



Town of Hartwick

Financial Condition

Report of Examination

Period Covered:

January 1, 2012 — March 8, 2013

2013M-118



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

September 2013

Dear Town Officials:

A top priority of the Office of the State Comptroller is to help local government officials manage government resources efficiently and effectively and, by so doing, provide accountability for tax dollars spent to support government operations. The Comptroller oversees the fiscal affairs of local governments statewide, as well as compliance with relevant statutes and observance of good business practices. This fiscal oversight is accomplished, in part, through our audits, which identify opportunities for improving operations and Town Board governance. Audits also can identify strategies to reduce costs and to strengthen controls intended to safeguard local government assets.

Following is a report of our audit of the Town of Hartwick, entitled Financial Condition. This audit was conducted pursuant to Article V, Section 1 of the State Constitution and the State Comptroller's authority as set forth in Article 3 of the General Municipal Law.

This audit's results and recommendations are resources for local government officials to use in effectively managing operations and in meeting the expectations of their constituents. If you have questions about this report, please feel free to contact the local regional office for your county, as listed at the end of this report.

Respectfully submitted,

*Office of the State Comptroller
Division of Local Government
and School Accountability*

Introduction

Background

The Town of Hartwick (Town) is located in Otsego County and has 2,110 residents. The Board comprises four elected Board members and the elected Town Supervisor (Supervisor) who governs the Town. The Board is responsible for the general management and control of the Town's finances and operations and protection of Town assets. The Supervisor,¹ as the chief fiscal officer, is responsible for maintaining accounting records and providing monthly reports to the Board. The elected Town Clerk has also been appointed the Tax Collector and is responsible for maintaining records and licenses issued by the Town and collecting real property taxes. The elected Town Justice is responsible for adjudicating tickets and setting fines.

The Town provides various services including general government support, justice court, road repair and maintenance, snow removal, fire protection, municipal lighting, water services, and a library. The Town's budgeted appropriations for the 2013 fiscal year are \$657,386 for the general fund, \$755,306 for the highway fund, \$155,794 for the water fund, \$146,016 for the fire protection fund, \$58,002 for the library fund, and \$6,000 for the lighting district fund. These appropriations are funded mainly through real property taxes, sales tax, State aid,² and user fees.

Objective

The objective of our audit was to ensure that the Board properly monitored the Town's financial operations. Our audit addressed the following related question:

- Did the Board ensure that the Town's financial plans were reasonable?

Scope and Methodology

We examined the financial records of the Town for the period January 1, 2012, to March 8, 2013. We extended our scope to include the 2008 to 2011 fiscal years to determine the Town's financial trends. We also reviewed the tax rates, levies, and assessments for the same extended period.

We conducted our audit in accordance with generally accepted government auditing standards (GAGAS). More information on such standards and the methodology used in performing this audit are included in Appendix B of this report.

¹ The current Supervisor took office in January 2012. The fiscal year 2012 budget was adopted by the Board in November 2011.

² Consolidated Local Street and Highway Improvement Program (CHIPS)

**Comments of
Local Officials and
Corrective Action**

The results of our audit and recommendations have been discussed with Town officials and their comments, which appear in Appendix A, have been considered in preparing this report. Town officials generally agreed with our recommendations and indicated they plan to take corrective action.

The Board has the responsibility to initiate corrective action. A written corrective action plan (CAP) that addresses the findings and recommendations in this report should be prepared and forwarded to our office within 90 days, pursuant to Section 35 of the General Municipal Law. For more information on preparing and filing your CAP, please refer to our brochure, *Responding to an OSC Audit Report*, which you received with the draft audit report. We encourage the Board to make this plan available for public review in the Town Clerk's office.

Financial Condition

The Board generally has the authority and responsibility to adopt realistic, structurally balanced budgets and to monitor the budget so that services are delivered within the limits provided. A sound budget should include ongoing revenue sources to finance operations. In addition, the Town can set aside, in legally established reserves, portions of that fund balance to finance future costs for a variety of specified objects or purposes. However, Town officials should not routinely rely on fund balance as a financing source for operations; this practice can deplete the fund balance to dangerous levels, leaving little money at year-end for cash flow purposes or unexpected events. The amount of real property taxes to be levied should be the final piece of the budget preparation process, after all estimated revenue and expenditures are included. Monitoring actual revenues and expenditures throughout the year enables the Board to identify any variances that might cause the Town to end the year with a significant surplus or deficit, and make the necessary budget amendments throughout the year.

The Board did not establish reasonable financial plans for three of its major operating funds but repeatedly relied on transfers from the general fund and appropriations of fund balance to finance operations in the highway and fire protection funds. Although Town officials accounted for these three funds individually, they maintained a consolidated checking account for the combined funds and paid for large purchases without verifying that the fund balance was actually available. As a result, the financial condition of the three funds deteriorated significantly over the past four years. While the Town's overall tax levy (for the general, highway, fire protection, library, lighting district, and water funds) was relatively steady over the past four years,³ the general and highway funds' budgeted tax fluctuated significantly and failed to consistently fund operations.

