board.** Utah Code Title 20A 5-101 prescribes a process that election officials must follow for giving public notice of upcoming elections and the opportunity people have to file as candidates. We were unable to verify whether limited purpose entities are complying with those provisions. However, we have received reports that few people are filing as candidates and that there has been, in some locations, low voter turnout. This raises concern about the adequacy of some entities' procedures for notifying the public of the available seats.

For example, a fire district reported to us that they gave public notice of the upcoming election by posting a flier on the front door of the district office another on the bulletin board of the local bank. Not

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**Entities can generate greater interest in serving on the board by engaging in a public outreach program. Among other things, they should announce upcoming board elections.**

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surprisingly, no one filed for the two open board seats. Instead, the chief and another part time fire fighter chose to file for the two vacant seats. Because they were the only two candidates, they took office without holding an election.

Even if entities are complying with the public notice requirements of the Elections Act, we believe more should be done to make the public aware when board seats are coming available. For example, it is not uncommon for cities to give notice on their websites and through other media that open council seats are coming available and that people should consider filing for office. Limited purpose entities might have more success finding people interested to serve on the board if they improved their public outreach prior to each election.

**Local Entities Should Follow an Objective Recruiting Process When Filling Staff Positions and Hiring Outside Contractors.** We are concerned by reports of board members and directors hiring themselves or their relatives to do work either as employees or as contractors. State Law requires that each limited purpose entity have a set of personnel and procurement policies to guide the process of hiring new staff and selecting outside contractors. By following formal procedures, local entities should be able to avoid concerns about potential conflicts of interest in the purchasing and hiring decisions they make.

### **Provide Regular Training to the Board and Staff**

State law requires each newly elected or appointed board member participate in the special training designed for new board members within one year of taking office. There is also a requirement that all board members receive training each year on the requirements of the open meetings act. Most outside training opportunities offer participants a certificate documenting their participation. Whether the training is provided by outside sources or in-house, documentation of the training should be kept on file.

**Provide Annual Training to Board and Staff.** The training requirements in statute are a minimum standard. The best practice is to provide annual training of the board and staff. We have observed board and staff training provided at:

- Annual Conference of the Utah Association of Special Districts,
- The Utah State Auditor’s online training at

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**New board members should take advantage of the many training opportunities available to them.**

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<http://auditor.utah.gov/training/local-district/>

- At board meetings by the entity's own legal counsel.
- Special local training arranged through the Utah Association of Special Districts or the State Auditor's Office.

Some local entities belong to industry-specific associations that also hold annual training conferences. For example, the Rural Water Association of Utah and the Utah Mosquito Abatement Association both have annual conferences at which the board and staff can receive industry specific training. Each of these associations also offer certification programs for system operators in these fields.

**Entities Should Retain the Certificates Board and Staff Receive After Completing their Training.** One of the tests that outside auditors are asked to perform is to verify compliance with certain statutory requirements that applies to an entity. One of those requirements for which auditors should test is that board members receive their annual training in the open and public meetings act. Because entities may be asked to demonstrate compliance with that requirement, it is a best practice to keep documentation on file of the training that has been provided and who has attended that training.

**Cost of Training is a Concern, but can be Managed.** Some board members have expressed concern for the cost associated with sending board and staff to annual training events. However, they need to realize that the district has an obligation to its customers to make sure their board and staff are qualified to handle the serious responsibilities they have been given. They should also recognize the risk associated with operating water systems, fire districts and landfills, etc. without a board and staff who are well qualified.

A water reclamation district in Northern Utah is a good example of an entity that provides in-house training each year to its board and staff. During each January meeting of the board, the district's legal counsel provides instruction on the open meetings act and also reviews the material related to governance and accountability that is part of the state auditor's new board member training.

If the cost is a concern, boards could also send just one or two of its members or a staff person to a conference. After they attend, these individuals can then report back to the board what they have learned. For example, at the board meeting of one of the fire protection districts we visited, we observed a report by an employee who had

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**Entities should retain documents showing that each board member has had the required training. Outside auditors may ask for this information.**

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recently attended the annual conference of the Utah Association of Special Districts. She summarized the information she learned at the conference and suggested new practices their district might adopt.

### **Hire or Appoint the Needed Outside Expertise**

Limited purpose entities must not hesitate to seek the technical outside expertise they need when facing a challenge for which their own staff may be poorly qualified. A district may need to hire outside consultants to address any number of technical problems that involve both management controls as well as the entity's operations.

**Appoint an Administrative Review Committee to Handle Specific Budgetary and Finance Tasks.** A governing board may not have the time or the expertise they need to address particularly difficult challenges. In this case, the board can create a special committee consisting of local experts to address the specific tasks as assigned by the board.

The administrative committee created by a Fire District Board in Northern Utah is a good example. The five mayors who sit on the board determined that they did not have time to review the budget in as much depth as they thought it deserved. For this reason, they created an administrative committee to help them oversee district finances and prepare a budget. The committee members include the city manager from each of the five communities served by the district and a budget officer from the county. The committee then submits to the board a proposed annual budget, a new salary scale, and its evaluation of major capital equipment purchases proposed by staff. As a public body, the committee's meetings are subject to the open and public meetings act.

**Hire Outside Consultants or Contractors.** When a specific technical need arises, a local entity should not hesitate to hire outside consultants. Relying on outside contractors may be particularly important for small local entities that cannot afford to hire full time staff. As with any purchase, an open competitive process should be used when hiring outside contractors. The steps used when selecting contractors should be spelled out in the districts procurement policies. Above all, local entities, even the smallest ones, should avoid hiring a family member of a board member or employee.

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**Boards should not hesitate to hire outside experts to handle tasks that their staff may not be fully qualified to perform.**

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**Several high-profile scandals have brought greater attention to the need for organizations to consider the influence that corporate culture has on the ethical behavior of employees.**

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## **Board and Executive Director Need to Promote a Culture of Ethical Behavior**

In recent years, there has been an increased interest in the effects of organizational culture on ethical behavior and ultimately the success of the organization. While adopting a long list of internal control procedures will help maintain proper accountability and control, without a culture of ethical behavior, an organization will still be at considerable risk. Ultimately, to prevent fraud, waste and abuse, the board and management need to foster an organizational culture that values compliance, accountability and ethical behavior. They can do this by setting the proper “tone at the top.”

