

**Utilities District of Western Indiana  
Rural Electric Membership Cooperative  
August 25, 2017**



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# Executive Summary

## INTRODUCTION

Blue & Co., LLC (Blue) performed an internal control review of the Utilities District of Western Indiana Rural Electric Membership Cooperative's (UDWI) processes for two (2) business functions:

- Board governance
- Accounting policies and procedures

The purpose of the internal control review was to evaluate the current internal control environment over these business functions relative to known leading practices. This report identifies strengths and opportunities for improvement within UDWI and provides recommendations to incorporate additional leading practices into the internal control environment to position UDWI for greater future success.

## BACKGROUND

UDWI, a Touchstone Energy Cooperative, is a member of the Hoosier Energy Power Network and the 4th-largest electric distribution cooperative in southern Indiana, serving over 19,000 meters in Clay, Daviess, Greene, Knox, Lawrence, Martin, Monroe, Owen, Putnam, Sullivan, and Vigo counties for 80 years.

UDWI is part owner of Hoosier Energy, a generation and transmission cooperative providing wholesale electric power and services to 18 member distribution cooperatives in central and southern Indiana and southeastern Illinois. Based in Bloomington, Indiana, Hoosier Energy operates coal, natural gas and renewable energy power plants and delivers power through a 1,500-mile transmission network. Hoosier Energy supplies UDWI with nearly all of UDWI's energy and transmission needs.

## SCOPE

The scope of our engagement as agreed upon, specifically requested Blue to perform an internal control review of the current internal control environment over 2 business functions related to UDWI as \_\_\_\_\_ of

June 1, 2017 including:

- Board Governance
- Accounting policies and procedures

Blue performed fieldwork from June 1, 2017 through June 30, 2017 where we:

- Obtained an understanding of UDWI's organizational structure
- Conducted interviews with UDWI's employees
- Assessed current documentation of key processes
- Evaluated current control environment design effectiveness
- Created a summary of internal control opportunities from interviews, review of existing documentation (primarily financial statements and other internal documents), and market factors for prioritization
- Prioritized internal control improvement opportunities

# Executive Summary

## OBJECTIVE

The objective of this internal control review was to assist UDWI in evaluating its internal control environment over the two business functions and identify control strengths and opportunities for improvement.

## SUMMARY OF OBSERVATIONS

As a result of performing this internal controls review, the following strengths and opportunities for improvement were identified. Our observations are intended to identify opportunities to further improve the internal control environment when compared to common and known leading practices.

Based on factors such as continued growth and lack of transparency between management and the board of directors, the internal control environment may be susceptible to manipulation. While processes are in place to address these risks, our recommendations will further align the UDWI's internal controls with existing leading practices.

### **Key control strengths include:**

- An employee culture that understands the necessity for strong controls and a continuous improvement philosophy
- A board of directors that understands there are opportunities to strengthen UDWI's internal controls and is willing to invest resources to make the necessary enhancements
- As of May 22, 2017 all checks are physically reviewed, approved, and signed by two (2) individuals

### **Opportunities for improvement include:**

- Enhancement of board of directors governing activities, including:
  - Evaluation of board reporting activities
  - Evaluation of current board committees
  - Implementation of a whistle blower policy
  - Review and approval of annual detailed budget
- Development and implementation of approval limits for purchases
- Enforcement of existing vendor selection policy
- Enforcement of existing Policy that requires supporting documentation for all expenses
- Enhancement of petty cash controls and dollar levels
- Categorization of expenses in the general ledger
- Evaluation of cost/benefit of paying for Contractor time off at Christmas
- Analysis of current policies for employee vacation and sick time

# Observations and Recommendations

## DETAILED OBSERVATIONS

Blue has provided detailed observations and recommendations for each of the two business functions. In addition, Blue has worked with UDWI to prioritize each observation within its respective business function.

## BOARD GOVERNANCE

Physical Review and Signing of Checks	
Observations	Business Impact
UDWI currently has a policy that all checks are reviewed, approved, and signed by two (2) of the following three (3) individuals: Board President, Board Treasurer, or Manager of HR/Compliance. While this control is effective during the search for a new Chief Executive Officer (CEO), it may hinder normal business operations once the new CEO has been placed in the role.	Day-to-day business operations of UDWI may not be effectively streamlined due to board oversight.
Recommendation	
We recommend UDWI re-evaluate the approved signors of checks for normal business operations once a new CEO has been selected. Additionally, we recommend the board of directors implement and formally document spending thresholds and approval limits for disbursements in its policies and procedures and communicate those thresholds to UDWI personnel.	

Board Reporting	
Observations	Business Impact
Currently, UDWI receives reports and other information as decided by the CEO, and there have been times when essential information was not provided to the full board.	The board of directors did not always receive necessary or complete information to make business decisions and effectively govern.
Recommendation	
We recommend that the board of directors determine what information needs to be reported on a regular basis based on their needs and communicate the required reporting to the CEO and senior management. Thereafter, the board of directors should periodically evaluate whether the information provided by management is organized effectively and provides sufficient level of detail and substantive content and direct any changes that may be necessary.	

