

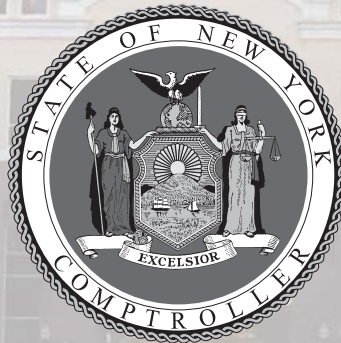
OFFICE OF THE NEW YORK STATE COMPTROLLER



DIVISION OF LOCAL GOVERNMENT
& SCHOOL ACCOUNTABILITY

Capital Planning

2009-MS-5



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

December 2009

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 local 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 entitled Capital Planning. 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*



State of New York Office of the State Comptroller

EXECUTIVE SUMMARY

Capital assets are generally defined as those used in operations that have expected useful lives of more than a year. These assets include, but are not limited to, buildings and other facilities, water and sewer infrastructure, streets and highways, equipment, vehicles, and machinery. Capital assets, by their very nature, represent a significant commitment of municipal resources. Their considerable costs and long lives make capital assets a major component of every municipality's operations. To ensure that essential operations continue uninterrupted, local officials must effectively plan for the acquisition and replacement of vital capital assets and infrastructure.

Scope and Objective

The objective of our audit was to determine if municipalities are formally planning for their capital needs for the period January 1, 2007 through August 31, 2008. Our audit addressed the following related questions:

- Do municipalities have entity-wide, long-term capital plans adopted by their governing boards?
- Have the governing boards adequately funded municipal capital needs?

Audit Results

Of the 10 local governments audited, we found that three of four cities had entity-wide, long-term capital plans approved by their governing boards, while none of the towns and counties did. Three local governments (the other city, a town and a county) had good procedures that included governing board involvement, but only adopted plans annually as part of the budget process. The remaining four local governments allowed decisions to be made on a departmental level. The City of New Rochelle is the only local government that has also established goals and objectives, developed a policy detailing the fundamentals of a multi-year capital plan, and established the criteria used for ranking of purchases to provide a framework for its long-term capital plan.

We also found that all of the local governments audited funded their known municipal capital needs. However, the three local governments with entity-wide, long term capital plans and the three local governments with Board adopted one-year capital plans spent an average of 24 percent of 2008 operating expenditures on maintaining and improving infrastructure while those units

using a departmental level approach only spent about 5 percent. This significant difference in funding capital expenditures suggests that the governing boards relying on department heads for capital planning may not have identified all of their significant capital needs.

Comments of Local Officials

The results of our audit and recommendations have been discussed with local officials and their comments, which appear in Appendix A, have been considered in preparing this report. Local officials generally agreed with our findings and recommendations.

Introduction

Background

Capital assets are generally defined as those used in operations that have expected useful lives of more than a year. These assets include, but are not limited to, buildings and other facilities, water and sewer infrastructure, streets and highways, equipment, vehicles, and machinery. Capital assets, by their very nature, represent a significant commitment of municipal resources. Their considerable costs and long lives make capital assets a major component of every municipality's operations. To ensure that essential operations continue uninterrupted, local officials must effectively plan for the acquisition and replacement of vital capital assets and infrastructure.

Municipalities are responsible for acquiring and maintaining capital assets and infrastructure within their jurisdictions. Acquiring capital assets or financing capital improvements often requires significant outlays of cash. Capital assets such as machinery and equipment eventually break down and need replacement, and roads, buildings, and infrastructure need periodic repairs and renovations. If a municipality does not give adequate attention to asset replacement and improvement, it must sometimes operate in a crisis or emergency environment.

We picked 10 local governments throughout New York State. Units picked varied in size, structure and average annual capital and equipment expenditures. The audit included: the Counties of Wayne, Genesee, and Essex; the Towns of Bethlehem, Oyster Bay, and Camillus; and the Cities of Watertown, Poughkeepsie, New Rochelle, and Ithaca. Some of these local governments maintained water and sewer infrastructure while others did not.

Local Government	2008 Operating Budget	Average Annual Capital & Equipment Expenditures ¹	Percent of Average Capital Expenditures to 2008 Operating Budget
Town of Oyster Bay	\$233,200,000	\$94,700,000	40.6%
City of Ithaca	\$54,400,000	\$18,000,000	33.1%
City of New Rochelle	\$107,000,000	\$12,500,000	11.7%
City of Watertown	\$46,800,000	\$10,400,000	22.2%
City of Poughkeepsie	\$70,700,000	\$10,000,000	14.1%
Wayne County	\$166,000,000	\$8,800,000	5.3%
Genesee County	\$134,200,000	\$8,400,000	6.3%
Essex County	\$94,300,000	\$4,500,000	4.8%
Town of Bethlehem	\$38,000,000	\$3,700,000	9.7%
Town of Camillus	\$35,200,000	\$1,300,000	3.7%

Objective

The objective of our audit was to determine if municipalities are formally planning their capital needs. Our audit addressed the following related questions:

- Do municipalities have entity-wide, long-term capital plans adopted by their governing boards?
- Have the governing boards adequately funded municipal capital needs?