### **Recent Corporate Scandals Highlight the Influence of Culture on Ethical Behavior**

In recent years, several highly publicized scandals have raised awareness of the influence that corporate culture has on ethical behavior. Whether a private corporation, an institution of higher education, or a public entity, there is growing realization that every organization needs to take steps to foster an ethical corporate culture. If not, the consequences can be devastating.

One example is Volkswagen, whose engineers crafted a “defeat device” to circumvent vehicle emissions tests. Another is Wells Fargo Bank, whose employees were pressured to create false consumer accounts and sign up customers for services they did not request. Finally, Baylor University suffered NCAA sanctions and a loss of reputation for its failure to address allegations of sexual assault by some of its athletes. In each of these cases, a corporate culture was blamed for creating an environment that enabled illegal and fraudulent activity to occur. In each case, the institution suffered a serious financial cost, not to mention a loss of public trust.

Similarly, recent cases of fraud among limited purpose entities have been attributed to organizational cultures that do not foster ethical behavior. For example, one report blames a recent case of fraud on a board culture that was too trusting of staff, that was “overly deferential to the Director,” and was “rubberstamping” staff recommendations. Another report attributes a case of fraud to “a culture that demands loyalty.” Out of loyalty to his director, the CFO chose not to alert the board to his concerns that funds were being misused.

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**By demonstrating ethical behavior themselves, the Board members and Executive Director can set the proper “tone at the top.”**

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## **Best Practices for Promoting a Healthy Organizational Culture**

To minimize the risk of fraud, we encourage the leaders of each of limited purpose entities to consider whether they are setting the proper ethical tone for their organizations. If their words and actions suggest a lack of support for ethical behavior, for control and accountability, they may be promoting a culture that puts the organization at risk. The following describes some of the best practices for promoting a healthy organizational culture.

**Set the proper “Tone at the Top.”** Creating a culture of integrity must begin at the top of the organization. The board and the executive director set the “tone at the top, as it were by applying high standards of accountability and performance to themselves. They then need to communicate those standards of behavior to their employees. If the board and executive director do not demonstrate a high commitment to following the rules that apply to them, they will be promoting a lack of respect for rules within their own organizations.

For example, we found that some local entities have had difficulty complying with some of the state’s requirements for financial reporting, public notice, transparency and training. By not complying with these state requirements, some boards and executive directors are communicating to staff that following rules is not important.

**Board can Adopt an Ethics Policy.** One way the board can communicate its commitment to a high standard of ethics is to adopt a code of ethics that clearly states the organization’s values and standards of behavior. As the board drafts its ethics policy, it should consider the Utah Public Officers' and Employees' Ethics Act (Utah Code Title 67 chapter 16). Another good example of an ethics policy is the one used by the Utah Association of Special Districts. It can be found on the association’s web site: <http://www.uasd.org/training.php>.

**Periodically Review the Ethics Policy with Staff.** Once a code of ethics is adopted as policy, it is important that it not be forgotten. Periodically, an effort should be made to reinforce the ethics policy with employees. This can be done during training, through the organization’s newsletter or through other methods of communicating with employees. Furthermore, when faced with difficult ethical problems, the opportunity should be taken to consult the ethics policy and to raise awareness of the entity’s standards of behavior.

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**Holding staff to an ethics policy and providing an ethics hotline are two ways that boards can promote ethical behavior.**

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**Because employees often become aware of illegal or unethical behavior before management, some organizations use an ethics hotline to allow staff to report unethical behavior.**

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**Hold Everyone Accountable, Even Managers, to High Standards of Performance.** If employees see that a colleague routinely violates the entity's standards of behavior and without consequence, it sends a message that the standards don't apply universally and can be compromised. For this reason, employees should be told what is expected and the standards that will be used to judge their performance. Then, if violations occur, employees should be held accountable and face consequences. Furthermore, those consequences should be meted out consistently.

**Provide for an Ethics Hotline or Whistleblower Policy.** Often employees become aware of illegal or unethical behavior before management does. To encourage employees to identify practices and behaviors that may put the organization at risk, a means should be provided to anonymously report potential violations of the organization's code of conduct. Some organizations use a whistleblower hotline; others use a suggestion box.

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**Figures 3.6. Solicit Anonymous Feedback from Employees.** Employees should be encouraged to anonymously report potential violations of the organization's code of conduct.

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Some organizations use a comment box to solicit anonymous feedback.



**Avoid Creating a Compensation and Reward Structure that Leads Employees to take Unnecessary Risks.** Senior management needs to craft an incentive system that will promote and reward high performance. However, caution must be used to avoid creating a system of incentives that motivates employees to act unethically in order to achieve their performance goals.

**Recommendations:**

1. We recommend that the board of each limited purpose entity in Utah review the letter and associated best practice checklist in Appendix A from the Legislative Audit Subcommittee chairs. The board should then meet with its executive director and discuss how to implement each of the best practices.

# Chapter IV

## Legislature Should Consider the Best Practices for State Oversight of Limited Purpose Entities

The prior chapter describes best practices for strengthening local control of limited purpose entities. In this chapter, we first describe some of the problems associated with the hidden nature of limited purpose entities. Then, to address these concerns, we suggest the legislature consider adopting the best practices we have observed for state and county oversight of limited purpose entities. Specifically, we suggest the following:

- Create a formal state registry of limited purpose entities
- Withhold funds from local entities that do not comply with all state disclosure laws
- Take steps to dissolve entities that are persistently non-compliant
- Encourage counties to take a larger role in promoting compliance by local entities
- Encourage counties to publish information regarding the limited purpose entities in each community

Finally, Utah’s many governmental nonprofit corporations should be encouraged to follow the same best practices for internal control that limited purpose entities follow.

### Hidden Nature of Limited Purpose Entities Can Be an Obstacle to Accountability

Limited purpose entities are sometimes described as a hidden level of government because they operate somewhat behind the scenes. The public is generally unaware that these entities provide services independent of other forms of local government. Adam Edelen, Kentucky's Auditor of Public Accounts, used the term “ghost governments” to describe these local entities because they are, as he put it, the “least understood level of government.”

