



Town of Ashford

Water District

Report of Examination

Period Covered:

March 14, 2012 – October 6, 2015

2015M-343



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

March 2016

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 Ashford, entitled Water District. 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 New York State 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 Ashford (Town) is located in Cattaraugus County (County) and has approximately 2,100 residents. The Town is governed by an elected Town Board (Board), which is composed of four council members and the Town Supervisor. The Board is responsible for the general management and control of the Town's financial affairs. The Town provides services to its residents, including street maintenance, snow removal, street lighting and general government support. General fund appropriations for 2016 totaled approximately \$515,000 and were funded primarily by sales tax and Justice Court revenues.

For over 100 years, a portion of the Town has received water services through a privately-owned company (Company). However, residents and the County Health Department were concerned with water quality and the Company's lack of efforts to improve the aging system. In November 2006, the Board began considering the possibility of purchasing the Company and forming a water district. The Board subsequently determined that doing so was not in the Town's best financial interests. Additionally, the County and the New York State Public Service Commission (PSC) were working with the Company's owner to resolve the issues with the aging water system. In 2009, the Company was sold to another individual. However, the issues were not resolved and residents again brought the matter to the attention of the Board. Ultimately, in March 2015, the Board established a water district (District).

In August 2015, the Town signed a one-year agreement with the Company to lease and operate the water system for \$1. Under a separate agreement, the Town agreed to purchase the current owner's intellectual property including engineering reports, customer list, billing information, financial records and accounting system for \$50,000. During the lease period, the Town will be leasing the water system in order to provide water to residents while it is constructing a new water system infrastructure. Once construction is complete, the existing system will no longer be needed by the Town and will be returned to the Company and the Town will continue providing water to residents using its own newly constructed water supply and distribution system. Town officials anticipate constructing a new water supply and distribution system in 2016 and that the construction project will cost approximately \$3.2 million and take one year to complete.

Objective

The objective of our audit was to evaluate the Board's oversight of the District. Our audit addressed the following related question:

- Did the Board properly plan and manage the establishment and development of the District?

**Scope and
Methodology**

We examined Town records and reports for the period March 14, 2012 through October 6, 2015. We extended our scope period back to November 16, 2006 to determine if there were any previous discussions or plans for the water system.

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.

**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 planned to initiate 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 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.

Water District

Special improvement districts play an important role in the delivery of water services to residents. New York State Town Law authorizes a town board to let contracts for the construction of water district improvements, determine the manner of levying assessments to cover costs, set water rents or other service charges and provide for the issuance of obligations to cover capital costs. The board is ultimately responsible for the oversight and management of water districts by ensuring they are properly planned, managed and monitored. Proper planning includes clearly defining the scope, funding, maximum cost projections, budget, timeline, policies and other criteria.

Although the Board and Town officials ensured that the District was properly established, they did not adequately plan for key aspects of construction and operations. The Board did not adopt written policies or procedures governing water use and billing until a few days before processing water bills for the first billing cycle.¹ The Board also did not ensure that adopted water rates would be sufficient to cover the cost of District operations. As a result, we project that the District is facing a potential revenue shortfall of approximately \$15,000 in the first year of District operations. Additionally, as of October 22, 2015, Town officials had yet to start the bidding process for the construction of the water lines even though construction was expected to be completed by June 30, 2016. The District will incur additional costs if construction is not completed on time, but the Board has no plans in place if costs of construction exceed current funding levels.

Establishment

Town residents can petition a board to request the establishment of a water district or, in the absence of a petition, the board can pass a formal motion to create a district. Once a district is created, the board is required to hold a public hearing after providing adequate public notice.

Town residents did not formally petition the Board to establish the District, but many residents repeatedly voiced concerns to the Board regarding water quality and safety. Additionally, the County and PSC expressed similar concerns to the Board. Therefore, the Board felt compelled to establish a District and assume responsibility for providing water to District residents.

