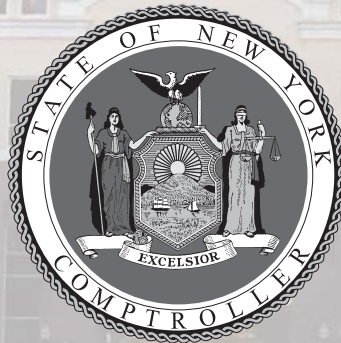




Peconic Bay Community Preservation Fund

2009-MR-6



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

June 2009

Dear Local 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 Peconic Bay Community Preservation Fund in the Suffolk County Towns of East Hampton, Riverhead, Shelter Island, Southampton, and Southold. 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

The State Legislature enacted Chapter 114 of the Laws of 1998 which authorized the creation of the Peconic Bay Community Preservation Fund (CPF). This legislation, contained within Town Law Section 64-e, authorized each of the Suffolk County Towns of East Hampton, Riverhead, Shelter Island, Southampton, and Southold to establish such a fund by local law.

The CPF's overall goal is to preserve open land and farmland in the five Towns, a goal which includes purchasing open space and environmentally-sensitive lands. The CPF is financed by a 2 percent real estate transfer tax.¹ In 2006, voters in all five Townships approved a referendum to extend the collection of this tax from 2020 to 2030. Proceeds of this transfer tax are disbursed to the Town in which the transaction takes place for the Town's acquisition of land, development rights, and other interests in property for conservation purposes. Towns are allowed to use CPF funds (not more than 10 percent) for management and stewardship of acquired property, and to make payments in lieu of taxes (PILOTs) to eligible fire, fire protection, and ambulance districts within the Central Pine Barrens area.²

Since the creation of the Peconic Bay CPF in 1998, the fund has generated approximately \$516 million for land preservation in the Peconic Bay Region, and Towns have acquired approximately 7,400 acres of open space, farmland, parks, and historic sites for preservation purposes.

Scope and Objective

At the request of Assemblymen Thiele and Alessi and Senator LaValle, we audited the Peconic Bay CPFs established locally in each of the five Towns in the Peconic Bay Region. The objective of our audit was to determine whether each Town was administering its CPF in accordance with Town Law. Our audit addressed the following related questions for the period April 1, 1999 to March 31, 2008:

- Have the individual CPFs been used for the intended purpose of acquiring interests in land to protect community character?

¹ Administration of the 2 percent real estate transfer tax is governed by the Tax Law.

² The Long Island Central Pine Barrens, which cover more than 100,000 acres, comprise public and private land holdings that are managed by a mix of Federal, State, county and local public land managers.

- Have all PILOTs been properly made to eligible school and special districts?
- Has all revenue from transactions subject to the real estate transfer tax been properly collected and recorded?
- Have the Towns established land acquisition processes that ensure the efficient expenditure of funds?
- Have the Towns obtained voter approval for any amendments to the local laws concerning the CPF?

Audit Results

We reviewed documents relating to the CPFs in all five Towns and found that controls in the Towns of Riverhead and Southold are, in general, adequately designed and effectively operating to ensure their CPFs are administered in compliance with Town Law. However, we found the following deficiencies in controls over the administration of CPFs in the Towns of East Hampton, Shelter Island and Southampton.

In general, the Towns of Riverhead, Shelter Island, Southampton, and Southold paid legitimate expenditures against the CPF. However, we found that East Hampton improperly advanced at least \$8 million from its CPF to other Town funds during 2007 to provide cash required to maintain Town services. Further, East Hampton officials transferred an additional \$1.5 million from the CPF to the general fund as reimbursement for expenses allegedly incurred on behalf of the CPF. However, the Town had no evidence showing these expenses were related to the CPF.

In 2004 and 2005, Southampton, which is the only Town that provided PILOTs, erroneously paid PILOTs totaling \$107,650 to a fire district that did not meet the eligibility requirements in those years. Furthermore, we found that a school district was paid \$2 million more in PILOTs than it was entitled to in 2007 because the Town calculated the PILOTs incorrectly.

As of June 2008 none of the revenue earned by the East Hampton CPF in the first three months of 2008 – approximately \$4.8 million, including transfer tax and interest – had been posted to the general ledger. The Supervisor told us he knew these transactions were not posted, but that transferring prior years’ data to a new software system was a higher priority. We also found that Shelter Island had not adequately segregated duties for individuals involved in the cash receipts process.

We reviewed the documentation for five acquisitions made in each of the Towns between April 1999 and March 2008 and found that, in general, each of the Towns has a process in place to ensure the prudent and efficient expenditure of funds. We also found that all the Towns had records of referenda held for each amendment made to their respective local laws.