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**Some describe limited purpose entities as “Ghost Governments” because of poor public awareness of these entities.**

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Our review of limited purpose entities in Utah confirms some of the stigma associated with this level of government. We identified three concerns:

1. Utah state agencies have had difficulty tracking these entities. As a result, no one has a complete list of all the local districts, special service districts and interlocal entities in the State of Utah.
2. Many limited purpose entities are not complying with the state's transparency laws, such as the requirements that they submit their financial statements to the State Auditor and give public notice of meetings.
3. Many districts struggle to find people interested in serving on their board of trustees. As a result, elections for seats on the board are often cancelled and accountability to voters is diminished.

These are problems that are not easily addressed by the local entities themselves. Therefore, we suggest the Legislature consider our list of best practices for providing state-level oversight of these entities.

### **Number of Limited Purpose Entities in Utah Unknown**

In Chapter I we reported that there are 481 limited purpose entities in Utah that collectively spend an estimated \$3.5 billion in public funds per year. That data includes 241 local districts, 162 special service districts, 65 interlocal entities, and 13 independent entities. However, these figures, obtained from the Office of the State Auditor, appear to understate the actual number of limited purpose entities in the state and their total outlays. We found evidence suggesting that many entities have escaped notice of the state auditor and other state agencies.

We obtained lists of local districts and special service districts from three different state agencies, seven counties, and the Utah Association of Special Districts. Upon comparing the various lists, we found that certain entities appear on some lists but not on others. For example, the lieutenant governor's list has nine special service districts that were created in recent years that do not appear on the lists provided us by the state auditor and by the tax commission. Some counties identified entities that do not appear on any list provided us by state government

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**We found special districts and local districts that are listed by the Lieutenant Governor and the counties are unknown to the state auditor.**

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agencies. Figure 4.1 shows the number of local districts and special service districts reported by several state and local agencies that do not appear on the list we received from the state auditor.

**Figure 4.1 State and Local Agencies Identified Special Service Districts and Local Districts That Are Not on the State Auditor’s List.** While the state auditor’s list is likely the most complete, it still doesn’t include names of some local districts and special service districts reported to us by several other state and local agencies.

Agency	Known Local and Special Service Districts That Do Not Appear on the State Auditor’s List
Tax Commission	54
Utah Assoc. of Special Dist.	43
Survey of Seven Counties	8
Lieutenant Governor	13
Division of Water Quality	3
Unduplicated Count	101

After comparing the names of special service districts and local districts from each of the different sources, we concluded that no state agency has a complete list of all the limited purpose entities in the state. Of greatest concern are the special service districts and local districts identified by the lieutenant governor and by the counties that are not known to the state auditor. Some may be operating without complying with the state’s basic reporting requirements.

Several explanations for the differences in the lists are possible. For example, some entities may have been dissolved or created without all state agencies being notified. Some discrepancies may be explained by entities' name changes. In any case, unless the state can identify all the limited purpose entities in Utah, we question how state agencies can monitor compliance with the applicable state laws which is the subject of the following section.

**Many Entities Not Complying with State Transparency Requirements**

State law imposes several requirements on state and local government entities that are designed to improve transparency and accountability. We found that some limited purpose entities are not complying with these laws. These requirements include:

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**No state agency has a complete list of all the limited purpose entities in the state.**

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**We question how state agencies can monitor compliance and enforce regulations if they have not identified all limited purpose entities in the state.**

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Many local entities seem to have difficulty filing their budgets and financial statements on time, and giving proper notice of their meetings.

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- **Annual Budget to Be Submitted to State Auditor.** State law requires local entities to submit their board-approved budgets to the state auditor. Specifically, Utah Code 17B-1-614 requires local districts to submit their budgets no later than 30 days after adoption.
- **Notice of Open and Public Meetings.** Utah Code 52-4 requires all public bodies, including limited purpose entities, to give at least 24 hours' notice of their public meetings by posting the meeting time and agenda on the Utah Public Notice Website.
- **Public Notice of Board Contact Information.** *Utah Code* 17B-1-303 requires local districts to post the name, email address, and phone number of each of the district's board members to the Utah Public Notice website. *Utah Code* 17D-1-106 applies this provision to special service districts as well.
- **Quarterly Revenue and Expense Statements to Transparency Utah.** Utah Code 63A-3-405(4) requires that beginning July 1, 2017, all local entities to provide financial information to the Utah Transparency website [www.utah.gov/transparency](http://www.utah.gov/transparency). Prior to that time, the requirement only applied to entities with budgets of \$1,000,000 or more.
- **Financial Statements to Be Submitted to State Auditor.** Utah Code 51-2a-202 requires the annual financial statement be submitted to the Office of the Utah State Auditor no later than six months after the end of the fiscal year.

**Compliance with Public Disclosure Laws Has Been Weak.** A test of 50 randomly selected special purpose entities found that 30 entities did not submit their annual financial statements and 33 did not submit budgets to the state auditor within required deadlines, if at all. In addition, 22 entities were not complying with Open and Public Meetings Act requirement to post their meeting agendas on the public notice website. The area with the weakest compliance was the requirement that entities post the contact information of their board member on the Open and Public Meetings website. Only 26 percent comply with that requirement. On the other hand, we found better compliance with the requirement that financial reports be submitted to



the transparency website. All 13 entities in our sample required to submit the reports (those with budgets greater than \$1 million) had complied with the requirement compliance test.

**Figure 4.2 Low Rates of Compliance with State Disclosure Laws.** A test of 50 special purpose entities revealed a low rate of compliance with the requirements to disclose their budgets, financial statements, meetings, and contact information.

	Budget Submitted within 30 Days of Approval?	Financial Statements Submitted within 180 Days of Year End?	Meetings Posted on Public Notice Website?	Board Contact Information Posted on Public Notice Website?	Finances Reported to Transparency Utah? <sup>1</sup>
Yes	34%	40%	56%	26%	100%
No	66%	60%	44%	74%	0%

• 1. Requirement only applies to entities with budgets greater than \$1,000,000.

As shown above, only 34 percent of sampled entities submitted their budgets to the state auditor within 30 days of approval, as required by state law; 40 percent submitted audited financial statements (or the equivalent reports) within 180 days of the fiscal year end; 56 percent gave proper notice of their meetings on the Utah Public Notice Website; only 26 percent provided the required contact information for their board members.