Scope and Methodology

We interviewed staff, examined policies and procedures, examined all budgets, budget-related support, capital and equipment purchases, and related funding for the period January 1, 2007 through August 31, 2008.

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 is included in Appendix B of this report.

Comments of Local Officials

The results of our audit and recommendations have been discussed with local officials and their comments, which appear in Appendix A, have been considered in preparing this report. Local officials generally agreed with our findings and recommendations.

¹ As reported to OSC for 2007 and 2008 fiscal years

Creating a Multi-Year Capital Plan

In order to create an entity-wide, multi-year plan, the local government should first establish capital program goals, objectives and criteria that are incorporated into a formal policy adopted by the governing board. Such a policy will provide a framework for the local government's long-term capital plan. A comprehensive policy should clearly identify the selection criteria for capital acquisitions and list, define, and rank the criteria in order of importance so that department heads and others can effectively gauge capital acquisition requests.

The local government should also assess its capital assets by maintaining a detailed list of its infrastructure, buildings, streets and highways and equipment. The list should include, but not be limited to, the description, condition, remaining useful life, and replacement cost. With such an inventory, officials can develop a plan based on expected needs. Managers should use the detailed list of all infrastructure and equipment together with established goals and objectives to identify capital projects and develop a formal long-term capital plan. Estimated costs for the projects should be verified through discussions with department heads, purchasing officers, engineers, potential vendors, State agencies, and local governments.

After local officials address all aspects of the plan, the governing board should approve the capital plan and formally adopt the annual budget, including the planned capital components. This will ensure that funding is coordinated with other required expenditures. An officially adopted capital plan will ensure that the governing board is aware of capital needs, and play an integral role in key decisions. In addition, it will also help ensure continuity during administration changes. The governing board and local officials should periodically review the capital plan and make appropriate adjustments to ensure that projects remain on schedule and within budget.

We found that only three of 10 local governments tested have entity-wide, long-term capital plans approved by their governing boards; three others had good procedures that involved their governing boards, but they only adopted plans annually as part of the budget process. The remaining four had no planning process; instead they allow the department heads to decide which capital expenditures would be made. A list of local governments and the status of their respective plans follows:

Local Government	Adopted an Entity-Wide, Long-Term Capital Plan	Current Practice
Wayne County	No	Departmental level
Genesee County	No	Only approves 1 year
Essex County	No	Departmental level
Town of Bethlehem	No	Departmental level
Town of Oyster Bay	No	Only approves 1 year
Town of Camillus	No	Departmental level
City of Watertown	Yes	
City of Poughkeepsie	Yes	
City of Ithaca	No	Only approves 1 year
City of New Rochelle	Yes	

Further, the City of New Rochelle is the only local government that has established goals and objectives, developed a policy detailing the fundamentals of a multi-year capital plan, and established the criteria used for ranking of purchases to provide a framework for its long-term capital plan. Wayne County’s Board of Supervisors approved a resolution in August, 2008 establishing a five-year capital planning process which includes deadlines and policies. The other units rely on past practices and informal procedures.

Lastly, we found that six (Cities of New Rochelle and Watertown, Town of Camillus and Wayne, Genesee, and Essex Counties) out of 10 local governments had assessed their capital assets and equipment and maintained detailed lists of all infrastructure and equipment on an entity-wide basis. Although departments generally have inventories of assets and are aware of what assets need replacement, without a comprehensive, centralized record of all capital assets the governing boards cannot properly plan for the maintenance, replacement, and timely funding of capital assets on an entity-wide basis.

Overall, without comprehensive, entity-wide long-term capital planning, local governments risk prioritizing projects inappropriately, as well as not funding them adequately. The following are examples of situations that might have been avoided, or at least made less serious, if the local government had used entity-wide long-term capital planning:

- The Oyster Bay Town Board authorized the issuance of \$4,000,000 in bonds for various improvements to the Old Bethpage Solid Waste Disposal Complex, including \$3,000,000 for the demolition of the incinerator building

in 1995. At that time, a developer was interested in the incinerator building location for a sports facility. The deal with the developer fell through and the incinerator, which is not being used, has remained idle. A long-term capital plan might have provided some time frame for the demolition of the incinerator building and the development or adaptation of the location for private or town use.