General Fund — Between 2009 and 2012, Town officials made \$550,000 in unplanned transfers to the highway fund and \$20,000 to the fire protection fund to keep those funds solvent. The reliance on the general fund to subsidize these other two funds resulted in the depletion of the general fund's year-end fund balance from \$780,195 in 2009 to \$220,688 in 2012. Had Town officials budgeted more realistically for the highway fund, rather than reallocating the \$550,000 from the general fund, the year-end fund balance of the general fund at the end of 2011 would have, in fact, maintained its

³ \$802,397 in 2009, \$814,534 in 2010, \$799,295 in 2011, and \$907,406 in 2012

previously healthy level.⁴ Going into 2013, the general fund had no unexpended surplus funds⁵ available for unexpected events or cash flow maintenance.

Table 1: Fund Balance – General Fund				
	FY 2009	FY 2010	FY 2011	FY 2012
Beginning Fund Balance	\$731,223	\$780,195	\$458,797	\$287,134
Revenues	\$548,730	\$719,249	\$579,252	\$492,733
Expenditures	\$499,758	\$640,647	\$606,915	\$539,179
Operating Surplus/ (Deficit)	\$48,972	\$78,602	(\$27,663)	(\$46,446)
Plus: Transfers From Other Funds	\$0	\$0	\$6,000	\$0
Less: Transfers to Other Funds	\$0	(\$400,000)	(\$150,000)	(\$20,000)
Year-End Fund Balance	\$780,195	\$458,797^a	\$287,134^a	\$220,688
Less: Following Year Appropriated Fund Balance	(\$300,000)	(\$265,000)	(\$250,000)	(\$270,475)
Total Unexpended Funds	\$480,195	\$193,797	\$37,134	(\$49,787)
Following Year Budgeted Tax Levy	\$339,135	\$ 249,519	\$132,248	\$134,761
^a These amounts include our calculations reflecting the Town’s prior-period adjustment in 2012, which was primarily to correct unreported real property tax revenue.				

The appropriated fund balance was not actually used because Town officials over-budgeted general fund appropriations. Therefore, the general fund will likely avoid total depletion in 2013. Had the appropriations of fund balance been used, the general fund could not have supported its significant (unplanned) transfers to the highway fund and would have run out of cash.

Although the appropriated fund balance within the general fund was not expended for general fund expenditures, the fund advances to

⁴ \$550,000 + \$220,688 (2012 fund balance) = \$770,688

⁵ The Governmental Accounting Standards Board (GASB) issued Statement 54, which replaces the fund balance classifications of reserved and unreserved with new classifications: non spendable, restricted, and unrestricted (comprising committed, assigned, and unassigned funds). The requirements of Statement 54 are effective for fiscal years ending June 30, 2011 and beyond. To ease comparability between fiscal years ending before and after the implementation of Statement 54, we will use the term “unexpended surplus funds” to refer to that portion of fund balance that was classified as unreserved, unappropriated (prior to Statement 54), and is now classified as unrestricted, less any amounts appropriated for the ensuing year’s budget (after Statement 54).

the highway fund caused the year-end fund balance of the general fund to decline from about \$459,000 in 2010 to \$287,000 in 2011. Town officials attempted to stabilize the 2012 overall tax levy with reductions in general fund levy due to the growth of highway fund appropriations (see following comments under Highway Fund), which required the use of appropriated fund balance for operations and increased the risk of depleting the general fund. Town officials indicated that they did not have a full understanding of fund balance and used the commingled checking-account funds as a common resource for the various operating funds.

It is critical that Town officials discontinue using the general fund to subsidize other funds and develop structurally sound budgets for each fund without relying on fund balance.

Highway Fund — Between 2009 and 2012, the Board adopted budgets that appropriated an average of \$191,000 in fund balance for the following year. However, for 2010 the Board planned to appropriate \$450,000 in surplus fund balance when only \$41,000 was actually available for use, and for 2011 planned to spend \$200,000 in surplus fund balance with only \$7,600 available for use. These consecutive errors required unplanned transfers from the general fund of \$400,000 in 2010 and \$150,000 in 2011. While the highway fund’s expenditures were somewhat less than budgeted, its actual available funds could not support these expenditures. Town officials also made one-time equipment purchases in 2010 and 2011, totaling \$384,176, paid for with current resources.

Although the highway fund’s operating results were improving, even with the influx of advanced moneys the year-end fund balance was down to just \$14,500 in 2011. Officials had budgeted a 63 percent tax levy increase (from \$353,262 to \$575,088) in this fund for 2012 in anticipation of increased spending.