Comments of Local Officials

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. Local officials generally agreed with our findings and recommendations. Appendix B contains our comments on issues raised in one Town’s response.

Introduction

Background

The State Legislature enacted Chapter 114 of the Laws of 1998 which authorized the creation of the Peconic Bay Community Preservation Fund (CPF). This legislation, contained within Town Law Section 64-e (Town Law), authorized each of the Suffolk County Towns of East Hampton, Riverhead, Shelter Island, Southampton, and Southold to establish such a fund by local law. Town Law has subsequently been amended by Chapter 250 of the Laws of 2002 to provide additional guidance on the administration of the CPF within the above Towns.

The CPF's overall goal is to preserve open land and farmland in the five Towns, a goal which includes purchasing open space and environmentally-sensitive lands. The CPF is financed by a 2 percent real estate transfer tax.³ Proceeds of this transfer tax are disbursed to the Town in which the transaction takes place for the Town's acquisition of land, development rights, and other interests in property for conservation purposes. In 2006, voters in all five Townships approved a referendum to extend the collection of this tax from 2020 to 2030. Town Law expressly prohibits any monies deposited in the CPF from being transferred to any other account.

Town Law specifies that the original purposes of the CPF were to implement a plan for the preservation of community character, to acquire interests or rights in real property for the preservation of community character within the Town, and to provide for the transfer of development rights. Another purpose of the CPF was to make payments to fire, fire protection, and ambulance districts in connection with lands owned by the State or any municipal corporation within the Long Island Central Pine Barrens.⁴ Only the Towns of Riverhead and Southampton contain any such eligible districts. The final purpose of the CPF was to provide for using not more than 10 percent of the fund to establish a management and stewardship program for maintaining and restoring preserved real property.

³ Administration of the 2 percent real estate transfer tax is governed by Tax Law.

⁴ The Long Island Central Pine Barrens, which cover more than 100,000 acres, comprise public and private land holdings that are managed by a mix of Federal, State, county and local public land managers.

Since the creation of the CPF in 1998, the fund has generated approximately \$516 million for land preservation in the Peconic Bay Region and has preserved approximately 7,400 acres of open space, farmland, parks, and historic sites.

Objective

At the request of Assemblymen Thiele and Alessi and Senator LaValle, we audited the CPFs in each of the five Towns in the Peconic Bay Region. The objective of our audit was to determine whether each Town was administering the CPF in accordance with Town Law. Our audit addressed the following related questions for the period April 1, 1999 to March 31, 2008:

- Have the individual CPFs been used for the intended purpose of acquiring interests in land to protect community character?
- Have all payments in lieu of real property taxes (PILOTs) been properly made to eligible school and special districts?
- Has all revenue from transactions subject to the real estate transfer tax been properly collected and recorded?
- Have the Towns established land acquisition processes that ensure the efficient expenditure of funds?
- Have the Towns obtained voter approval for any amendments to the local laws concerning the CPF?

Scope and Methodology

We audited internal controls over the administration of the Peconic Bay Community Preservation Fund established in the Towns of East Hampton, Riverhead, Shelter Island, Southampton, and Southold. During this audit, we examined accounting records relating to the administration of the individual CPFs for the period April 1, 1999 to March 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 are included in Appendix C of this report.

Comments of Local Officials

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. Local officials generally agreed with our findings and recommendations. Appendix B contains our comments on issues raised in one Town's response.

Use of Funds

Town Law authorizes the Towns in the Peconic Bay region to use their CPF monies to pay the costs of acquiring land for the purpose of preserving community character, along with preliminary and incidental costs related to the acquisition. Town Law requires each Town Board to adopt a community preservation project plan that includes a list of every project the Town will undertake in connection with its CPF. Town Law also provides for creating a management and stewardship program for lands acquired by the CPF. Funds for management and stewardship cannot be more than 10 percent of the CPF.

The Towns can also use CPF monies to pay the salaries of employees, or independent contractors, hired to manage the CPF, but only if the individuals' job responsibilities are directly dedicated to implementing the provisions of the CPF. Monies from the CPF may also be used to repay any indebtedness or obligations incurred for the CPF. According to Town Law, the Towns should use their CPFs to pay only those expenses specifically permitted by law. Monies deposited into the CPF should not be transferred to any other Town fund for any reason.

We reviewed the costs incurred by each of the five Towns in connection with their CPFs to determine whether the funds have been used for proper purposes. We examined general ledger transactions, disbursement listings, cancelled checks, and bank statements related to expenditures charged against the CPFs from April 1, 1999 through March 31, 2008. In general, the Towns of Riverhead, Shelter Island, Southampton, and Southold paid legitimate expenditures against the CPF. Of these four Towns, only Southampton has established a CPF office and paid salary expenses directly from its CPF. Other expenses that we found in the CPFs included mostly fees for appraisals, surveys, title searches and debt service.

