



Town of Otsego Financial Condition

Report of Examination

Period Covered:

January 1, 2012 — August 20, 2013

2013M-307



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

November 2014

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 Otsego, entitled Financial Condition. This audit was conducted pursuant to Article V, Section 1 of the State Constitution and the State Comptroller's authority as set forth in Article 3 of the 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 Otsego (Town) is located in Otsego County and includes a portion of the Village of Cooperstown. The Town has 3,900 residents and provides various services, including road maintenance, snow removal, fire protection and general government support. The Town's 2014 annual budget is \$1,542,024, financed primarily by real property taxes and sales tax.

An elected five-member Town Board (Board), comprising the Town Supervisor (Supervisor) and four Council members, governs the Town. The Supervisor serves as the Town's chief executive officer and chief fiscal officer. The Board, along with the Supervisor, is responsible for developing and adopting a balanced and realistic budget each year. All of the Board members in place during our audit took office in either January 2012 or January 2013.

Objective

The objective of our audit was to assess the Town's practices regarding budget development and adoption. Our audit addressed the following question:

- Did the Board adopt reasonable budgets?

Scope and Methodology

We examined Board minutes, adopted budgets and various financial reports, and we interviewed various Town officials and staff members for the period January 1, 2012 through August 20, 2013. We extended our audit period back to January 1, 2007 and forward to December 31, 2013 to examine and provide a more comprehensive understanding of the Town's financial position.

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 C 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 B, have been considered in preparing this report. Town officials generally agreed with our findings and indicated they plan 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 the New York

State General Municipal Law. For more information on preparing and filing your CAP, please refer to our brochure, *Responding to an OSC Audit Report*, which you received with the draft audit report. We encourage the Board to make this plan available for public review in the Town Clerk's office.

Financial Condition

While the Supervisor, as the Budget Officer, leads the Town's annual budget development process, the Board has the authority and responsibility to adopt realistic, structurally balanced budgets and to continually monitor the budget. A reasonable annual budget begins with sound estimates and well-supported budgetary assumptions. Spending levels and financial resources must be accurately gauged at budget preparation time to ensure that planned services are properly funded. To that end, Board members should avail themselves of as much pertinent information as possible. While valuable information is available from a number of sources, the Budget Officer should also work closely with the Highway Superintendent to develop budget estimates.

New York State Tax Law provides that, if a town with a village receives sales tax payments from the county and the village also receives such payments directly from the county, the town must first use the sales tax proceeds to benefit the area outside the village. Such operations are accounted for in the part-town funds. However, when a town does not levy property taxes in its part-town funds, it may then apply portions of the sales tax revenues on a town-wide basis. Because the Town has a village, the Board must ensure that sales tax revenue estimates are realistic and properly allocate sales tax revenues to the appropriate funds. Doing so will ensure equity among taxpayers and that only necessary amounts of taxes are being raised.

The Board did not adopt realistic budgets; budgets varied significantly from the actual results each year. We reviewed the Town's four operating funds¹ for the four-year period ending in 2013 to determine if the Board reasonably budgeted for revenues and expenditures. Annually, each of the funds' estimates generally varied from actual results: the general town-wide and highway part-town overestimated revenues and expenditures, the general part-town underestimated revenues and overestimated expenditures and the highway town-wide underestimated both revenues and expenditures. Our budget-to-actual comparisons for all funds are included in Appendix A.

¹ Because the Town includes a portion of a village, it maintains the following four funds: general town-wide, general part-town, highway town-wide and highway part-town.

These unrealistic budgets resulted in annual operating surpluses that caused unexpended surplus funds² to increase in the general town-wide and highway part-town funds year after year, as indicated in Figure 1.

Figure 1: Unexpended Surplus Funds

	FY 2010	FY 2011	FY 2012	FY 2013
General Town-Wide Fund	\$472,654	\$516,292	\$579,450	\$558,068
General Part-Town Fund ^a	\$238,419	\$237,669	\$234,846	\$238,033
Highway Town-Wide Fund ^b	\$529,586	\$403,192	\$213,731	\$182,410
Highway Part-Town Fund	\$111,423	\$155,066	\$222,599	\$416,311

^a The general part-town fund's unexpended surplus remained relatively unchanged during this period due to the limited activity and routine nature of the items accounted for in this fund.
^b The highway town-wide fund's unexpended surplus declined during this period mainly due to unbudgeted equipment purchases.

For fiscal years 2010 through 2013, total actual revenues for the combined general and highway funds exceeded budget estimates by an aggregate of more than \$315,000. Revenue variances were primarily driven by inaccurate sales tax estimates, which were consistently underestimated by a total of \$686,432, or 64 percent. The Town’s average annual sales tax was estimated at \$267,815, whereas the average annual sales tax actually received was \$439,423 for the four years reviewed.

