



ALAN G. HEVESI
COMPTROLLER

STATE OF NEW YORK
OFFICE OF THE STATE COMPTROLLER
110 STATE STREET
ALBANY, NEW YORK 12236

MARK P. PATTISON
DEPUTY COMPTROLLER
DIVISION OF LOCAL GOVERNMENT SERVICES
AND ECONOMIC DEVELOPMENT
Tel: (518) 474-4037 Fax: (518) 486-6479

April 5, 2006

Report No. B1-6-01

The Honorable David Carucci and
Members of the Common Council
City of Olean
101 East State Street
Olean, New York 14760-0668

Dear Mayor Carucci and Members of the Common Council:

Our Office has recently completed an audit of the City of Olean (City) budget for the 2006-07 fiscal year. The objective of the audit was to provide an independent evaluation of the tentative budget. Our audit addressed the following questions related to the City's budget for the 2006-07 fiscal year:

- Are the City's revenue and expenditure projections in the proposed budget reasonable?
- Is the City's budget structurally balanced so that recurring costs are financed with recurring revenues?

We conducted our audit in accordance with Generally Accepted Government Auditing Standards (GAGAS) with the exception of reporting views of responsible officials which were not solicited for this report due to the necessity of providing the City with this time-sensitive information. However, the results of this audit were discussed with City officials and their comments have been considered in preparing this report. GAGAS requires that we plan and perform our audit to adequately assess the estimates in the tentative budget. Further, those standards require that we understand the City's management controls and those laws, rules and regulations that are relevant to preparing estimates for the tentative budget.

To accomplish our objectives in this audit, we requested your tentative budget along with other pertinent information. We analyzed the composition of revenues and expenditures in order to determine if the revenue and expenditure estimates are reasonable and if the budget is structurally balanced so that recurring costs are financed with recurring revenues. It was not our intent and we do not offer comments on public policy decisions, such as, the type and level of services to be provided.

The tentative budget package for the fiscal year ended May 31, 2007, submitted for audit consisted of the following:

- Proposed budget submitted February 15, 2006, by the Mayor to the Common Council
- Supplementary Information

The tentative budget for the City's three major operating funds as submitted to our office is summarized below:

Fund	Appropriations and Provisions for Other Uses	Estimated Revenues	Appropriated Fund Balance	Real Property Taxes
General	\$14,572,881	\$8,729,812	-0-	\$5,843,069
Water	\$3,383,373	\$3,383,373	-0-	-0-
Sewer	\$2,730,996	\$2,730,996	-0-	-0-
Total	\$20,687,250	\$14,844,181	\$-0-	\$5,843,069

The observations and recommendations resulting from our audit are, to a great extent, influenced by the quality and quantity of materials submitted, and the time between submission and budget adoption.

We determined that the revenue and expenditure estimates in the proposed budget are not reasonable and the budget is not structurally balanced. Revenue estimates for water and sewer rents may not be realized and the contingency appropriation is not adequate. In addition, there is no provision in the budget to redeem interfund receivables and payables between the general and water and sewer funds, respectively.

Our audit disclosed the following findings which should be reviewed by the Common Council for appropriate action. Good management practices require that City officials take prompt action concerning our recommendations. We believe that prompt action by City officials will help improve the City's financial condition.

Financial Condition

The City's recent financial condition has been marked by recurring deficits and depleted fund balances. An operating deficit was reported in the general fund for the last three completed fiscal years¹. During this time City officials failed to significantly raise taxes or realize new revenue sources to fund increasing costs. Instead, they utilized available fund balance as a financing source in

¹ The operating deficits for the last three completed fiscal years were \$874,567 (2002-03), \$963,953 (2003-04), and \$1,661,720 (2004-05). These annual operating deficits were only partially planned, as the City appropriated fund balance in 2002-03 (\$500,000) 2003-04 (\$863,500), and 2004-05 (\$850,000). The unplanned operating deficits were caused by a variety of reasons. For example, in the 2004-05 fiscal year, health insurance costs exceeded the budgeted amounts by \$141,000 and the retirement appropriation was overexpended by \$507,000.

the annual budget, until it was depleted. As of May 31, 2005, the general fund reported a deficit fund balance of \$658,365. City officials expect the deficit in the general fund to increase to almost \$1.25 million at the end of the 2005-06 fiscal year. Furthermore, the City's water and sewer funds reported fund balance deficits of \$81,000 and \$555,000, respectively, at May 31, 2005. The deficits were caused by significant revenue shortfalls in these two funds. In the 2004-05 fiscal year, actual revenues from water rents were nearly \$734,000 less than the budgeted estimate, while actual sewer rent revenues were almost \$405,000 less than the budget estimate. City officials included water and sewer rate increases in the revenue estimates included in the 2004-05 adopted budget, but the increases were not adopted by the Common Council during the 2004-05 fiscal year. City officials also expect that the size of the deficits in the water and sewer funds could increase to \$419,000 and \$606,000, respectively, by the end of the 2005-06 fiscal year.