However, we found that East Hampton's CPF monies were used for inappropriate purposes because the Town did not have adequate controls over advances and disbursements. The Town also lacked controls over wire transfers.

Inappropriate Uses of CPF Monies

We identified that East Hampton has used millions of dollars of CPF monies for inappropriate purposes. For example, CPF monies were advanced to other Town funds to maintain

operations, used to buy land for non-preservation purposes, and used to reimburse the general fund for costs reportedly incurred on behalf of the CPF. As a result, CPF funds were used for unallowable or improper purposes.

CPF Monies Loaned to Other Town Funds — General Municipal Law (GML) generally authorizes a municipal corporation to temporarily advance monies held in a fund to any other municipal fund. This statute also requires that interfund advances be authorized in the same manner as budgetary transfers between appropriations and that repayment be made no later than the close of the fiscal year in which the advance was made. When an advance is made between funds supported by different tax bases, repayment must include an amount reasonably equivalent to the amount that would have been earned on the investment of the monies advanced. Monies held by the Supervisor in a trust or fiduciary capacity, or those which, by law, may be used only for stated purposes, may not be advanced to other funds.

This limitation on the authority to make interfund advances applies to, among other things, monies in a capital reserve fund, since they are kept in a separate account and may be used only for the purposes set forth in GML. Town Law requires that CPF monies be kept in a separate fund, states the purposes for which the monies are to be exclusively used, and provides that CPF monies may be used only for projects contained in the community preservation project plan. As such, CPF monies are monies that, by law, may be used only for stated purposes and may not be advanced to other funds. Furthermore, Town Law expressly prohibits any monies deposited into the CPF from being transferred to any other funds.

Town Law prohibits the loan of CPF monies to other funds. However, documentation prepared by the Town's public accountant⁵ shows that, during 2007, East Hampton officials made interfund advances totaling at least \$8 million from the CPF to provide cash required to maintain Town services. The Town's budget officer authorized these interfund advances without the approval of the Board. At December 31, 2007, the end of the Town's fiscal year, the Town had not repaid these interfund advances to the CPF, as required by GML. On January 25, 2008, Town of East Hampton officials transferred a total of \$7.6 million from other Town funds to the CPF. Town officials, the Town's former public accountant, and the Town's current public

⁵ This documentation consisted of the current public accountant's interpretation of work done by the former public accountant

accountant all provided conflicting explanations about why the Town did not repay the total amount due to the CPF.

Further, although the Town repaid \$7.6 million from other Town funds to the CPF, it did not repay any of the advances with interest. The interest charged should have been the estimated amount that would have been earned on the investment of the money if it had not been advanced. At its December 2008 meeting, the East Hampton Town Board determined that the amount of unpaid interest still due to the CPF was approximately \$138,000. The practice of temporarily transferring CPF monies to other funds results in the use of the money for purposes other than those intended by Town Law.

Purchase of Land for Housing — The purposes of the CPF are to implement a plan for the preservation of community character, to acquire interests or rights in real property for the preservation of open space and farmland within the Towns, to provide for the transfer of development rights, and to implement a management and stewardship program to help maintain and preserve acquired property. There is no authorization in Town Law for expenditures from the CPF for purposes that do not relate to community preservation.

On April 27, 2007, the Town transferred \$886,021 from the CPF to the capital projects fund to finance the purchase of approximately three acres of land to be used for the construction of affordable housing. There is no provision in Town Law authorizing the expenditure of CPF monies for such a purpose.

Undocumented CPF Costs — The Town of East Hampton also lacks a system to identify the actual general fund costs incurred on behalf of the CPF. Therefore, the methodology used by Town officials to determine the amount to be reimbursed to the general fund from the CPF was based mostly on estimates rather than actual expenditures. The Town did not have proper documentation to support these estimates. As a result, Town officials were unable to prove that reimbursements totaling at least \$1.5 million from the CPF to the general fund were appropriate.

The CPF transferred a total of at least \$1.5 million from the CPF to the general fund, reportedly to reimburse the general fund for CPF-related expenditures paid between 2004 and 2007. To support the reimbursements, the Town's budget officer provided us with schedules showing how the reimbursements were calculated for 2005 through 2007. While the total reimbursement

for 2004 equaled the salary of a single employee, the amount reimbursed for the years 2005 through 2007 was developed by allotting a fixed percentage of certain Town salaries and fixed costs to the CPF, as follows:

Town Department	Percentage of Cost Allotted to CPF
Town Supervisor	10%
Town Comptroller	10%
Town Attorney	10%
Unallocated Insurance	10%
Natural Resources	10%
Community Preservation	100%

Town officials did not have any documentation to support their contention that the above percentages of Town department expenditures for 2005 through 2007 were actually related to the CPF, and were permitted by law to be paid from the CPF. To the extent that transfers exceeded actual CPF-related expenditures, the CPF was improperly subsidizing the activities of the general fund.