The Board established a water committee (Committee)² composed of two Board members and two residents to identify and research

¹ Town officials did not consider the need for a written policy until we inquired about their water billing, collection and enforcement procedures.

² The Committee was originally formed in 2007 and was reinstated in July 2014.

options for addressing water quality and safety concerns. The Committee presented two construction options (one estimated to cost \$5.8 million and the other estimated to cost \$3.2 million) and an option to take no action. The Board subsequently decided that the most cost-effective option would be to temporarily lease the existing system and construct a new system estimated to cost \$3.2 million.

The Board ensured the District was properly created in accordance with legal requirements. The Board consulted with legal counsel regarding the required resolutions and reviewed studies from other municipalities who developed water districts. An engineer was retained by an organized group of residents to identify the necessary improvements and the total estimated cost. The engineering study estimated that the annual operating and maintenance costs would be \$80,000 and the total construction costs would be \$3.2 million. After reviewing the engineering study, the Board established the District in March 2015. The District's construction costs were to be financed with a 30-year, interest-free loan from the New York State Environmental Facilities Corporation (EFC).

Although the Board properly established the District, we question its complete reliance on certain matters found in the engineering study, which the Town received December 10, 2014 and adopted December 28, 2014. This allowed Town officials 18 days to review all of the findings, boundaries, costs and unit classifications submitted by the engineer. Further, the Board did not use this limited timeframe to ask educated questions. For example, Board members did not request support for the engineer's calculation of estimated annual operating and maintenance costs.

The engineer told us he calculated these costs using similar projects and his overall familiarity with water systems. We requested documentation from the engineer pertaining to these projects but were not provided with any documentation to support or otherwise substantiate the engineer's calculations. Accepting an engineering report without performing a thorough review could lead to additional costs and potentially create financial hardships for some District customers.

The engineer estimated that the annual cost per household would be approximately \$748 per unit per year (\$320 for operating costs and \$428 for debt payments³ associated with the capital improvements). The engineer calculated these estimates using 250 units. However,

³ The engineer calculated the annual per household unit operating costs by dividing the estimated annual operating costs of \$80,000 by 250 units. He calculated the annual per household unit debt cost by dividing the \$3.2 million in debt costs by 30 years (equaling \$106,880 in annual costs), which he then divided by 250 units.

50 of these units are vacant lots that would not be assessed the \$320 operating fee. We recalculated the annual cost per household with the 50 vacant units eliminated from the operating fees and found that the cost per household would increase to approximately \$828 per unit annually (\$400 operating⁴ and \$428 debt) for an increase of \$80 per household.

Project Planning

Proper planning requires a thorough understanding of the project's overall scope and cost. Initial estimated costs must be realistic so the Board can properly evaluate methods and costs of financing. Once all aspects of the project (needs, priorities, costs and financing) are identified, the Board should formally adopt a project plan.

In accordance with the agreement, the Town is leasing the Company's water system including its water lines, pump house and property at an annual cost of \$1. According to the agreement, the Town must finish construction by June 30, 2016, or pay a monthly rent payment of \$1,000 until the project is completed.⁵

The Board anticipates construction to take at least one year but could not provide us with documentation or rationale to support this time estimate. As of October 22, 2015, the Town had not yet put the project to public bid and officials told us they expect the bid process to take at least one month before the Board will be able to award a contract. Thus, actual construction is not likely to begin until spring 2016. However, the Board has not determined how it will finance the additional monthly rent payments or how the additional cost will affect District residents. As part of project planning, the Board should have developed a timetable in which it documented when bidding would be done, the amount of time required to review the bids and when the construction would start and be completed.

In May 2015, the Board approved a resolution authorizing a capital project for the construction of water lines with an estimated maximum cost not to exceed \$3.2 million. The resolution stated that the project would include the installation of new water lines, a new storage tank, water meters and fire hydrants. However, Town officials could not provide a detailed project plan detailing the project scope, timetable or documentation to support the estimated costs. The project's initial estimated cost was based solely on the engineering study and a one-page construction plan presented to the Board by the engineer in December 2014. The engineer estimated total construction costs for the project to be \$3.2 million, which included \$575,000 for all legal, financial advisory, administrative and engineering costs.