- In Essex County, a repair of a leaking roof over the highway garage in conjunction with an addition to the building cost more because of delays in the project. The Public Works Superintendent and his Deputy Superintendent stated that the roof was leaking and in dire need of repair. Approximately \$138,000 was carried forward from the prior year to do the repair. However, when the roof was finally torn off and replaced, there was additional damage to the building/roof discovered, as the water that had been leaking caused the wood to rot. Department officials indicated that because the roof project was put off for so long, \$26,000 in additional damage occurred that could have been avoided. An entity-wide long-term capital plan might have helped the Board of Supervisors better organize, prioritize and fund this project, avoiding unnecessary costs.

Recommendations

1. Governing boards should establish a capital assets policy that reflects their long-term capital goals and objectives, and establishes parameters for the development and implementation of formal capital plans.
2. Local governments should combine existing departmental equipment records with updated infrastructure records to develop a comprehensive set of records on the condition of capital assets, which can be used to plan for the funding of asset replacements.
3. Governing boards should create and adopt an entity-wide, multi-year capital plan that is flexible, is affordable, and considers replacement costs as well as historical costs.

Funding of Capital Assets and Equipment Purchases

Capital acquisitions can consume large amounts of financial resources. Planning for these costly purchases can allow managers time to increase pay-as-you-go financing thereby decreasing the amount to be borrowed and reducing the associated costs. It also gives managers time to obtain the best purchase price and seek alternative financing sources (e.g., State and Federal aid). Long-term capital plans can also allow managers to spread the acquisition costs over a number of years so that no one budget year is overburdened with several capital purchases. Similarly, the planned replacement of aging assets can prevent costly emergency purchases from disrupting operations, budgets, and tax rates.

Once accurate cost estimates have been developed for each project, funding availability becomes a factor for prioritizing the projects. Funding for capital projects can come from any combination of State or Federal sources, local funds, or the proceeds of debt. State and Federal funding sources include grants, low-interest loans, or the direct provision of equipment, labor, or services. Local funding sources include available fund balances, relevant reserve funds, annual budget appropriations, proceeds from the sale of existing assets, payments under inter-municipal cooperative agreements with other local governments, and private sources such as gifts and donations. When reserve funds are established, local officials should responsibly establish a plan for their use, anticipated balance requirements, and funding. Projects funded through borrowing have certain associated legal costs and require budgeting for principal and interest payments annually to retire the debt.

We found that all of the local governments audited funded various levels of municipal capital needs. The six local governments with Board involvement provided funding necessary to implement the planned capital purchases. Those without long-term formal plans either included a one-year list as a part of the annual budget and appropriated amounts for specific items, or funded departments and allowed the department heads to purchase items as they deemed necessary. The last option of funding the departments has some risks. Without entity-wide planning, the departments may not be allocating enough money to meet their needs. Capital spending as a percentage of the total operating budget for the units audited was as follows:

Analysis of Capital Needs Spending			
Local Governments with a Capital Planning Process that Involves the Board:			
Local Government	Method of Capital Planning	2008 Operating Budget	Average Annual Capital & Equipment Expenditures
Town of Oyster Bay	One year Board plan	\$233,200,000	\$94,700,000
City of Ithaca	One year Board plan	\$54,400,000	\$18,000,000
City of New Rochelle	Multi-Year Board Plan	\$107,000,000	\$12,500,000
City of Watertown	Multi-Year Board Plan	\$46,800,000	\$10,400,000
City of Poughkeepsie	Multi-Year Board Plan	\$70,700,000	\$10,000,000
Genesee County	One year Board plan	\$134,200,000	\$8,400,000
	Total:	\$646,300,000	\$154,000,000
Percentage of Capital Spending to Operating Budget:			23.83%
Local Governments with a Department Level Capital Planning Process:			
Wayne County	Department Level	\$166,000,000	\$8,800,000
Essex County	Department Level	\$94,300,000	\$4,500,000
Town of Bethlehem	Department Level	\$38,000,000	\$3,700,000
Town of Camillus	Department Level	\$35,200,000	\$1,300,000
	Total:	\$333,500,000	\$18,300,000
Percentage of Capital Spending to Operating Budget:			5.49%

The table shows that those units with a departmental level capital planning process spent an average of 5 percent of the 2008 operating budget on capital needs. This is far less than the 24 percent spent by those units using a capital planning process that includes Board involvement. This leads us to conclude that where a departmental capital planning process is used and Board involvement is limited, capital expenditures receive less priority. For example:

- In the Town of Bethlehem, department heads have some discretion as to what capital purchases they will make within the appropriations allotted to them, but capital needs are not prioritized on a Town-wide basis. As a result, in June 2007, the Town declared an emergency to fund the replacement of an elevated sewer trunk line at a cost of \$710,000. Documentation for this project indicates the pipe's condition had been monitored at the departmental level as far back as the 1990s. The condition deteriorated to a point that a failure of the line was to

be reasonably expected. Further, some Board members were made aware of the situation only after it became an emergency and was presented at a Board meeting by the Town's Director of Public Works. We believe that the emergency declaration could have been avoided if Town officials had been better-informed and properly planned for the upgrade of the sewer trunk line.