The impact of the sales tax variances was exacerbated by the inconsistent allocation of sales tax revenues across the four operating funds. During the four years reviewed, the Town received more than \$1.7 million in sales tax revenues. The Board should have first eliminated the tax levy in the part-town funds before allocating sales tax to the town-wide funds but did not do so. Specifically, over the four years, the Board should have allocated \$321,864 between the general town-wide and highway town-wide funds, but instead allocated more than \$1 million. The general part-town fund should have been allocated \$38,454 but was allocated \$27,500, and the highway part-town fund should have been allocated \$710,940 but was allocated \$688,647. This improper allocation of sales tax caused taxpayer inequities; part-town funds were taxed more than necessary while the town-wide funds were charged less than they should have been.

² The Governmental Accounting Standards Board (GASB) issued Statement 54, which replaces the fund balance classifications of reserved and unreserved with new classifications: nonspendable, restricted, and unrestricted (comprising committed, assigned and unassigned funds). The requirements of Statement 54 are effective for fiscal years ending June 30, 2011 and beyond. To ease comparability between fiscal years ending before and after the implementation of Statement 54, we will use the term “unexpended surplus funds” to refer to that portion of fund balance that was classified as unreserved, unappropriated (prior to Statement 54), and is now classified as unrestricted, less any amounts appropriated for the ensuing year’s budget (after Statement 54).

Overall, the conservative revenue estimates resulted in positive budget variances and unused appropriated fund balance. While the Board appropriated more than \$1.4 million in fund balance to fund operations in these four years, it actually used \$350,672 (24 percent) of this amount during this time. Ultimately, the Board's budgeting practices resulted in operating surpluses that limited the intended use of fund balance. The Town had a total unexpended surplus fund balance of \$1.39 million in its four operating funds in 2013, while its budgets for these funds averaged about \$1.3 million. Maintaining surplus funds that are equivalent to the total annual budget is excessive.

We discussed Town officials' budgeting practices with them during our fieldwork; they told us that the Board's practice for developing the budget was to consider the previous year's adopted amounts, along with any requests for purchases from department heads. Basing budget estimates on previous years' inaccurate estimates will continue the trend of increasing already excessive fund balances. We also reviewed the Town's 2014 adopted budget and determined that the Board's practices of misallocating sales tax continued. Specifically, it budgeted to levy real property taxes and also allocate sales tax revenues to the town-wide funds without first eliminating the tax burden for the part-town funds. Therefore, it is likely that the Town will end 2014 with surpluses and taxpayer inequities similar to those in previous years.

By improving its budgeting practices and adopting realistic budgets, the Board will have an accurate depiction of the Town's actual financial condition. Further, by distributing sales tax in an equitable manner, it will be more accountable to taxpayers.

Recommendations

The Board should:

1. Utilize all information provided to it, including actual revenues and expenditures, when developing budgets. Such information will allow it to adopt more realistic budgets.
2. Adopt budgets that properly allocate sales tax revenues in accordance with statutory requirements.
3. Reduce the amount of surplus fund balance by:
 - Continuing to appropriate fund balance and
 - Establishing and funding necessary reserve funds.

APPENDIX A

BUDGET-TO-ACTUAL COMPARISON BY FUND

Figure 2: Budget-to-Actual Comparison								
General, Town-Wide					General, Part-Town			
	2010	2011	2012	2013	2010	2011	2012	2013
Estimated Revenues	\$312,570	\$263,370	\$238,720	\$332,446	\$28,577	\$28,027	\$36,025	\$36,305
Actual Revenues	\$368,009	\$339,496	\$334,015	\$271,842	\$11,267	\$29,573	\$29,088	\$35,293
Variance	\$55,439	\$76,126	\$95,295	(\$60,604)	(\$17,310)	\$1,546	(\$6,937)	(\$1,012)
% Variance	18%	29%	40%	(18%)	(61%)	6%	(19%)	(3%)
Appropriations	\$372,570	\$341,365	\$331,446	\$332,446	\$34,577	\$31,780	\$36,305	\$36,305
Actual Expenditures	\$403,801	\$295,858	\$270,840	\$293,224	\$32,995	\$30,530	\$31,911	\$32,106
Variance	(\$31,231)	\$45,507	\$60,606	\$39,222	\$1,582	\$1,250	\$4,394	\$4,199
% Variance	(8%)	13%	18%	12%	5%	4%	12%	12%
Highway, Town-Wide					Highway, Part-Town			
	2010	2011	2012	2013	2010	2011	2012	2013
Estimated Revenues	\$329,878	\$280,078	\$179,326	\$372,326	\$416,136	\$535,936	\$567,468	\$583,868
Actual Revenues	\$328,991	\$348,250	\$294,150	\$302,584	\$262,518	\$543,726	\$557,619	\$656,807
Variance	(\$887)	\$68,172	\$114,824	(\$69,742)	(\$153,618)	\$7,790	(\$9,849)	\$72,939
% Variance	0%	24%	64%	(19%)	(37%)	1%	(2%)	12%
Appropriations	\$414,878	\$381,276	\$372,326	\$372,326	\$490,136	\$560,276	\$583,868	\$583,868
Actual Expenditures	\$340,516	\$474,644	\$484,126	\$333,905	\$494,618	\$499,112	\$490,085	\$555,628
Variance	\$74,362	(\$93,368)	(\$111,800)	\$38,421	(\$4,482)	\$61,164	\$93,783	\$28,240
% Variance	18%	(24%)	(30%)	10%	(1%)	11%	16%	5%