	FY 2009	FY 2010	FY 2011	FY 2012
Beginning Fund Balance	\$309,723	\$41,292	\$7,646	\$14,496
Revenues	\$623,409	\$325,712	\$466,156 ^a	\$768,465 ^b
Expenditures	\$891,840	\$759,358	\$609,306	\$625,857
Operating Surplus/(Deficit)	(\$268,431)	(\$433,646)	(\$143,150)	\$142,608
Plus: Transfers From General Fund	\$0	\$400,000	\$150,000	\$0
Less: Transfers to Other Funds	\$0	\$0	\$0	\$0
Year-End Fund Balance	\$41,292	\$7,646	\$14,496	\$157,104
Less: Following Year Appropriated Fund Balance	(\$450,000)	(\$200,000)	(\$50,000)	(\$64,791)
Total Unexpended Funds	(\$408,708)	(\$192,354)	(\$35,504)	\$92,313
Following Year Budgeted Tax Levy	\$296,689	\$353,262	\$575,088	\$586,015
^a Includes \$96,452 in CHIPS reimbursement				
^b Includes \$161,346 in CHIPS reimbursement				

The current Supervisor told us that the Town now plans to reduce its highway expenditures but will continue highway improvement projects that are likely to be reimbursed through CHIPS aid. From 2011 to 2012, CHIPS reimbursements and real property taxes increased the fund balance sufficiently to cover appropriations and reverse the highway fund's pattern of operating deficits. To help maintain this positive condition, Town officials must discontinue the use of fund balance as a financing source unless there is enough fund balance on hand for this purpose. It is important for the Board to develop realistic budgets for each individual fund with adequate revenues to finance expenditures, which will help stabilize the tax levy.

Fire Protection Fund — This fund's operating results declined steeply from a surplus of \$18,750 in 2009 to a deficit of \$58,928 in 2012. The fund balance of \$42,725 at the end of 2011 was not sufficient to finance the next year's operations; therefore, Town officials transferred \$20,000 from the general fund to the fire protection fund. Even with this transfer, the fire protection fund began 2013 with only \$3,797 in fund balance, an 89 percent decline from 2009.

Table 3: Fund Balance – Fire Protection Fund				
	FY 2009	FY 2010	FY 2011	FY 2012
Beginning Fund Balance	\$15,186	\$33,936	\$38,967	\$42,725
Revenues	\$126,512	\$118,709	\$139,340	\$143,189
Expenditures	\$107,762	\$113,678	\$135,582	\$202,117
Operating Surplus/(Deficit)	\$18,750	\$5,031	\$3,758	(\$58,928)
Plus: Transfers From General Fund	\$0	\$0	\$0	\$20,000
Less: Transfers to Other Funds	\$0	\$0	\$0	\$0
Year-End Fund Balance	\$33,936	\$38,967	\$42,725	\$3,797
Less: Following Year Appropriated Fund Balance	(\$20,000)	\$0	\$0	(\$820)
Total Unexpended Funds	\$13,936	\$38,967	\$42,725	\$2,977
Following Year Budgeted Tax Levy	\$118,555	\$138,834	\$142,390	\$145,096

These significant budgetary issues occurred because Town officials believed they had more fund balance than was actually available and did not curtail expenditures. While they accounted for these three operating funds individually, the records did not reflect the amount of money actually held in the Town's checking account.⁶ The commingling of fund moneys within a single checking account further obscured the fund balances that were actually available. The Board also did not consider operating results beyond the immediate prior year in developing estimates for revenues and expenditures and

⁶ Cash was understated by \$60,000 as of December 31, 2011. We also identified an incorrectly calculated tax levy for 2010, which was about \$52,000 more than it should have been, and another \$8,000 in unaccounted-for revenues.

did not develop long-term financial plans, including provisions for future capital needs. If these practices are not corrected, the Town's delivery of services to its residents could be in jeopardy.

In its 2013 adopted budget, the Board again appropriated more fund balance in the general fund than was available; due to the inaccuracy of Town records, the accounting system projected a larger fund balance amount for year-end 2012 than was actually the case.⁷ However, the highway fund budget calls for the appropriation of \$65,000 in fund balance which is well below the \$157,000 actually available. Although the fire protection fund has not relied on appropriated fund balance in recent years, its fund balance has been dangerously depleted. A better understanding of fund balance and structurally sound budgeting practices will enable Town officials to improve the Town's financial condition.

Recommendations

1. The Board should manage each fund's operations separately, with sufficient revenues included in the budget for each fund. Town officials should consider separate checking accounts for each operating fund or require a monthly report of cash balances by fund which accounts for the balance in the combined account. The Board should monitor fund balance levels for each operating fund throughout the year and develop realistic estimates of the amount of fund balance that will be available at year end.
2. The Board and Town officials should ensure that the financial records are accurate and up to date, and should request and review monthly budget status reports.
3. The Board should consider long-term trends and needs when preparing budget estimates. Non-routine purchases, such as highway equipment purchases, should be specifically provided for in the budget. Town officials should consider attending training offered by OSC for local government officials.⁸

⁷ The Board appropriated over \$270,000 when actual available fund balance totaled under \$221,000.