- In the Town of Camillus, department heads are often asked to stick to the prior year's budget amounts. This may present some difficulties for department heads with the prioritization and execution of capital plans, as it is not likely that capital expenditures will remain constant from year to year.

By creating a multi-year plan and also ensuring that funding is available, local officials decrease the risks of incurring additional unexpected costs, and improve flexibility. In Watertown, when unforeseen situations arise or equipment deteriorates more rapidly than expected, the City can easily adapt without incurring unnecessary costs or forgoing other necessary items. For example, during the year a front-end loader, which was scheduled for replacement in the following year, required \$17,000 in repairs, the current year capital plan included the purchase of a \$90,000 dump truck, which was then substituted for the front-end loader. While this could occur with or without a multi-year plan, having the long-range plan provided the City with a source to quickly reference and a starting place for adjustments.

Governing boards play an essential part in ensuring the fiscal well-being of local governments. Without direct involvement of the governing boards in the decisions to prioritize and finance major capital improvements, there is a risk that departments will not address needs until emergency conditions exist.

Recommendation

4. Governing boards should incorporate entity-wide capital planning into the budget process to ensure that adequate funding is available and that budgetary appropriations align with capital needs.

APPENDIX A

RESPONSES FROM LOCAL OFFICIALS

We provided a draft copy of this report to each of the 10 municipalities we audited and requested responses. The following comments were excerpted from the five official responses received. Responses were provided by the City of New Rochelle, Wayne County, the City of Watertown, the Town of Oyster Bay and the Town of Bethlehem.

Overall Comments

City of New Rochelle — “We have reviewed the document and concur with both your conclusions and recommendations. We stand ready to offer our process as a model for other communities throughout New York State.”

Wayne County — “As a commentary on the analysis that was done regarding Capital Needs Spending, it is likely that governments that have no water or sewer infrastructure to maintain will spend significantly less on capital projects. In addition, when comparing percentages of amount spent on capital programs as opposed to jurisdictions overall operating budget it would appear that county governments which have significant state mandated reimbursement programs and pass through payments will generally have a lower percent spent on capital projects.”

City of Watertown — “The city realizes the importance of capital planning from both an operational point-of-view and a financial point-of-view. Operationally, the city looks at the issues likely to affect the community over the five year planning period and beyond, and our ability to meet the changing demand. During the development we review and project major equipment replacements and/or additions, facility improvements or rehabilitations, and infrastructure improvements.”

Town of Oyster Bay — “The Town does not have any major differences of opinion concerning the findings as detailed in your draft report.”

“... the town of Oyster Bay highly regards any recommendations made by the New York State Comptroller’s Office and will incorporate same in the Town’s corrective action plan.”

Town of Bethlehem — “We agree that municipalities need to formally plan their capital needs. In July 2008, The Town Supervisor organized a capital planning committee to identify capital needs and establish priorities for completion. The committee continues to meet on a monthly basis and plans to present a Preliminary Capital Plan at the December 9, 2009 Bethlehem Town Board meeting for Board acceptance.”

APPENDIX B

AUDIT METHODOLOGY AND STANDARDS

We interviewed staff, examined policies and procedures, examined all budgets, budget-related support, capital and equipment purchases, and related funding for the period January 1, 2007 through August 31, 2008 in 10 municipalities throughout New York State. These municipalities were chosen based on structure, total recent capital expenditures, and from results of a brief survey with municipalities.

In each unit, we reviewed policies and procedures over capital asset planning, purchasing and funding. We also conducted interviews with staff involved in each key area to help gain an understanding of the adequacy of the internal controls in place.

Review of minutes — We reviewed all meeting minutes during our scope and documented any scope related transfers and/or all situations in which purchases were classified as “emergency” or unusual. We then determined the purpose of all non-routine budget transfers or funding to ensure that all purchases were anticipated.

Expenditure test — To determine if the municipality adequately addressed all reasonable capital needs, we traced total Capital/Equipment Expenditures for a period (calendar year) to the Budgeted amount. All material variances were then looked into further to determine why the budgeted plan was not followed. In some municipalities this could not be done because they did not maintain detailed budget support.

Selected outlay test — To determine if municipalities are adequately planning their capital asset needs, we reviewed a minimum of 100 transactions, 50 from 2007 and 50 from 2008. We traced the individual capital asset purchase to the capital plan to ensure that the purchase was planned. If the municipality did not have a plan, we then compared the purchase to a budget detail. Again, in some municipalities this could not be done because they did not maintain detailed budget support.

We conducted our 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 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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