If adhered to, Utah’s public disclosure laws seem adequate to provide the intended transparency for limited purpose entities. However, as our test of 50 entities shows, the low rate of compliance in some areas raises concern about transparency and accountability.

### Limited Purpose Entities Have Difficulty Finding People to Serve on Their Boards

As noted in Chapter II, the governing board plays a critical role in providing accountability and control to an organization. We are concerned that some limited purpose entities are having difficulty finding people willing to serve on the board of directors. Elections are often cancelled because of a lack of candidates. Sometimes vacant seats are only filled after the executive director or existing board members have recruited neighbors, friends and acquaintances to serve. This

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**The low rate of compliance with state disclosure laws raises concern about transparency and accountability.**

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**Board elections are often cancelled because local districts have only enough candidates to fill the available board seats.**

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approach to selecting a governing board raises questions about board independence and their ability to represent the local entity.

**During Weber County’s 2015 Municipal Elections, Eight of Ten Local Districts Cancelled their Elections.** To assess how frequently board elections are held, we examined the 2015 election results in Weber and Salt Lake Counties. Weber County has 12 local districts. Ten of those have at least some board members who are elected. Of those, only two districts had enough candidates to hold an election. The others cancelled elections because there were only enough candidates to fill the seats available. In contrast, we found that during that same election year, 13 of 14 elections for city council seats in Weber County were contested.

We interviewed the members of a board whose elections have been cancelled in past years. We asked how they came to decide to run for the board position. Three of the five board members said the district’s general manager invited them to file (as the only candidates) for their board seats.

**Only a Few Entities in Salt Lake County Held Elections in 2015.** We also surveyed the 17 local districts in Salt Lake County regarding their 2015 municipal elections. Ten of the 17 districts responded. Of the ten, only three (30 percent) said they had enough candidates to hold an election. The remaining districts (70 percent) reported that their elections were either cancelled or the election was held with the same number of candidates as there were seats available. One local district reported that no one filed for the vacant board position, so the board appointed the outgoing board member for another term. As in Weber County, most city council elections in Salt Lake County were contested. During the 2015 municipal elections, 34 of 42 council seats (81 percent) were contested.

**Low Public Awareness May Contribute to the Low Interest in Serving on Boards.** Compared to city and county governments, many local districts, special service districts, and interlocal entities are not well known to the public they serve. What makes matters worse is that some local districts use more than one name. We believe that limited purpose entities need to find better ways to communicate who they are and the services they provide. This, we believe, can increase the number of people willing to serve on the board, and ultimately improve accountability.

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**A general lack of public awareness of limited purpose entities may explain why few people are filing as candidates for local board seats.**

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We believe that a better community outreach program could help improve public awareness of these entities and increase the number of people interested in serving on the boards.

## **Utah Should Adopt the Best Practices for Holding Limited Purpose Entities Accountable**

In addition to encouraging local entity boards to adopt best practices described in Chapter III, the Legislature should consider adopting best practices for strengthening accountability at the state level. By adopting any of the following best practices, the Legislature could strengthen accountability and reduce the risks associated with the hidden nature of limited purpose entities.

### **Legislature Should Consider Creating a Formal State Registry of Limited Purpose Entities**

Until we have identified all the limited purpose entities in the state, we question whether we can even begin to oversee their activities and ensure they are complying with state law. For this reason, legislators should consider requiring the Lieutenant Governor's office to maintain a formal registry of all local districts, special service districts, and interlocal entities. We found two other states, Kentucky and Idaho, that have formal registries for limited purpose entities.

#### **Kentucky Created a Central Registry for Its Special Districts.**

In 2012, the Auditor of Public Accounts (APA) in the Commonwealth of Kentucky released a report titled *Ghost Government: A Report on Special Districts in Kentucky*. This report discussed failure to comply with various statutory reporting requirements and a lack of enforcement mechanisms when non-compliance occurred in its special districts. The report recommended development of an online central registry for Kentucky special districts. As a result, Kentucky special districts now register annually, pay a registration fee, and submit statutorily required reports through a single on-line registry.

**Idaho Created a Registry for Special Districts.** Similar to Kentucky, the State of Idaho created a central registry for its special districts in the 2014 General Session that went into effect in fiscal year 2015. As in Utah, Idaho found it difficult to obtain a comprehensive list of special districts in Idaho. The Legislative Services Office reported that it found "...no clear reporting or oversight function to

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**The Idaho State Legislature passed a bill in 2014 creating a registry and new reporting requirements for special districts.**

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identify all special districts...” or “...track spending levels...” Additionally, they reported widespread non-compliance with statutory reporting requirements and the absence of an adequate enforcement mechanism.

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**Figures 4.3 Idaho Took Steps to Increase Visibility of Special Districts.** Concerns about lack of compliance and transparency led the Idaho Legislature to pass legislation requiring special districts to register with the state and submit reports.

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During its 2014 session, the Idaho Legislature unanimously approved HB 560, which required that by:

- January 1, 2015 –Legislative Services Office (LSO) must create an online registry.
- March 1, 2015 – Every existing local governing entity must complete the initial registration.
- September 1 – Every year on or before this date, the LSO must notify the appropriate board of county commissioners and the Idaho State Tax Commission of any local entities that failed to comply with annual reporting requirements.
- December 1 – Every year on or before this date, local entities must update registration information, the State Tax Commission must submit a list to LSO of all taxing districts within the state, and the county clerk of each county must submit a list to LSO of all taxing districts and all other local governing entities in the county.

**Utah does not Require Limited Purpose Entities to Register with the State.** Utah law (*Utah Code* 17B-1-215) requires local public entities to file a certificate of incorporation with the Lieutenant Governor’s office when they are created. They must also submit additional filings when they modify their boundaries, change names or dissolve. However, the records maintained by the Lieutenant Governor do not represent an actual registry of legal public entities that are authorized to operate in the State of Utah. For example, the Lieutenant Governor does not maintain a registry of public entities similar to that maintained by the Department of Commerce for corporations that are legally authorized to conduct business in Utah. However, other states, such as Idaho and Kentucky, do require local governmental entities to maintain their registration with the state as a basic requirement for operating as a public entity. We recommend that legislature consider requiring the same type of registration for limited purpose entities that wish to operate as a public entity in the State of Utah.