## Observations and Recommendations

Board Committees	
Observations	Business Impact
<p>UDWI's board of directors currently operates with the following committees:</p> <ul style="list-style-type: none"> <li>• Building Committee</li> <li>• Equipment Committee</li> <li>• Bylaws &amp; Policy Committee</li> <li>• Labor and Negotiation Committee</li> <li>• Redistricting Committee</li> <li>• Solar Committee</li> <li>• Member Relations Committee</li> </ul>	<p>The board of directors may have inactive committees based on the overall size of the board of directors, leading to ineffective board governance.</p>
Recommendation	
<p>We recommend that the board continue to evaluate the need for its current standing committees. For each current committee, the board should ask whether the committee is necessary. If the committee is necessary, then the board should ensure the committee is actively performing its assigned duties. If the committee is not necessary, the board should consider whether to eliminate the committee to free up board time and attention for more important matters.</p> <p>Additionally, we recommend the board establish an audit committee. An audit committee is typically responsible for an entity's financial reporting, internal control system, risk management, and internal and external audit functions. An audit committee reports its activities, findings, and recommendation to the full board for board action when necessary. Delegating these activities to an Audit Committee will be more efficient than having full board involved at a detailed level, and will lead to more proactive and timely oversight over the financial and accounting activities of the company.</p>	

Whistle Blower Policy	
Observations	Business Impact
<p>UDWI does not currently have a whistle blower policy.</p>	<p>An employee may be pressured into not following UDWI's policies and procedures by their supervisor, with no effective avenue to report the event. Furthermore, without a whistleblower policy, employees and board members do not have clarity on how and to whom to report problems.</p>
Recommendation	
<p>We recommend that UDWI consider developing and implementing a whistle blower policy to give employees an avenue to communicate activities that they believe are not in conformance with UDWI's policies and procedures.</p>	

## Observations and Recommendations

Annual Budget Approval Process	
Observations	Business Impact
The board of directors was only provided a high-level budget to review and approve on an annual basis, which does not allow for a review of the actual detail that makes up a particular budgeted line item.	The board of directors did not receive the information necessary to determine whether UDWI's strategic goals and objectives for the upcoming year were projected to be accomplished. Furthermore, the board of director's ability to be flexible based on the industry's changing environment and to monitor revenues and expenses throughout the year was limited because the annual budget did not provide enough detail.
Recommendation	
We recommend that the board of directors review and approve the detailed line item budget on an annual basis. Additionally, we recommend that the board of directors receive a "budget vs. Actual" comparison on a monthly basis; including highlighting those items with a percentage change over a certain threshold as determined by the board of directors.	

### ACCOUNTING FINDINGS

Purchase Thresholds and Approval Limits	
Observations	Business Impact
UDWI has documented policies and procedures; however, the policies and procedures do not identify approval limits and thresholds for disbursements such as checks and ACH payments. At times major items such as property were purchased without explicit approval from the full board.	The lack of any disbursement limits essentially gave management unlimited authority to make purchases and enter into contracts without the need for full board approval.
Recommendation	
We recommend UDWI implement and formally document in its policies and procedures disbursement approval limits and thresholds and communicate those thresholds to UDWI personnel.	

## Observations and Recommendations

Vendor Approval Policy	
Observations	Business Impact
While UDWI has policies and procedures for selecting vendors and obtaining competitive bids, those policies and procedures were not always followed by management. Furthermore, there have been times when essential information relating to vendor selection was not provided to the full board.	The board of directors received inaccurate information to make necessary business decisions. Furthermore, if UDWI does not follow the proper procedures to select a vendor, UDWI might select a vendor that is not the most qualified or not offering the best price and terms for the work.
Recommendation	
We recommend that UDWI continue to evaluate the need of enhancing current policies and procedures for vendor selection to include dollar thresholds, vendor due-diligence steps, and vendor master list review.	

Adequate Supporting Documentation for Expenditures	
Observations	Business Impact
In many instances, the CEO and other staff did not comply with the employee handbook policy, which requires employees to provide adequate supporting documentation for all allowable and reimbursable business expenses paid for with either an employee's personal or company credit card.	UDWI personnel could have been reimbursed for non-allowable expenses without providing supporting documentation. Furthermore, lack of oversight of employee expense reimbursements could lead to intentional abuse by employees if they know expenses will not be scrutinized.
Recommendation	
We recommend that all expenses, including travel expenses, have adequate supporting documentation to document the amount, date, place, and business purpose in accordance with the employee handbook and that the full board or an audit committee review expenses and documentation on a regular basis.	

Petty Cash Documentation	
Observations	Business Impact
In many instances, withdrawals from the account commonly referred to as the "Wire Fund" did not have documentation to support the amount, date, place, and business purpose for the funds used.	Non-allowable expenses or expenses that were personal in nature could have been paid for with UDWI funds.
Recommendation	
We recommend that all transactions recorded in the General Ledger, including the account commonly referred to as the "Wire Fund" have adequate supporting documentation to document the amount, date, place, and business purpose in accordance with the employee handbook.	