At May 31, 2005, interfund receivables totaling \$3,862,023 and a corresponding amount of interfund payables were reported in the City's financial statements. These receivables and payables represented cash advances from one fund to another, which were necessitated by cash flow deficiencies in the borrowing funds. The advances were not repaid because there were insufficient cash resources in the water and sewer funds. The water and sewer funds owe the general fund \$436,559 and \$820,237 respectively, as of May 31, 2005.

The Mayor submitted a tentative budget to the Common Council that included a 35 percent tax increase in the general fund, a level of taxation that is well within the City's constitutional tax limit. For the 2005-06 fiscal year, the City exhausted only 32 percent of its constitutional tax limit, and the proposed tax levy will increase that amount to approximately 51 percent. The Mayor's budget also proposed user fee rate increases in both the water and sewer funds. However, the proposed budget does not address repayment of the interfund loans.

Contingency Appropriation

The general fund budget includes an appropriation for contingencies in the amount of \$25,000. This amount represents less than 1 percent of total appropriations. The current amount budgeted provides the City with very little flexibility to deal with revenue shortfalls or insufficient appropriations. The allowance of an adequate contingency account within the budget would help cushion against unexpected events. This account is particularly important because the City does not have any available fund balance to finance any such occurrences. Even a modest 1 percent cushion would require a contingency item in the amount of \$146,000, or \$121,000 more than in the tentative budget.

City officials should review the contingency appropriation and raise it to a reasonable amount.

Water and Sewer Revenue Estimates

The City's tentative budget includes a revenue estimate of \$3,349,873 from water rents. This estimate is based on the assumption that the proposed water rate increase of \$10 per one thousand

The Honorable David Carucci and Members of the Common Council

April 5, 2006

Page 4 of 4

cubic feet of usage² will commence with the September 1, 2006 billing. We estimate that the proposed water rate increase will generate revenues of approximately \$3,231,000 in the 2006-07 fiscal year. Our estimate is \$118,873 less than the amount included in the tentative budget. The City's estimate does not appear to give appropriate consideration to historical usage patterns and the timing of the rate increase.

The City's tentative budget also includes a revenue estimate of \$2,500,496 from sewer rents. This estimate is based on the assumption that the proposed sewer rate increases³ will commence as planned. We estimate that the proposed rate increases will generate revenues totaling \$2,383,000, which is \$117,496 less than the City's estimate. Again, the City's estimate does not appear to give appropriate consideration to historical usage patterns and the timing of the rate increase. This overestimation of water and sewer rent revenues makes the tentative budget structurally imbalanced.

City officials should review and consider amending the budget estimates for water and sewer rents. They should also monitor the revenue throughout the year and adjust the budget accordingly if estimates are not met.

The Common Council has the responsibility to initiate corrective action. Pursuant to Section 35 of the General Municipal Law, the Common Council should prepare a plan of action that addresses the recommendations in this report and forward the plan to our office within ninety days. We encourage the Common Council to make this plan available for public review in the City Clerk's office. For guidance in preparing your plan of action and filing this report, please refer to the attached documents. We also request that you provide us with a copy of the adopted budget.

We hope that this information is useful as you adopt a budget for your city. If you have any questions on the scope of our work, please feel free to contact our Buffalo Regional Office at 716-847-3647

Very truly yours,

Robert E. Meller
Chief Examiner of Local Government Services and
Economic Development

cc: Steve Pachla, City Auditor
Mary Ellen Barrett, Deputy City Clerk
Kelly Sweet, Clerk to the Council

² The Proposed Water Rent increase is from \$46.54 to \$56.54 per one thousand cubic feet of water used

³ Proposed Sewer Rent increases: \$26.27 to \$29.27 for the June 1, 2006 billing and from \$29.27 to \$39.27 per one thousand cubic feet of water used for the September 1, 2006 billing.