⁸ Training and contact information is available at <http://www.osc.state.ny.us/localgov/training/index.htm>

APPENDIX A
RESPONSE FROM LOCAL OFFICIALS

The local officials' response to this audit can be found on the following page.

TOWN OF HARTWICK
Town Supervisor
PO Box 240, Hartwick, NY 13348
Phone: 607-293-8134 Fax: 607-293-7914

August 26, 2013

H. Todd Eames, Chief Examiner
State Office Building, Suite 1702
44 Hawley Street
Binghamton, New York 13901-4417

Mr. Eames,

This letter is provided as the Response to the *Town of Hartwick Financial Condition Report of Examination* (2013M-118). First and foremost, the Town wants to thank the OSC personnel who performed the audit. These individuals were very professional and helpful. They took every effort to ensure Town personnel were apprised of every step of the process and provided every opportunity to answer questions or provide alternative explanations.

The Town agrees with the findings provided in the aforementioned report and finds itself fortunate to have the Office of the State Comptroller step in when it did. After reviewing the report and those records evaluated therein, it is clear to the current administration that the financial oversight of the previous Chief Fiscal Officer (CFO) and the related inaccuracy in reporting and managing fund balance has put the Town in a precarious position. It is clear that the Town Board—in full—is responsible for the financial condition of the Town and said Board has too long relied upon the financial recommendation and guidance of its CFO in making financial decisions. This past practice will not continue.

Our recently acquired [REDACTED] Software which includes detailed monthly reporting capabilities will provide the current and future Boards with the tools to better monitor the Town's finances. Beginning with the preparation of the 2014 Budget (Fall, 2013), the Town will endeavor to better evaluate its finances while ensuring that appropriations, revenues, and use of fund balance are projected with the intent to improve the Town's long term financial condition without a short-term gouging of the taxpayers.

Additionally, as CFO, I am making it common practice to encourage all Town Board members to engage in municipal accounting educational opportunities and require reporting from participating members to the Board so that all may benefit. As CFO, I will ensure full access to current financial reports and assist Board Members in accessing, reviewing, and understanding said reports or connecting them with appropriate officials to answer those questions I cannot.

Again, the Town agrees with the stated findings and is already making strides to improve not only our financial condition but also the Town's understanding of the financial process. Thank you for helping us better serve the citizens of the Town of Hartwick.

David J. Butlér, Supervisor

The Town of Hartwick is an equal opportunity provider and employer. Discrimination is prohibited by Federal Law. To file a complaint of discrimination, write: USDA, Director, Office of Civil Rights, Washington, DC 20250-9410, or call (202) 720-5964 (voice or TDD).

APPENDIX B

AUDIT METHODOLOGY AND STANDARDS

To accomplish our audit objective, we interviewed appropriate Town officials and employees, tested selected records, and examined pertinent documents. Our procedures included the following:

- We reviewed the Town's financial information and documented the trends in results of operations for the general, highway, and fire protection funds for the 2008 to 2012 fiscal years.
- We reviewed the trend of the property tax rates, levies, and assessments for the 2008 to 2013 (budgeted) fiscal years.
- We performed an analysis of budget-to-actual revenues and expenditures for the 2008 through 2012 fiscal years. We also compared the budget appropriation and revenue lines to the actual expenditures and revenues to determine if any line items were over-expended without a budget transfer being done first.
- We analyzed the Town's financial information reported from the annual update document (AUD) for the 2008 to 2012 fiscal years to determine the Town's financial condition by reviewing the trend of fund balance, reserve funds, and appropriated fund balance.
- We reviewed interfund transfer trends over the 2008 to 2012 fiscal years.
- We interviewed Town officials to gain an understanding of the Town's budget development process for the 2012-2013 fiscal years and to determine what reports are prepared and provided to the Board for monitoring the budget. We also inquired whether the Town has established legal reserves.
- We reviewed the bank reconciliation for December 2012 and verified the authenticity of the paper bank statements.
- We compared a sample of 20 account codes from the AUD to the accounting records to determine if AUD data was consistent with the accounting records. Our sample comprised five cash accounts from the general, highway, and fire protection funds, which we judgmentally selected based on discrepancies between recorded cash amounts and the Town's checking account, and five non-cash accounts that we randomly selected from each of the three funds.

We conducted this performance audit in accordance with generally accepted government auditing standards (GAGAS). Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

APPENDIX C

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Andrew A. SanFilippo, Executive Deputy Comptroller
Nathalie N. Carey, Assistant Comptroller

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