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**Although corporations doing business in Utah must register with the Department of Commerce, no formal registration is required of limited purpose entities operating in the state.**

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## **State Auditor Should Continue to Withhold Funds Of Entities that Do Not Comply with State Disclosure Laws**

Utah's state auditor has been given broad latitude to respond when local entities do not comply with state reporting requirements. For example, the state auditor is able to freeze the bank accounts of fee assessing entities that do not comply with the state's financial reporting requirements. He is also able to freeze the accounts of any local government entity that does not submit its duly approved budget within 30 days of passage. Failure to submit reports to the transparency Utah website can also result in a similar response by the state auditor. These steps are consistent with the response we have observed in other states as they strive to encourage local districts to comply with state public disclosure laws.

In recent years, the state auditor has become more aggressive in threatening the use of sanctions when limited purpose entities do not submit their annual financial statements as required by law. In fact, this past February, 42 local districts, special districts and interlocal entities were sent letters of warning stating that their funds could be placed on hold because they did not submit their financial statements on time. In addition, the state auditor ordered 55 entities to suspend their use of funds after they failed to respond to a warning that they had not submitted their annual budget on time. A few were even told their bank accounts would be frozen if they did not comply with state reporting requirements.

However, even after the State Auditor has threatened to withhold funds and freeze bank accounts, some entities still failed to comply with the financial reporting laws. When entities do not respond to the threat of losing their funding, it presents the state auditor with the difficult choice of either (1) ignoring an entity's noncompliance, or (2) freezing the entity's funding and, in effect, stopping their ability to provide needed public services.

In our view, the state needs to develop additional ways of responding to entities that do not comply with state reporting requirements. For example the state auditor should be able to withhold tax receipts and freeze bank accounts of any entity that persists in ignoring state reporting requirements. In addition, we recommend that state auditor notify each county commission or council of any noncompliant entities within their jurisdictions and that

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**Utah's state auditor has authority to withhold funding from agencies that do not comply with the state's reporting requirements.**

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the counties be given the authority to direct whatever changes are deemed necessary to obtain and entity's compliance with the law. One option, discussed in the following section, would be for the county commission to be given authority to dissolve the entity and to find a new method for providing that entity's public services.

### **Legislature Should Consider Streamlining The Process for Dissolving Limited Purpose Entities**

For limited purpose entities that consistently fail to comply with the states registration, financial reporting, and public disclosure laws, the Legislature may want to streamline the process for dissolving an entity. *Utah Code* 17B-1-217 already specifies a process for dissolving local districts, but the criteria are so narrow that it would only be used for entities that have been completely inactive for many years. In contrast, other states such as Idaho, Kentucky, and Oregon, use the threat of dissolution to ensure that entities operate in compliance with state law. The following example describes the process used by Oregon. We recommend that the legislature consider the merits of adopting a similar process for dissolving limited purpose entities.

**Oregon Allows for the Dissolution of Special Districts that Do Not Comply with State Disclosure Laws.** Oregon law designates its secretary of state and its counties both play a role in overseeing limited purpose entities, which are mainly referred to as special districts. An audit division in Oregon's Office of the Secretary of State performs a role similar to that of Utah's state auditor. Oregon's audit division receives all financial statements and outside audit reports for special districts, and so is uniquely positioned to monitor their compliance with financial reporting laws.

When a special district in Oregon does not comply with reporting requirements for three consecutive years, state statute requires the secretary of state to notify the county where the non-compliant district is located. The county commission then has 30 days to initiate a statutorily outlined dissolution process. An audit director told us that they never need to begin the dissolution process because entities usually come into compliance before reaching the three-year mark. The audit director also stated that the threat of dissolution is enough to get special districts to comply.

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**Other states use the threat of dissolution as a means of encouraging entities to comply with state training and reporting requirements.**

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**If special districts do not comply with state reporting requirements for three years, the county leaders may then be asked to begin the process of dissolving that entity.**

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**Figures 4.4 Oregon’s Process for Dissolving Limited Purpose Entities.** Oregon law requires that counties begin the process of dissolving limited purpose entities after they fail to submit annual reports for three years.

**Oregon Revised Statutes 198.345  
Effect of failure to file certain reports.**

(1) If a special district for three consecutive years fails to file a report as required...the Secretary of State...shall notify the county board of the county where the district, or the greater portion of the assessed valuation of taxable property in the district, is located.

(2) Within 30 days after receiving the notice provided by subsection (1) of this section, the county board shall initiate proceedings to dissolve the special district as provided by ORS 198.345 to 198.365.

(3) The county board may appoint three individuals, residents of the district, to assist in locating the assets, debts and records of the district.

In Oregon if a limited purpose entity (or special district) consistently fails to submit their annual budget and audited financial statements, as required by law, that entity is then disqualified from using public funds and must be dissolved. In our view, Utah should consider adopting a similar policy of dissolving limited purpose entities that fail to comply with similar requirements imposed by Utah state law.

**Legislature should Consider Requiring Counties to take a Greater Role in Promoting Compliance by Local Entities**

In both Idaho and Oregon, county governments play an important role in overseeing local and special service districts. Staff from the Utah's Office of the State Auditor have also observed that when counties are involved in overseeing the limited purpose entities within their jurisdictions, the entities tend to be better run and more quickly come into compliance with the applicable state laws. For this reason, we suggest the Legislature consider creating a formal role for counties in the process of holding local and special service districts accountable for complying with state laws.

**Idaho Gives the County Commission a Role in Addressing Non-Compliance by Limited Purpose Entities.** As in Utah, local government entities in Idaho may have their tax revenues withheld if they fail to comply with the state’s financial reporting requirements. However, some special districts receive very little, if any, tax revenues.

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**Idaho relies on its county commissions to bring limited purpose entities into compliance with state reporting rules.**

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To bring those entities into compliance, Idaho statute requires that county commissions take steps to bring the entities into compliance. Upon receiving notice from the legislative services office, the county commissions decide what steps to take to bring the entity into compliance. As shown in Figure 4.5, a commission may issue fines, or require that the entity cover the cost of an audit.

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**Figures 4.5 Idaho Requires County Commissions to take Action against Non-compliant Limited Purpose Entities.** Idaho law requires that county commissions convene a meeting to decide how best to respond when limited purpose entities do not comply with state reporting and registration requirements.