APPENDIX B
RESPONSE FROM LOCAL OFFICIALS

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

TOWN OF OTSEGO
P O BOX 183
FLY CREEK, NY 13337

October 1, 2014

To: Office of the State Comptroller
State of New York
[REDACTED]
Division of Local Government and
School Accountability
49 Hawley Street
Binghamton, NY 13901

**Response to the Draft Audit of the Budget Process
of the Town of Otsego's Financial Condition including the CAP**

Supervisor Anne Geddes-Atwell and Town Board members Bennett Sandler, Thomas Hohensee, and Julie Huntsman have worked diligently with the auditors. The Board agrees with the findings of this report and the stated recommendations will guide the Board in future budget planning.

Enclosed please find the Town's Corrective Action Plan for the 2015 budget.

Sincerely,

Anne Geddes-Atwell
Supervisor
Town of Otsego

Enclosure: Town of Otsego Plan of Corrective Action for the 2015 Budget

TOWN OF OTSEGO
P O BOX 183
FLY CREEK, NY 13337

October 1, 2014

**TOWN OF OTSEGO FINANCIAL CONDITION DRAFT
REPORT OF EXAMINATION
January 1, 2012 – August 20, 2013
PLAN OF CORRECTIVE ACTION for the 2015 BUDGET**

The Town sent the draft audit report to our accountants, Mostert, Manzanero & Scott for review. Both our accountant and one of the company's partners reviewed the draft. In feedback, they concurred with the items in the draft audit. Accounting professionals will regularly review the Town's quarterly reports in 2015.

In response to the List of Recommendations provided by the auditors, the Town Board is proceeding as follows:

1. Audit Recommendation:

Utilize all information provided to it, including actual revenues and expenditures, when developing budgets. Such information will allow it to adopt more realistic budgets.

Implementation Plan of Action(s):

The Town Board will review actual annual revenues and expenditures over the previous three years. It will use this data to produce a more realistic budget. Due to the Village Court consolidation with the Town that occurred on April 1, 2014 and with no true past figures to guide us, the Board is working with the court's department heads to produce a realistic budget.

2. Audit Recommendation:

Adopt budgets that properly allocate sales tax revenues in accordance with statutory requirements.

Implementation Plan of Action:

In the 2015 budget, the Board is planning to complete its compliance with the sales tax allocation statute by adopting future budgets which allocate sales tax revenues into the B and DB Funds until property tax is "covered."

3. Audit Recommendation:

Reduce the amount of surplus fund balance by:

- Continuing to appropriate fund balance, and
- Establishing and funding necessary reserve funds.

Implementation Plan of Action:

The 2015 budget will utilize fund balance to offset changes in taxation and will add appropriate revenues into each of two reserve funds.

Person Responsible for Implementation:

The Town Board has worked with the Supervisor to arrive at these solutions. Supervisor Anne Geddes-Atwell is the person responsible.

Signed:

Date:

October 2, 2014

Anne Geddes-Atwell

APPENDIX C

AUDIT METHODOLOGY AND STANDARDS

Our overall goal was to assess the Board's practices when developing budgets to determine if Board-adopted budgets were reasonable. To accomplish our audit objective and obtain valid and relevant audit evidence, we performed the following procedures:

- We interviewed the Supervisor, Board members and Town staff members to gain an understanding of the Town's budget process and information used when determining amounts to be budgeted.
- We compared budgeted revenues and expenditures to actual revenues and expenditures for the last four completed years (2010-2013) to determine if Board-adopted budgets were reasonable.
- We compared budgeted sales tax revenues to actual sales tax revenues to determine if the Board used realistic figures for sales tax revenues when developing budgets. We also reviewed the distribution of sales tax revenues to determine if distribution was appropriate.
- We compared historical averages of revenues and expenditures to budgeted revenues and expenditures to determine if Board-adopted budget estimates were reasonable.
- We calculated the results of operations (revenues vs. expenditures) and determined if budgeted fund balance appropriations were in fact appropriated.
- We calculated surplus fund balances as a percentage of the ensuing year's appropriations to determine if percentages were increasing or decreasing.

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 D

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