Wire Transfers

Wire transfers provide a means of direct access to the monies held in the Town's name. Appropriate controls over wire transfer activity include management authorization of a transaction before the transaction is initiated; itemized documentation to support the purpose, source, destination, and amount of the transaction; and documentation to appropriately account for and record the transaction. Town officials are responsible for segregating critical financial duties involved in wire transfer activity or providing compensating controls to help ensure transactions are authorized and appropriate.

During the two fiscal years 2006 and 2007, 19 wire transfers totaling \$31.9 million were made from the CPF to various Town bank accounts. Our review of these wire transfers disclosed six instances, totaling \$8.9 million, where wire transfers were initiated by employees who were not authorized to make them. We found that the former assistant budget officer initiated five transfers totaling \$4.4 million between June 2006 and April 2007, and the account clerk initiated a transfer of \$4.5 million on July 20, 2007. Neither the assistant budget officer nor the account clerk was authorized to make wire transfers. Although none of these

transfers was inappropriate, allowing unauthorized employees to initiate wire transfers could result in the misuse of CPF funds.

Recommendations

1. Town of East Hampton officials should discontinue the practice of temporarily advancing CPF monies to other funds.
2. Town of East Hampton officials should determine the amount of interest due to the CPF and ensure that the money is transferred from the appropriate Town funds.
3. Town of East Hampton officials should implement a system to identify the actual costs incurred by other funds on behalf of the CPF. Proper documentation should be retained to support these costs.
4. Town of East Hampton officials should provide the Town's depository banks with the names of employees and officials authorized by resolution to conduct transactions, such as wire transfers, on Town bank accounts.
5. Town of East Hampton officials should expend CPF funds for only those purposes authorized by law.

Payments in Lieu of Real Property Taxes

Town Law provides that Towns may make payments in lieu of real property taxes (PILOTs) to fire, fire protection, and ambulance districts (special districts) within the Central Pine Barrens area. To be eligible for PILOTs, more than 25 percent of the assessed value in each fire, fire protection, or ambulance district must be wholly exempt from real property taxes because it is owned by the State or a by municipal corporation (such as a county or Town). Certain school districts may also receive PILOTs from a CPF provided that real property within the school district (school districts need not meet the 25 percent requirement) has been made exempt from real property taxes in connection with CPF purposes and the school district is determined by the State Education Department to be a high- or average-need school district. No Town may use more than 10 percent of its CPF to make PILOTs in any calendar year. Southampton is the only Town within the Peconic Bay region that makes PILOTs to special districts and school districts.

Each year that PILOTs are due, Southampton must determine the total tax levied within Southampton by the eligible districts, and then determine the percentage of this amount levied by each district. The amount designated by Southampton for PILOTs is then allocated to each district according to this percentage, up to the amount of tax that would have been due to the district on the exempt lands owned by the State or the municipal corporation for preservation purposes. Town Law sets a maximum allocation for the PILOTs each district receives. If any monies remain after this first allocation, the leftover amount is allocated among the remaining eligible districts whose PILOTs have not yet reached the maximum allocation.

There are seven school and special districts within Southampton that met the PILOT eligibility requirements in 2007, as shown in the following table.

Districts Eligible for PILOTs in the Town of Southampton in 2007				
Name of District	Total Assessed Value (Southampton Town Portion)	Wholly Exempt Value	Amount Exempt for Preservation	Percentage Wholly Exempt
Riverhead Fire District	\$458,579,682	\$244,003,469	\$10,627,800	53 %
Flanders Fire District	\$856,575,159	\$218,942,200	\$136,355,400	26 %
Northeast Quogue Fire Protection District	\$436,391,181	\$295,080,520	\$58,299,434	68 %
Northampton Ambulance District	\$1,291,496,845	\$449,514,569	\$146,167,800	35 %
Riverhead Central School District	\$1,771,875,883	\$530,703,483	\$194,677,344	30 %
Hampton Bays Union Free School District	\$4,264,210,164	\$491,837,200	\$205,127,764	12 %
Eastport-South Manor Central School District	\$345,719,449	\$27,909,419	\$3,282,800	8 %

Our review of PILOTs made in prior years disclosed that PILOTs were not always based on proper calculation, which resulted in overpayments of \$107,650 to one special district in prior years, and an overpayment of \$2 million to a school district in 2007.