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**Idaho Statutes 67-450E.**

**Local Governing Entities Central Registry – Reporting Information Required – Penalties for Failure to Report.**

(e) For any local governing entity that is a non-taxing district, including entities established pursuant to title 50, Idaho Code, upon notification to the board of county commissioners from the legislative services office of noncompliance by such entity, the board of county commissioners shall convene to determine appropriate compliance measures including, but not limited to, the following:

(ii) Assess a noncompliance fee on the noncomplying entity. Such fee shall not exceed five thousand dollars (\$5,000). Such fees and costs may be deducted from any distributions of taxes, fees or assessments collected by the county on behalf of the local governing entity. The amount of any such fee shall not be passed on to persons subject to the jurisdiction of the entity in the form of adjustments to any fee or assessment imposed or collected by the entity. Any fee collected shall be deposited into the county’s current expense fund;

(iii) Cause a special audit to be conducted on the entity at the cost of the entity.

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**Kane County has stepped up its efforts to help limited purpose entities comply with state training and reporting requirements.**

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**Kane County is Voluntarily Working to Improve Accountability among its Limited Purpose Entities.** Even without the formal statutory authority we see in Idaho, some Utah counties have helped their limited purpose entities comply with the state’s reporting requirements and public disclosure laws. For example, Kane County has taken steps to strengthen oversight of limited purpose entities in its jurisdiction. Kane County has:



- Assigned a county employee to track board member training, and the terms of board members
- Reviewed the financial statements of its limited purpose entities
- Arranged for training for board and staff and invited director of the Utah Association of Special Districts (UASD) to attend
- Approved a procurement policy for the county and directed that if a special service district has not adopted its own procurement policy, that entity is required to use the county's policy.

In our opinion, if other counties supported their limited purpose entities in a similar manner as Kane County does, we would see better local governance, and greater compliance with Utah's transparency and reporting laws. Of course, under the current statute, such support is voluntary.

The Legislature should explore strategies for creating a larger role for counties in overseeing limited purpose entities. One option would be to have the state auditor report to each county clerk the limited purpose entities that are out of compliance with the relevant state laws. Upon receiving these reports, the county clerk could provide training and monitor each entity's progress towards compliance. The other option would be to enact laws like those in Idaho and Oregon that mandate a formal response by the county when entities are not complying with state law.

### **Legislature Should Encourage Counties to Promote Greater Public Awareness of the Limited Purpose in their Areas**

We identified several Utah counties that do an excellent job of publishing information about the limited purpose entities in their communities. This information is part of a public outreach effort to encourage transparency and to invite people to participate on public boards.

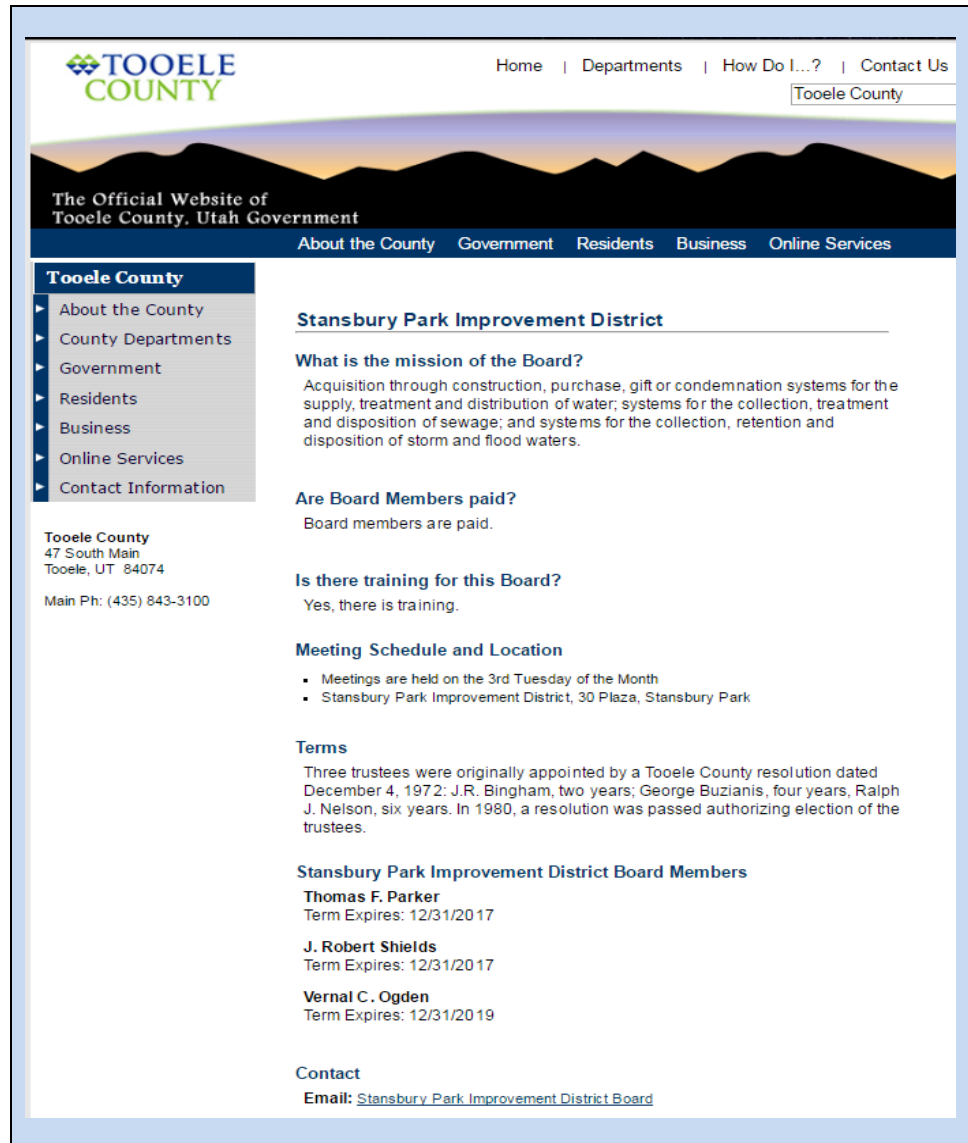
For example, Figure 4.6 shows a page from the Tooele County website (<http://www.co.tooele.ut.us/boards-committees.htm#boards>) that lists the boards and commissions of each public organization in the county. It includes information about board membership, meeting schedules, and board member terms of office. Visitors to the website can also download an application to serve on the boards.

