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October 9, 2009

Audit Committee Members of New York City Municipal Water Finance Authority
75 Park Place
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Audit Committee Members of New York City Water Board
59-17 Junction Boulevard, 8th Floor
Flushing, NY 11373-5108

Management of New York City Municipal Water Finance Authority
75 Park Place
New York, NY 10007

Management of New York City Water Board
59-17 Junction Boulevard, 8th Floor
Flushing, NY 11373-5108

Dear Audit Committee Members and Management:

In planning and performing our audit of the financial statements of New York Municipal Water Finance Authority and New York City Water Board, which collectively comprise the New York City Water and Sewer System (the "System") as of and for the year ended June 30, 2009 (on which we have issued our report dated October 9, 2009 which included an explanatory paragraph for a change in accounting for pollution remediation obligations to conform to GASB Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*), in accordance with auditing standards generally accepted in the United States of America, we considered the System's internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the System's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the System's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, in connection with our audit, we have identified, and included in the attached Appendix, observations related to the System's internal control over financial reporting as of June 30, 2009 that we wish to bring to your attention

We have previously communicated certain matters noted during our audit of the financial statements of the System for the year ended June 30, 2008 which we considered to be material weaknesses, in our report to management and those charged with governance dated October 10, 2008. As of the date of this report, we believe the System is still in the process of remediating certain of these material weaknesses. We have outlined in the attached Appendix those previously-reported matters which we believe are in the process of being remediated.

The definitions of a deficiency, a material weakness, and a significant deficiency are also set forth in the attached Appendix.

Although we have included management's written response to our comments in the attached Appendix, such responses have not been subjected to the auditing procedures applied in our audit and, accordingly, we do not express an opinion or provide any form of assurance on the appropriateness of the responses or the effectiveness of any corrective actions described therein.

This report is intended solely for the information and use of management, Audit Committee members, and others within the organization and is not intended to be, and should not be, used by anyone other than these specified parties.

Yours truly,

Deloitte & Touche LLP

APPENDIX

SECTION I — OBSERVATIONS

Our observations concerning other matters related to operations and best practices involving internal control over financial reporting that we wish to bring to your attention are as follows:

1. **Accounts Receivable – Maintaining Check Copies**

<u>Observation</u>

Customers have the option to pay their water and sewer bill via check. We observed that a check can sometimes be processed and sent to the bank without making a copy to maintain in the files at DEP. Often, checks are deposited in batches and it is difficult to obtain the copy of a specific check once it has been deposited to the bank. As a result, we were unable to agree selections of customer payments to the underlying check copy.

<u>Impact</u>

The purpose of the audit trail is to allow verification of the balance in an account by tracing the selected amount to the source document. When no source document can be viewed, integrity is lost. Additionally, poor audit trails can create opportunities for fraud.

<u>Recommendation</u>

We recommend that DEP make a photocopy of each customer payment check prior to deposit.

<u>Management's Response</u>

Management understands the importance of obtaining and retaining photocopies of all payments made via check. Existing processes were reviewed and altered to address this issue. New procedures and processes have been implemented to further ensure all paper check payments received and processed by our Central and Borough locations will be copied and stored electronically as well as physically. Copies of all check payments made through outside agents of the NYCWB, such as NYCServ, an entity of the Department of Finance, are available upon request. Electronic files of all customer account payments made through NYCServ or other entities are delivered to the NYCWB/DEP OIT daily for account updates. Payments are sent by wire transfer.

2. Department of Environmental Protection (DEP)– Terminated Users With Active Application IDs

Observation

An assessment of the NYC Water and Sewer CIS application environment identified four terminated users who continued to have active application IDs.

Impact

To test the process of user access termination, we compared the CIS active user listing to the terminated users listing from Human Resources. This process identified four terminated users who continued to have active application IDs. Unauthorized access and the integrity of data can be compromised when terminated users have access to the application.