In 2007, Southampton's Receiver of Taxes performed an analysis of PILOT eligibility for the Flanders Fire District for prior years, which showed that the amount of tax exempt property in this fire district in 2004 and 2005 represented only 20 percent and 19 percent, respectively, of total assessed value. As a result, Flanders was not eligible for PILOTs from the Town of Southampton. However, Flanders received a PILOT of \$33,695 in 2004 and a PILOT of \$73,955 in 2005. When we brought this overpayment to the attention of the Town Supervisor in July 2008, she stated she had not previously been aware of this issue.

We also found that the PILOT made to the Riverhead Central School District in 2007 was inflated, because Southampton calculated the PILOT using the school district's entire tax levy, \$76.1 million, rather than the amount of tax levied only within Southampton, \$12.8 million. As a result, the Town awarded Riverhead a PILOT of \$3.1 million, representing 65 percent of the total PILOT distribution for the year. If the proper tax levy portion had been applied, Riverhead would have received only \$1.1 million, or \$2 million less than it was paid.

Since Riverhead received more than it was entitled to receive, and the total amount for PILOT distribution is fixed, the other six districts received less than their fair share. Hampton Bays Union Free School District received a PILOT of about \$1.4 million. Based upon Hampton Bays' tax levy, all of which was levied in Southampton, it was entitled to \$3.1 million – or about \$1.7 million more than it received. Likewise, the other five districts also received less than they were entitled to by the following amounts: Eastport-South Manor Central School District: \$234,000; Riverhead Fire District: \$19,600; Northampton Ambulance District: \$19,300; Flanders Fire District: \$17,500; and Northeast Quogue Fire Protection District: \$2,200. The Supervisor provided documentation to show that, as of 2008, the PILOTs for Riverhead are calculated properly because they are based on only the Southampton portion of the tax levies.

Recommendations

6. The Southampton Town Board should take steps to recover the \$107,650 overpayment made to the Flanders Fire District.
7. Southampton officials should annually review the assessed values of its special districts to ensure that only those meeting the eligibility requirements receive PILOTs.
8. The Southampton Town Board should work cooperatively with the Riverhead Central School District to recover the \$2 million overpayment through adjustments to future PILOT distributions.
9. The Southampton Town Board should take steps to ensure that Hampton Bays and the other five districts receive their fair share of the PILOT overpayment that was inappropriately given to Riverhead Central School District.
10. Where a school or special district is not wholly within Southampton, Town officials should verify that only the Southampton portion of the district's tax levy is used to calculate any PILOTs due to the district.

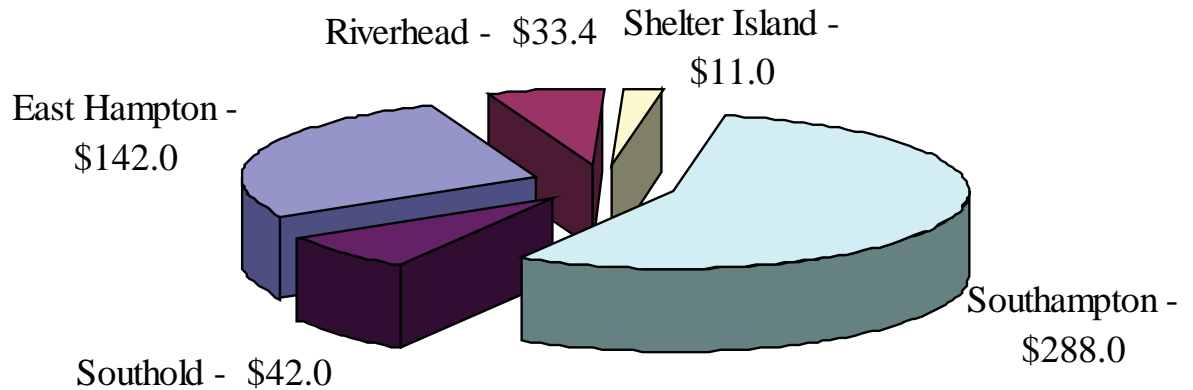
Collection and Recording of Revenues

At a minimum, the CPF of each Town receives all revenues generated from a 2 percent transfer tax on transfers of real property within the Town. This tax is generally collected by Suffolk County and is remitted to the Towns on a monthly basis. The tax imposed on transfers of real property that do not involve the transfer of a deed (i.e., shares in a condominium or co-operative housing) are collected directly by each Town. The transfer tax became effective as of April 1, 1999 and has a sunset date that has been extended through legislation to December 31, 2030.⁶ Town Law also authorizes the CPF of each Town to accept gifts of funds or any interests in land. Any interest accrued by monies deposited into the CPF must be credited to the CPF. From 1999 through March 2008, the CPFs established in East Hampton, Riverhead, Shelter Island, Southampton, and Southold have collectively generated approximately \$516 million.