⁴ We divided the \$80,000 annual operating costs by 200 units.

⁵ The Town will be assessed the monthly fee unless an agreement is reached with the current owner before the lease expires on June 30, 2016.

The Board already committed to pay engineering costs totaling \$330,000, or about 57 percent of these costs. However, this amount is specifically limited to the engineering work stated in the proposal and any additional work required will result in additional fees. The proposal specifically listed additional items for which the District could be charged extra, but without a detailed project plan, the Board cannot be sure if the additional services will be necessary. In addition, the Town has already received bills totaling \$27,330 from its attorney and financial advisor. As of September 3, 2015, the Town has already spent or approved to spend 62 percent of the total amount budgeted for legal, financial and engineering costs. This is especially concerning because the Board expects to incur additional costs for legal and financial services throughout the project and could possibly incur additional engineering costs.

It is essential for Town officials to determine the funding process to ensure sufficient resources are available to pay project-related costs in a timely manner. The Town applied for EFC financing in August 2015,⁶ but officials were unaware of the funding process specifics and did not identify alternative financing options if project costs exceed the amount estimated by the engineer. For example, officials were unaware if the EFC loan is reimbursement-based⁷ or if the entire amount of funding will be received before the start of the project. Further, as of October 6, 2015, the EFC had not approved the Town's application. The Town's application will most likely be approved, but funding will not be available until spring 2016. Once the Town's application is approved, all invoices will be submitted to the EFC and the Town will be provided with a draw-down each month. Town officials borrowed \$100,000 from the general fund and issued a bond anticipation note for any costs incurred until the EFC financing is finalized.

Without a well-developed project plan in place, the Board puts the District at risk of incurring unanticipated costs and potential construction delays.

Water Rates and Billing

The Board is responsible for setting water rates and ensuring that water rents are properly billed, collected and enforced. Therefore, it is essential that the Board establish written policies and procedures governing water operations. Adequate policies and procedures, at a minimum, should include setting water rates and establishing procedures for water rent billing and for collecting and enforcing unpaid charges. Additionally, it is the Board's responsibility to review water rates to ensure anticipated revenue adequately covers the cost of water operations.

⁶ EFC provides 30-year, interest-free loans.

⁷ Funds are received after the Town has incurred expenditures.

The Town's responsibility for providing water services and billing customers was scheduled to begin on July 1, 2015. However, the Board did not adopt a written policy until September 22, 2015, just nine days before the first billing was to take place. Current plans include continuing to bill water customers at the same rates (flat fee) that were used by the Company. However, the Board did not determine if these rates were adequate to cover the estimated \$186,880⁸ in annual costs. Additionally, the Board did not ensure that rates were assessed fairly upon commercial customers. After the water project is completed, the Town will be switching to a metered system. This will require the Board to adjust rates to cover costs based on customer water use and may result in higher charges for certain users. Currently, the Board does not have a plan in place to determine when Town officials will analyze the current rate structure.

We reviewed the water bills that were sent out in October 2015 to determine if the Town was billing an adequate amount to cover anticipated annual costs. The Town billed water customers \$21,440 for the period August 18 through September 30, 2015.⁹ This amount included a flat fee for water use and a surcharge to pay for associated debt.

Based on the amounts billed, we project that a full quarterly billing cycle would generate approximately \$42,880 or annual revenues totaling approximately \$171,520. As a result, we project the District will incur an operating deficit of approximately \$15,360 in the first year of operation.¹⁰ The Town did not bill the debt service surcharge to 50 vacant lots located within the District. However, when establishing the District, the Board determined that all properties would benefit from the proposed improvements. Therefore, all properties including the vacant lots should be assessed the debt service charge. If these properties are billed for the debt service charge, we estimate that an additional \$17,044¹¹ in annual revenue would be generated and the projected operating deficit would be eliminated.