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**To improve public awareness, Tooele County provides information regarding each of its local districts and special service districts on its website.**

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**Figures 4.6 Tooele County’s Website Lists Available Board Positions for Local and Special Service Districts in the County.** Tooele is one of several counties providing information on their websites regarding local board seats. Among other information, the site lists when board seats are coming available.



The Tooele County website also helps people understand how to apply for local board seat that may soon become available.

Tooele County’s public outreach effort promotes greater public awareness of the local entities that provide vital public services. It also encourages individuals to consider participating on a local board. We noticed that the two local districts in Tooele County that were included in the study described in Chapter II both had competitive elections with a sizable voter turnout.

Several other counties provide information similar to that posted on the Tooele website. If every county were to publish this information, public awareness of limited purpose entities would likely increase. Alternatively, the state could require that each entity publish this information on the state's public notice website. Such public outreach efforts could encourage more people to consider serving on entity boards.

## **Greater Accountability Needed for Governmental Nonprofits**

Among Utah's limited purpose entities, perhaps the least understood and potentially the least accountable to the public, are governmental not-for-profit corporations. We identified about 270 nonprofit corporations that have been created by local governments, school districts, universities and other public entities. These entities face as much risk of fraud, waste, and abuse as other types of limited purpose entities. We recommend the Legislature consider authorizing further investigations into the risks presented by these entities.

### **About 270 Governmental Nonprofit Entities Exist in Utah**

By consulting the registry of not-for-profit corporations maintained by the Utah Department of Commerce, we identified about 270 nonprofit corporations with a close association to a local public agency. They either have the same address as a public agency or have the same director as the affiliated government agency. For purposes of this report we describe these entities as governmental nonprofit organizations. We recognize, however, that certain sections of the statute, namely *Utah Code* Title 11, Chapter 13 (amended by HB 55 during the last session) apply a narrower definition to governmental nonprofits than is used in this report.

The governmental nonprofits include school foundations, arts councils, economic development agencies, community foundations, and housing projects created by the local building authority. From our limited work, it appears that they are typically created to further the purpose of the sponsoring public agency by using grants, contracts and private donations. Some of these government-sponsored nonprofits may receive public funds but others do not. Some are sponsored by public agencies with a controlling interest in the

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**There are about 270 governmental nonprofit organizations that provide supportive services to Utah local government agencies.**

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**Governmental nonprofit entities need to follow the same best practices for preventing fraud, waste, and abuse as other local government entities.**

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corporation, while others are not. The following are three governmental nonprofits that we reviewed during this audit.

**Granite School District Foundation.** A nonprofit organization affiliated with the Granite School District. The foundation accepts donations from the public to help the district meet the special needs of its students. The foundation's director and support staff are employees of the Granite School District. It is led by a board consisting of community members. New board members are selected from names proposed by a nominating committee of the board.

**Weber Human Services Foundation.** This not-for-profit raises money to meet the human services needs of the community that would not otherwise be covered by the Weber Human Services District. It is staffed by the employees of the Weber Human Services District, and is directed by a board comprised of Weber Human Services employees and community members.

**Southeastern Utah Economic Development District.** Created by the Southeastern Utah Association of Governments to raise funds to promote economic development. Its main source of funds has been a grant from the US Department of Commerce. The district is staffed by employees of the Southeastern Utah Association of Governments. Its board members represent local governments and businesses in the area.

### **Governmental Nonprofits Face the Same Risk for Fraud, Waste and Abuse as Limited Purpose Entities**

The first two entities described above, the Granite School District Foundation and the Weber Human Services Foundation, do not fit the definition for a governmental nonprofit as stated in HB 55, which was approved by the Legislature and signed into law during the last session. However, because they are so closely affiliated with government agencies and even receive staff support from those agencies, we believe those government agencies would still share some responsibility if fraud, waste or abuse occurred in those foundations.

Our limited review of these organizations found only a few minor concerns with their internal controls. However, we are concerned about the potential risk that these quasi-public entities face as they are somewhat detached from their sponsoring governmental agencies. For this reason, we believe all governmental nonprofits affiliated with a

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**The legislature should consider authorizing a study of the internal controls used by governmental nonprofit organizations.**

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public agency should follow the same best practices for internal control that all governmental agencies are required to follow. If legislators share this concern, they may want to consider authorizing a more thorough review of the controls used by this subgroup of limited purpose entities.

## **Recommendations**

1. We recommend that the Legislature consider requiring the Lieutenant Governor's office to maintain a registry of all local districts, special service districts and interlocal entities in Utah.
2. We recommend that if an entity on the state registry (recommended in #1 above) fails to file the required reports with the Office of the State Auditor, file transparency reports with the Division of Finance, or give public notice of meetings on the Public Notice Website for an entire year, that the state auditor (1) notify the local county commission or council where the entity is located, and (2) be authorized to withhold the entity's tax receipts, or freeze its bank accounts.
3. We recommend that the Legislature consider giving counties authority to oversee limited purpose entities that persistently fail to comply with state laws regarding financial reporting and public notice. The options include (1) requiring voluntary action by the counties upon receiving notice from the state auditor that an entity is non-compliant, or (2) giving counties authority to impose fines, require outside audits and dissolve entities.
4. We recommend that the Legislature direct each county to publish on its website information regarding the boards and commissions of each public organization in the county. The website should list the names of the board members, when meetings are held, when each board member's term expires and the process for applying for any seats on the board that soon may become vacant.
5. We recommend that the Legislature consider authorizing a review of the risk of fraud, waste and abuse within Utah's governmental nonprofit entities.

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## **Appendices**

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**Appendix A**  
**Checklist of Best Practices for Internal Control**

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# Utah State Legislature

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June 20, 2017

TO: ALL BOARD MEMBERS OF UTAH SPECIAL PURPOSE ENTITIES

We recognize the valuable services provided by Utah's special purpose entities, which include our local districts, special service districts, interlocal agencies and independent entities. We also appreciate the important role that you play in guiding the work of these governmental units.