CPF Transfer Tax Revenues

1999 – March 2008

(in millions)



Note: above figures include transfer tax revenues, but may not reflect gifts, donations, or interest

The Town Boards are responsible for establishing adequate internal controls to properly safeguard their respective Towns' cash assets. An effective system of internal controls over cash receipts ensures that all monies received are properly recorded,

⁶ Initially authorized by Chapter 114 of the Laws of 1998, the life of the 2 percent real estate transfer tax was originally scheduled to end at December 31, 2010. However, the New York State Legislature extended this date first to December 31, 2020 with Chapter 250 of the Laws of 2002, and ultimately to December 31, 2030 with Chapter 391 of the Laws of 2006.

deposited, and accounted for. We reviewed documents relating to the collection and recording of revenue and interviewed Town employees in all five Towns. Although the controls in place over the receipt and recording of revenue were generally adequate in Riverhead, Southampton and Southold, we found deficiencies in the controls of East Hampton and Shelter Island.

Recording Revenues

Timely, sufficient, and accurate accounting records assist local officials in the preparation of monthly and annual financial reports, which local officials can use to make informed decisions about revenue, expenditure and fund balance estimates in the annual budget, and to make needed budgetary modifications during the fiscal year.

In each Town, we reviewed general ledger transactions for the CPF revenue account codes and interviewed Town employees. As of June 2008, none of the revenue earned by the East Hampton CPF during the first three months of 2008 – approximately \$4.8 million, including transfer tax and interest – had been posted to the general ledger. When we brought this to the Supervisor’s attention, he indicated that he was aware of this, but that transferring prior years’ data to a new software system was a higher priority than posting current transactions to the general ledger.

While accurate and timely financial information is always a benefit for local officials, it is critically important for officials in East Hampton. East Hampton is currently experiencing significant financial stress, and the Town Board needs reliable financial records to actively manage the Town’s current budgetary commitments and limited cash resources. Without timely and accurate financial records, it is unlikely that the Town can produce credible financial reports. The lack of reliable financial reports hampers the Town Board’s ability to ensure that CPF monies are expended efficiently and in accordance with statutory requirements.

Collection and Handling of Cash

The Towns receive revenue for their CPFs from the transfer tax remitted monthly by Suffolk County, and from gifts, donations, and interest earned on investments. Effective controls over cash receipts require, among other things, that Town employees issue cash receipt forms and post such receipts to a log or cash receipts journal immediately upon receipt to provide evidence of the collection of cash. The receipt forms need to be press-numbered and issued sequentially. In addition, all forms need to be retained, including forms that have been voided. It is important that a

responsible manager reviews logs or journals to detect errors, inappropriate entries, or voids to prevent the loss or misuse of cash receipt data and to reduce the risk that Town monies could be stolen.

In addition, effective internal control over cash requires the separation of duties so that no single individual controls most or all phases of the cash collection and recording process. Although optimal segregation of duties may not always be practical, at a minimum, the duties of handling cash and maintaining financial records should be segregated. Assigning key duties (i.e., authorization, recordkeeping, and custody) to one individual significantly increases the risk that errors and/or irregularities might occur and go undetected and uncorrected. If it is not possible to segregate key duties, regular review of the cash collections results by a management official can serve as a compensating control measure.

Cash Collection Procedures – We reviewed the cash receipt logs, cash receipt forms, general ledgers, and bank statements in each of the five Towns. In general, the controls in place for the cash receipt process in East Hampton, Riverhead, Southampton, and Southold were adequately designed and effectively operating.

However, in Shelter Island, where CPF cash receipts averaged about \$1 million to \$2 million a year throughout the audit period, there were no procedures in place requiring the issuance of cash receipt forms, the recording of receipts in a log when monies are received, or the retention of receipt forms. The employee responsible for collecting receipts for the CPF did not issue press-numbered receipt forms when cash was collected and cash receipts were not posted to a cash receipts journal at the time money was received. Instead, after the employee deposited the cash in a bank account and the deposit was confirmed by the bank, the employee used the bank deposit slip as the source document for recording the cash receipt in the Town’s accounting records. No other Town official reviewed the accounting records to verify their accuracy. Unless the Town issues press-numbered receipts for cash received and promptly enters the amount received in the Town’s accounting records, there is increased risk that cash could be lost or stolen.