Water rates should take into account water use and be established based on particular types of property. For example, multifamily residential properties should generally not be charged the same flat rate as a property with a single-family home because the amount of

⁸ Estimated annual operating and maintenance costs of \$80,000 and debt of \$106,880

⁹ The Town did not take over water operations (from the Company) until August 18, 2015, with its first quarterly billing expected to go out October 1, 2015. Town officials expected to bill water customers for approximately one-half of the billing quarter from July 1 through September 30, 2015.

¹⁰ Our projected deficit is composed of \$1,025 for operating costs and \$14,335 for debt.

¹¹ Billing for each vacant unit would be \$85.22 per quarter.

water used at a multifamily property would most likely be greater. The Town's water rate schedule establishes unique rates for the varying types of residential properties, which appear to correlate with water use. However, the basis for establishing varying rates for commercial or nonresidential properties is unclear. For example, two churches were charged significantly different amounts, but Town officials could provide no rationale for using two different rates. One church was billed a flat rate of \$148.48 per quarter while the other was billed \$311.03 per quarter. We found a similar disparity in rates established for two bars.

Without proper Board oversight of the billing and collection process, errors could occur resulting in lost District revenues.

Recommendations

The Board and Town officials should:

1. Develop and monitor a detailed project plan to ensure that the water project is completed in a timely manner.
2. Assess the capital project costs to ensure estimated costs are reasonable and that adequate funding is available.
3. Review water rates to ensure that rates are assessed in a fair and equitable fashion and revenues will sufficiently cover expenditures.
4. Ensure vacant properties are billed for capital costs and customers are billed the appropriate amounts based on accurate unit classifications.

APPENDIX A
RESPONSE FROM LOCAL OFFICIALS

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



TOWN OF ASHFORD

9377 Route 240
P. O. Box #306
West Valley, NY 14171

CHARLES E. DAVIS, III, SUPERVISOR

Phone (716) 942-6016
Fax (716) 942-3957
www.ashfordwv@yahoo.com

COUNCILMAN

John A. Pfeffer
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Jean M. Bond

March 8, 2016

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Patricia R. Dashnaw

TOWN JUSTICE

Richard L. Neumann, Jr.
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Office of the State Comptroller
Division of Local Government and School Accountability
295 Main Street
Buffalo, NY 14203

HIGHWAY

SUPERINTENDENT

Tim A. Engels

Re: Response to the Draft Audit Report

ASSESSOR

Dawn Martin

The Town of Ashford agrees with the Preliminary Draft Audit Report findings as reported by the Office of the State Comptroller.

Sincerely,

Charles E. Davis III
Supervisor for the Town of Ashford

APPENDIX B

AUDIT METHODOLOGY AND STANDARDS

To accomplish our audit objective and obtain valid evidence, we performed the following procedures:

- We interviewed the Supervisor and Board members to gain an understanding of the procedures taken to establish, obtain funding for and plan to operate the District. We also reviewed information regarding estimated completion dates for the construction bidding process.
- We interviewed the engineer to obtain information regarding District estimated operating and maintenance costs. We reviewed these cost estimates to determine if they appeared reasonable compared to the Company's annual operating costs.
- We reviewed the adopted written policy for water operations to obtain an understanding of the rate structure and billing procedures.
- We reviewed Board minutes from November 2006 through August 2015 for relevant or significant discussions or resolutions related to the District.
- We reviewed the lease and purchase agreements to determine associated District costs.
- We obtained the current customer listing and compared it to the 2015 assessment role to determine if the number and classifications of the listed units were accurate.
- We reviewed the accepted engineering services proposal and legal and financial services claim vouchers approved for payment.
- We projected the District's annual revenues and annual operating results.

We conducted this performance audit in accordance with 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 objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

APPENDIX C

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