## Observations and Recommendations

Petty Cash Limit	
Observations	Business Impact
We noted that the current maximum amount of cash maintained in the office is more than the recommended amount for a company of this size.	Monies maintained in the office could be better utilized to serve UDWI's members in the general cash account.
Recommendation	
We recommend that the board of directors evaluate the need to maintain the current level of cash on site for business purposes. Typically, the range of a petty cash fund is between \$200 and \$500.	

Monthly Credit Card Review	
Observations	Business Impact
In many instances, the CEO and other staff did not comply with the employee handbook policy, which requires that all charges on UDWI issued credit cards have documentation to support the expenses.	Non-allowable expenses or expenses that are personal in nature could have been paid for with UDWI funds.
Recommendation	
We recommend that on a monthly basis all credit card expenses are reviewed and approved with all appropriate supporting documentation to ensure all expenses are allowable business expenses. This monthly review could be performed by the employee's supervisor and/or the office manager. For CEO expenses, the full board or an audit committee should review expenses and documentation on a regular basis.	

Employee Morale and Team Building Expenses	
Observations	Business Impact
Expenses to assist with employee morale and team building, such as Indianapolis Indians tickets and Christmas party expenses, were improperly coded to general ledger accounts titled "Key Accounts" and "Employee Pensions and Benefits."	The board of directors received inaccurate and misleading information to make necessary business decisions. Furthermore, the inconsistent and non-transparent manner in which these expenses were recorded in the general ledger means that the board could not effectively monitor these expenses and determine whether they are in-line with board expectations.
Recommendation	
We recommend that UDWI evaluate the cost/benefit of recording all expenses related to employee morale and team building in a separate general ledger account so that expenses can be monitored more effectively and efficiently. Furthermore, we recommend that the board of directors establish an annual budget for these types of expenses to provide guidance to management as to what level of employee morale and team building expenses are appropriate.	

## Observations and Recommendations

Key Account Tickets	
Observations	Business Impact
Tickets for sporting events were improperly coded and recorded in the general ledger account called "Key Accounts", but some of the tickets were used for personal use or for purposes other than maintaining and developing relationships with "Key Accounts". At times non-allowable expenses or expenses that are personal in nature were paid for with UDWI funds.	UDWI funds were not utilized in the most effective and efficient way to serve its members. The board of directors received inaccurate and misleading information to make necessary business decisions. Furthermore, the inconsistent and non-transparent manner in which these expenses were recorded in the general ledger means that the board could not effectively monitor these expenses and determine whether they are in-line with board expectations.
Recommendation	
We recommend that if tickets for sporting events are purchased for the business purpose of maintaining customer relationships; those tickets should be recorded in "Key Accounts" and the tickets should be offered to customers identified by UDWI. Furthermore, we recommend that the board of directors establish an annual budget for these types of expenses to provide guidance to management as to what level of expenses are appropriate relating to maintaining and developing relationships with "Key Accounts".	

Contractor Christmas Time Off	
Observations	Business Impact
It has been UDWI's practice to give its contractors "days off" with pay at Christmas to mirror the time off that the inside employees receive.	UDWI funds were not utilized in the most effective and efficient way to serve its members. Furthermore, this practice ignores the fact that contractors are responsible for compensating and providing benefits (including vacation) to their employees.
Recommendation	
We recommend that UDWI discontinue the "days off" with pay at Christmas for the contractors because it is not the most effective use of UDWI's funds to serve its members.	

Vacation and Sick Time	
Observations	Business Impact
We noted that the employee handbook states that employees can accrue vacation and sick leave time. Additionally, the Employee Handbook states the CEO may pay out an employees unused vacation time at the end of each year based on economic conditions.	Employees may not take adequate time off to "unplug" from UDWI operations to assist in avoiding burnout. Additionally, UDWI may incur greater employee costs if unused vacation time is paid out on an annual basis.
Recommendation	
We recommend that the board of directors and senior management continue to evaluate the nature of these policies and procedures to determine if a change would be more beneficial for employees and UDWI's members.	

## Observations and Recommendations

Employee Cash Bonuses	
Observations	Business Impact
Some UDWI employee bonuses were not recorded properly.	The inconsistent and non-transparent manner in which these expenses were recorded in the general ledger means that the board could not effectively monitor these expenses and determine whether they were in-line with board expectations.
Recommendation	
We recommend that any bonuses issued by UDWI be done through payroll in accordance with proper accounting practices.	

Internal Control Follow-Up	
Observations	Business Impact
The UDWI board of directors is in the process of evaluating current operating policies and procedures to enhance the internal control environment.	UDWI policies and procedures that were identified to be unclear as to actual expectations for operations may be changed to strengthen the internal control environment.
Recommendation	
We recommend that the board of directors either perform an internal review or hire a third party to review the implementation of enhanced policies and procedures to ensure internal controls are operating as intended. Additionally, we recommend this review be performed 6 – 12 months after the policies and procedures have been implemented.	