Segregation of Duties – We reviewed the responsibilities of employees collecting and handling cash and recording cash receipts in each of the five Towns. In general, we found that cash

handling and recording duties were adequately segregated in East Hampton, Riverhead, Southampton, and Southold.

However, during our audit period, the Shelter Island employee responsible for opening the mail, handling cash, and preparing bank deposits was also responsible for recording the transactions and depositing the money, which totaled about \$11 million. No other Town official reviewed the results of these transactions. Controls are compromised when all of these duties are performed by one individual because that individual has the ability to conceal a theft of funds by not recording a transaction or by altering records.

Because Shelter Island had poor cash collection and recording procedures and did not segregate financial duties, we traced 16 deposits totaling \$2,178,580 from the bank statements to the general ledger. These deposits were made to the Town's CPF bank account between December 1999 and March 2008. Although our tests disclosed no exceptions, it is essential that the Town institute adequate control procedures for recording cash receipts and segregate critical financial duties to reduce the risk that monies intended for the CPF could be misappropriated.

Recommendations

11. Town of Shelter Island officials should ensure that all revenues are recorded when they are received.
12. The Shelter Island Town Board should implement written procedures that govern the receipt and the recording of cash for all officers and employees.
13. Cash collections should be evidenced by the issuance of press-numbered receipts. Cash collections should be posted timely to a log or cash receipts journal.
14. Cash handling and recording duties should be performed by different individuals. If this is not possible, the Shelter Island Town Board or a Town official should provide periodic oversight.

Land Acquisition

The original purpose of establishing a community preservation fund was to implement a plan for the preservation of community character which, according to Town Law involves one or more of the following:

- Establishment of parks, nature preserves, or recreation areas
- Preservation of open space, including agricultural lands
- Preservation of lands of exceptional scenic value
- Preservation of fresh and saltwater marshes or other wetlands
- Preservation of aquifer recharge areas
- Preservation of undeveloped beach lands or shoreline
- Establishment of wildlife refuges for the purpose of maintaining native animal species diversity, including the protection of habitats essential to the recovery of rare, threatened, or endangered species
- Preservation of pine barrens consisting of such biota as pitch pine and scrub oak
- Preservation of forested land
- Preservation of unique or threatened ecological areas
- Preservation of rivers and river areas in a natural, free-flowing condition
- Preservation of public access to lands for public use, including stream rights and waterways
- Preservation of historic places and properties listed on the New York State register of historic places and/or protected under a municipal historic preservation ordinance or law
- Undertaking any of the above in furtherance of the establishment of a greenbelt.

As each Town established a CPF, Town Law required that the Town Boards adopt by local law a community preservation project plan. Town Law specified that the plan should include a list of every project the Town planned to take on in connection with its CPF, and a prioritized list of every Town property believed to be essential to protecting community character, with farmland as the highest priority. Town Law requires that, starting three years from the adoption of these plans, the Towns update their community preservation project plans at least once every five years.

Towns establishing a CPF were also required to create an advisory board of five to seven legal Town residents, including at least one active farmer, who have experience with land preservation or conservation and who serve on a voluntary basis. This advisory board is responsible for reviewing any proposed real estate acquisitions that would use CPF monies and making recommendations to the Town on these proposed acquisitions. A public hearing must be held after the advisory board has reviewed a proposed acquisition, but before the Town Board approves it.

Land acquisitions have been funded primarily by the 2 percent real estate transfer tax revenues, donations, and the issuance of debt. The Town Boards are responsible for establishing procedures that provide for the prudent and efficient use of CPF monies when acquiring land. Documentation of the acquisition process maintained by the Towns should include evidence of the seller's willingness to sell the property, evidence of at least one appraisal to identify the fair market value of the property, CPF advisory board and Town Board discussion of the property identifying a price range for negotiation, a public hearing, and Town Board authorization to sign the land sale contract.

Since the creation of the CPFs in East Hampton, Riverhead, Shelter Island, Southampton, and Southold in 1999, these Towns have used CPF monies to collectively acquire approximately 7,400 acres to preserve the characters of their communities.

Approximate Acres Acquired by Town April 1999 – March 2008	
Southampton	2,600
Riverhead	1,700
East Hampton	1,600
Southold	1,300
Shelter Island	200
Total	7,400

We reviewed the documentation for five acquisitions made in each of the Towns between April 1999 and March 2008. In general, each of the Towns has an adequate process in place to ensure the prudent and efficient expenditure of funds.

Amendments to Local Law

Municipal Home Rule and Tax Laws require a mandatory referendum⁷ to amend local laws with the intent of imposing, repealing, or re-imposing the 2 percent real estate transfer tax. As such, each time that the State enacted legislation to extend the life of the 2 percent real estate transfer tax, each of the five Towns was required to submit this to their voters for approval as an amendment to the local law of each Town.