Unfortunately, concerns have arisen with many special purpose entities. Several audits have documented occurrences of fraud, waste, abuse, and poor management among Utah's special purpose entities. In response to these concerns, we asked the Legislative Auditor General to conduct a survey of the internal controls used by a sample of these entities.

The Auditor General has recently completed the survey and found significant control weaknesses were common among these special purpose entities. We are very concerned with these findings. The Auditor General has developed a list of best practices for internal control and governance that describe each best practice at length. The report can be found at [http://le.utah.gov/audit/17\\_05rpt.pdf](http://le.utah.gov/audit/17_05rpt.pdf). We ask that you carefully review each of the best practices identified in the report and ensure they are implemented within your organization. Attached to this letter is a checklist of each of these best practices.

Because of the serious nature of the problems and concerns identified we will continue to aggressively review special service entities for compliance with this best practices list. We intend to assign the Auditor General annual follow-up reviews to verify that these best practices have been successfully implemented.

Thank you for all you do to serve the people of the State of Utah.

Sincerely,

President Wayne Niederhauser  
Co-Chair  
Legislative Audit Subcommittee

Speaker Greg Hughes  
Co-Chair  
Legislative Audit Subcommittee



## Checklist of Best Practices for Board Members Of Special Purpose Entities

<b>Roles of Board and Staff</b>	
See report pages 23 to 27.	
1. The board takes ultimate responsibility for governance of the entity by (1) appointing an executive staff, (2) providing broad policy guidance, (3) authorizing the use of resources, (4) setting goals and expectations, and (5) monitoring results.	<input type="checkbox"/>
2. The board members recognize their role is to be more than just a ceremonial body. They have a responsibility to lead and hold staff accountable for results.	<input type="checkbox"/>
3. The board chair reviews and approves the agenda before each meeting, inviting other board members to propose additional agenda items, if desired.	<input type="checkbox"/>
4. The executive director (a) helps the board draft a set of internal control policies and (b) guides staff as they carry out the board's policies.	<input type="checkbox"/>
5. To protect against fraud, staff duties are segregated such that no one person has control over all parts of a financial transaction.	<input type="checkbox"/>
6. The board appoints a board chair, a treasurer and a clerk.	<input type="checkbox"/>
7. For organizations with an insufficient number of staff to achieve a proper separation of duties, board members serve as treasurer, and clerk.	<input type="checkbox"/>
8. The board approves a staffing policy that defines the responsibilities of all those who handle different aspects of the entity's finances.	<input type="checkbox"/>
9. The board is solely responsible for hiring and directing the audit function.	<input type="checkbox"/>

<b>Internal Controls</b>	
See report pages 28 to 33.	
10. The board approves policies that govern the organization and addresses each best practice described in the best practice audit. This would include policies such as a personnel policy, a procurement policy, and records retention policy. A procurement policy is of particular importance with the recent instances of fraud, waste, and abuse that have occurred.	<input type="checkbox"/>
11. The board regularly reviews a report of entity disbursements. The report includes the date, vendor and amount of each expense since the last board meeting.	<input type="checkbox"/>
12. To control credit purchases, purchase cards (or "p-cards") are issued to a limited number of staff. Limits are placed on the dollar amount, type and number of charges made to each card.	<input type="checkbox"/>
13. An independent person with no book keeping responsibilities is assigned to reconcile the bank statement each month with that month's receipts and expenses.	<input type="checkbox"/>

14. The board requires its formal approval of any expenditure above a certain dollar amount.	<input type="checkbox"/>
15. The board requires that two people sign all local entity checks. Before signing, both signers will review and approve the attached requisition sheet.	<input type="checkbox"/>

<b>Recruiting Qualified Personnel</b> Report pages 33 to 37.	
16. Staff avoid recruiting individuals to serve as board members	<input type="checkbox"/>
17. Local entities publicize the opportunity to apply for any elected board seats that will soon be coming available and any vacant staff positions.	<input type="checkbox"/>
18. Local entities follow an open and objective recruiting process when filling staff positions and hiring outside contractors. Hiring relatives or business associates of the board and management is avoided.	<input type="checkbox"/>
19. Board and staff regularly receive the required training in open and public meetings, board governance and other matters applicable to the entity's mission.	<input type="checkbox"/>
20. When in-house expertise is not available to perform special tasks, the entity hires or appoints qualified outside experts.	<input type="checkbox"/>

<b>Tone at the Top</b> Report pages 38 to 40.	
21. The board adopts a code of ethics that clearly states the organization's values and standards of behavior.	<input type="checkbox"/>
22. The board and management seek opportunities to reinforce the organization's ethical standards during staff meetings, training, and newsletters.	<input type="checkbox"/>
23. The board holds everyone accountable, including management, to high standards of performance.	<input type="checkbox"/>
24. The board and executive director avoid using a compensation system and other incentives that encourage employees to take unnecessary risks.	<input type="checkbox"/>
25. The board provides an ethics hotline and adopts a whistleblower policy.	<input type="checkbox"/>

## **Agency Response**

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June 12, 2017

John M. Schaff, CIA, Auditor General  
Office of the Legislative Auditor General  
W315 Utah State Capitol Complex  
Salt Lake City, UT 84114

Re: Best Practices Audit Response

Dear Mr. Schaff:

The Utah Association of Special Districts (UASD) appreciates the invitation to respond to the Best Practices Audit.

The objective of the UASD is to promote the proper and efficient operation of all Local Districts and Special Service Districts in Utah. Past findings and recommendations generated by the Office of the Legislative Auditor General have been and are being utilized by the UASD to train district board members and management throughout Utah.

The findings, recommendations, and best practices from this audit will be helpful as we continue to provide training, best practices, vision, and focus to our members. It should be noted that some of the entities included in the audit are not districts and do not receive the training and resources provided by the UASD. The UASD has and will continue to promote examples of excellence among districts to all districts in Utah, some of which were noted in the audit. Recommendations from this audit will also be utilized in future training events and in convention presentations.

We appreciate the professionalism and courtesy extended by your staff, and thank them for their efforts in identifying areas that may need improvement, and for providing helpful recommendations. The UASD will continue to work diligently to promote the proper and efficient operation of Local Districts and Special Service Districts in Utah.

Sincerely,

LeGrand W. Bitter  
Executive Director

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