Recommendation

Management should consider establishing a process to revoke the access of terminated users from CIS in a timely manner. Recertifying users' access on a periodic basis, minimizes future occurrences and protects the system from unauthorized access

Corrective Action Taken

Management deleted the accounts for the 4 terminated users as of 08/28/09.

Management's Response

Additional procedures will be implemented in response to the recommendations. Inclusion of the Quality Assurance Unit and a 'termination document' requirement as a back up will further ensure these changes address any weakness in this area.

SECTION II — MATERIAL WEAKNESSES IDENTIFIED IN A PREVIOUS AUDIT THAT ARE IN THE PROCESS OF BEING REMEDIATED

We identified and previously communicated the following deficiencies that were considered to be a material weakness in the System's internal control over financial reporting during our audit of the financial statements of the System for the year ended June 30, 2008. As of the date of this report, we believe these deficiencies have not yet been remediated by the System**:**

1. Accounts Receivable – Customer Information System

Observation Communicated in Letter Dated October 10, 2008

The Accounts receivable system currently utilized by the Authority does not provide sufficient, reliable real-time information to allow management to determine an accurate accounting of customer accounts receivables. It was noted that the current configuration of the system requires many adjustments that potentially result in the inclusion of incorrect information within the system, and also, does not produce a reliable aging of accounts receivable. For example, in many circumstances, balances are adjusted by crediting the entire balance and establishing the receivable with a totally new entry. As a result, the system ages the balance based upon the date of the new entry instead of the date which the receivable was originally created resulting in an inaccurate aging. In order to determine an accurate aging, management is required to perform an extensive analysis of each account which results in inefficiencies and is subject to error. This also results in the inability to produce current, reliable information due to the time requirements necessary to undertake this effort. Therefore, given the current work load demands, aging is performed only on a sporadic basis, generally annually. In addition, adjustments are made to accounts receivable without documentation of an independent review. Therefore, it is difficult to determine if the appropriate segregation of duties over the adjustment process is being exercised. This situation could result in inappropriate adjustments, inaccuracies and abuse.

We have also observed that the system does not have the in-house capabilities to review the current accounts receivable required to make accurate judgments concerning the collectability of receivables; thus creating the potential for a material misstatement of accounts receivable amounts in the financial statements.

Management's Response Communicated in Letter Dated October 10, 2008

Management understands that the accounts' receivable reporting has been an ongoing issue for the System. In FY 2008, it began the procurement process for a new billing and customer information tracking system.

Such a new system will address the recommendations noted above. Management will also examine the technical and resource requirements required to address the recommendations that DEP establish procedures to provide for an independent review of receivable adjustments and review the collectability of receivables at least quarterly.

2009 Update

The current configuration of the system still requires many adjustments that potentially result in the inclusion of incorrect information within the system, and also, does not produce a reliable aging of accounts receivable. However, we observed that management has created a report that calculates a reserve for each customer account based on a computer-designed logic. During our testing, we did not note any material differences between our expectation of the reserve for selected customer accounts and the reserve assigned to that customer account by the report.

Management has begun the procurement process for a new billing and customer information tracking system. Because of this and the aforementioned improvement of management's ability to assess customer account reserves, we have not identified this as a material weakness in the current year.

Management's Response

Management is continuing to pursue the procurement process for a replacement customer billing and tracking system. The inclusion of appropriate controls and measures to effectively age and report on Accounts Receivables is of the highest importance and is a requirement.

SECTION III — DEFINITIONS

The definitions of a deficiency, a material weakness, and a significant deficiency that are established in AU 325, *Communicating Internal Control Related Matters Identified in an Audit*, are as follows:

A *deficiency* in internal control over financial reporting exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when (a) a properly designed control does not operate as designed, or (b) the person performing the control does not possess the necessary authority or competence to perform the control effectively.

A *material weakness* is a deficiency, or combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

A *significant deficiency* is a deficiency, or combination of deficiencies, in internal control over financial reporting that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

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