We reviewed the local laws relating to the CPF in East Hampton, Riverhead, Shelter Island, Southampton, and Southold, and found that all the Towns had a record of referenda held for each amendment made to their respective local laws.

⁷ A referendum is a general vote by the electorate on a single political question that the Town has referred to them for a direct decision.

APPENDIX A

RESPONSES FROM LOCAL OFFICIALS

We provided a draft copy of this global report to each of the five Towns that we audited and requested responses. The following comments were excerpted from the three official responses received. Responses were provided by the Town of East Hampton, the Town of Shelter Island and the Town of Southampton.

OVERALL COMMENTS

Town of Shelter Island: “We do welcome the very constructive comments of the Comptroller’s auditors, which will be implemented and will improve our controls over Community Preservation Fund monies.”

Town of Southampton: “We appreciate the overall favorable review of ... Town’s administration of this critically important land acquisition and stewardship program, established in 1999 by enactment of Town Law, §64-e and Town Law Article 31-D.”

INAPPROPRIATE USES OF CPF MONIES

Town of East Hampton: “The Town agrees that General Municipal Law generally authorizes a municipal corporation to temporarily advance monies held in a fund to any other municipal fund. Said inter-fund advances should be repaid no later than the close of the fiscal year in which the advance was made with a reasonable amount of interest on said advance. Additionally, the Town agrees that Town Law, Article 4, Section 64-e, Subsection 2, prohibits the transfer of CPF funds to any other accounts, but the law is silent regarding inter-fund advances (loans). Based on the language in the law, the Town does not believe it improperly advanced funds.”

See
Note 1
Page 24

Town of East Hampton: “The Town disagrees with the opinion that the CPF was improperly subsidizing the general fund. According to Article 4, Section 64-e, Sub-section 4-d, the plan provides for a management and stewardship program for preserved land and properties. The Town further disagrees that by comparing the costs of the other five Towns, we can form an opinion on the reasonableness of the numbers.”

See
Note 2
Page 24

APPENDIX B

OSC COMMENTS ON LOCAL OFFICIALS' RESPONSES

Note 1

Town Law §64-e provides the purposes for which the monies are to be “exclusively” used. Monies from the fund may only be used for projects contained in the community preservation project plan. As such, CPF monies are monies which, “by law, may be used only for stated purposes” and, may not be advanced to other funds.

Note 2

We did not form an opinion on the reasonableness of the amount of money transferred from the CPF to cover management and stewardship costs. Our criticism of the amount of money transferred to the general fund was based on the fact that the Town does not have a system in place to identify the actual general fund costs incurred on behalf of the CPF. The methodology used by the Town to determine the amount to be reimbursed to the general fund from the CPF was based primarily on estimated rather than actual expenditures. The Town did not have proper documentation to support these estimates.

APPENDIX C

AUDIT METHODOLOGY AND STANDARDS

Our overall goal was to assess the adequacy of internal controls in place over the administration of the community preservation funds established by the Towns of the Peconic Bay region (East Hampton, Riverhead, Shelter Island, Southampton, and Southold) and to determine whether the Towns have complied with Town Law. Our audit encompassed the lifetime of the Peconic Bay Community Preservation Fund, from its inception on April 1, 1999 through March 31, 2008.

To accomplish the objectives of this audit, our procedures included the following:

- We interviewed appropriate Town officials and employees to determine the procedures in place over the collection and recording of revenue, the disbursement of monies, and the acquisition of land.
- We examined cash receipts and supporting documentation, general ledger and cash receipts journals, and bank statements to evaluate the controls over the collection of revenue and to assess whether the revenues were recorded timely.
- We selected a sample of disbursements made from each Town's community preservation fund to determine whether they were legitimate expenditures related to land acquisition or management and stewardship costs.
- We obtained and reviewed debt service schedules and other documentation to verify whether debt paid from the community preservation fund of each Town was properly allocated to the CPF and represented a legitimate liability incurred by the CPF.
- We selected five land acquisitions made by each Town between April 1999 and March 2008 to verify whether an adequate process was in place to ensure the prudent and efficient expenditure of funds.
- We reviewed the local laws (Town Code) in each Town and interviewed the Town clerk to determine whether referenda were held in connection with amendments to local law relating to the community preservation funds.

We based our performance criteria for this audit largely upon the enacting legislation contained within Town Law Article 4, Section 64-e and Tax Law Article 31-D. These laws contain requirements for the establishment and administration of community preservation funds by the five Towns of the Peconic Bay region of Suffolk County, New York.

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 objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

APPENDIX D

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