



# Village of Fort Edward Financial Condition

## Report of Examination

Period Covered:

June 1, 2010 — October 25, 2011

2012M-175



Thomas P. DiNapoli

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# State of New York Office of the State Comptroller

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## **Division of Local Government and School Accountability**

December 2012

Dear Village 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 Village 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 Village of Fort Edward, 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 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 Village of Fort Edward (Village) is located in Washington County. The Village covers one square mile and has a population of almost 3,600 residents. The Village provides various services to its residents, including water services, law enforcement, street maintenance, snow removal, and general government support. The Village's general fund budget for fiscal year 2011-12 was \$2.1 million.

The Village Board (Board) is comprised of four elected Trustees and an elected Village Mayor (Mayor). The Board is the legislative body responsible for the general management and control of the Village's financial affairs, as well as establishing financial policies and procedures. The Board has the power to levy taxes on real property located in the Village and to issue debt.

The Mayor is the Village's chief executive officer and the Village Clerk-Treasurer is the chief financial officer. The Clerk-Treasurer is responsible for preparing, maintaining, and reporting all necessary financial information. The Water Superintendent is responsible for the daily operation of the water treatment plant, including oversight of the water processing and distribution procedures. Other Village officials oversee the Police, Street, and Recreation Departments.

## Objective

The objective of our audit was to evaluate the Village's financial condition for the period June 1, 2010 to October 25, 2011. Our audit addressed the following related question:

- Does the Board adopt realistic budgets and take appropriate actions to maintain the Village's financial stability?

## Scope and Methodology

We examined the Village's financial operations for the period June 1, 2010 to October 25, 2011.

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 Village officials and their comments, which appear in Appendix A, have been considered in preparing this report. Village 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 the 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 Village Clerk's office.

## Financial Condition

The Board is responsible for making sound financial decisions that are in the best interest of the Village and its taxpayers. As such, it is essential that the Board adopt structurally balanced budgets<sup>1</sup> that provide sufficient recurring revenues to finance recurring expenditures for all operating funds. To do so, the Board must receive accurate financial information to assist it in financial planning and oversight. Additionally, Village officials should ensure that the level of fund balance – i.e., the accumulated difference between revenues and expenditures from prior years – is sufficient to provide available cash for contingencies throughout the year. Furthermore, the Board must ensure that interfund advances are repaid as soon as possible to avoid placing an undue burden on the funds loaning the moneys. Having a multi-year plan in place for future capital expenditures allows the Board to address such needs before they become emergencies.

We found that the reported unreserved fund balances for the water fund, (\$114,017), and the general fund, \$475,041, were inaccurate due to various accounting errors. After adjusting for these accounting errors, the water fund's deficit was reduced to (\$10,454) and the general fund's positive balance was reduced to \$290,041.

The water fund's continued reliance on the general fund to fund operating costs will result in an inequity among low-usage tax payers, and is impairing the general fund's financial condition. The Board has not yet adopted a long-term financial and capital plan for the water fund. Without a long-term capital plan, the Village may be unable to replace the water fund's aging infrastructure in a timely, cost-effective manner.

### Water Fund

The Village charges fees for water services based on water usage. Ideally, the Board should structure these user fees to ensure that they adequately cover the water fund's operating costs. However, Village Law allows a village to defray the cost of operating and maintaining a water system by charging water rents, a general tax, or a combination of both methods.<sup>2</sup>

Although the water fund's reported unreserved fund balance deficit at May 31, 2011 was (\$114,017), it was significantly overstated. After adjustment for accounting errors, the deficit was reduced to (\$10,454). These accounting errors included an understatement of

<sup>1</sup> A budget is structurally balanced when, with the cyclical fluctuations of the business cycle removed, revenues equal expenditures.

<sup>2</sup> Village Law Section 11-1118. See also 34 Opinion of the State Comptroller 26, 1978 and Opinion of the State Comptroller 69-346

water rents receivable of \$28,563 and an overstatement of interfund payables of \$75,000. After adjustment, the water fund balance sheet still included a \$105,000 interfund advance payable to the general fund. As discussed below, with its current revenue structure, it is unlikely that the water fund will be able to repay this advance.

We examined the budgets and corresponding results of operations for the fiscal years ending in 2009, 2010, and 2011 and found that the water fund experienced operating deficits each year, more significantly in the first two years. In each year, the operating deficits were primarily the result of a shortfall in water rents. These deficits were offset, to some degree, by an under-expenditure of appropriations. Operations improved in the 2010-11 fiscal year due to a reduction in debt expenditures and an increase in residential water rates for the 2010-11 fiscal year. However, revenues continue to fall short because the Village has collected less water rents from industrial users each year and has not accurately adjusted budget estimates in response to that decrease. Annual operating results for the water fund are shown in Table 1.

<b>FYE May 31</b>	<b>Revenues or Expenditures</b>	<b>Adopted Budget</b>	<b>Actual</b>	<b>Budget Variance</b>	<b>Percentage of Actual to Budgeted</b>
2012	Revenues	\$370,000	\$354,687	(\$15,313)	95.9%
	Expenditures	\$370,000	\$341,981	(\$28,019)	92.4%
	Operating Surplus		\$12,706		
2011	Revenues	\$366,400	\$323,638	(\$42,762)	88.3%
	Expenditures	\$366,400	\$335,579	(\$30,821)	91.6%
	Operating Deficit		(\$11,941)		
2010	Revenues	\$397,800	\$294,051	(\$103,749)	73.9%
	Expenditures	\$397,800	\$384,614	(\$13,186)	96.7%
	Operating Deficit		(\$90,563)		
2009	Revenues	\$465,400	\$336,348	(\$129,052)	72.3%
	Expenditures	\$465,400	\$378,224	(\$87,176)	81.3%
	Operating Deficit		(\$41,876)		

Annual shortfalls in water rents are illustrated in Table 2.

<b>FYE May 31</b>	<b>Adopted Budget</b>	<b>Actual</b>	<b>Budget Variance</b>	<b>Percentage of Actual to Budgeted</b>
2012 Water rents	\$320,000	\$296,834	(\$23,166)	92.8%
2011 Water rents	\$316,300	\$291,624	(\$24,676)	92.2%
2010 Water rents	\$357,300	\$260,895	(\$96,405)	73.0%
2009 Water rents	\$424,900	\$303,349	(\$121,551)	71.4%

Preliminary data for the 2011-12 fiscal year indicates that the water fund will finish the year with an operating surplus in excess of \$12,000, which will result in a positive fund balance of approximately \$2,000. This surplus is partially due to an increase in interfund revenues resulting from increased billings for work performed by water department employees. The preliminary data also indicates that water rents continued to fall short of budget estimates by approximately \$23,000 in the 2011-12 fiscal year. Based on 2012-13 budget information reported by Village officials, they continued to estimate water fund revenues at levels similar to 2011-12, which will continue the same trend of annual revenue shortfalls.

As illustrated in Tables 1 and 2, a structural imbalance exists between budgeted revenues and expenditures. This becomes even more problematic when water-related debt that is budgeted and paid for by the general fund is considered. For example, while water fund expenditures in the 2010-11 fiscal year totaled \$335,579, water-related debt that was budgeted and paid for by the general fund in the same year totaled \$414,107. According to the Mayor, the general fund pays for this debt because, years ago, a prior administration decided that this arrangement was preferable to a very large water rate increase.

If Village officials continue their current budgeting practices, the true cost of providing water to Village customers will not be readily apparent, setting water rates becomes more difficult, interfund loan balances owed to the general fund will likely go unpaid, and the shift of funding from users to taxpayers may result in an inequity to low-usage taxpayers.

## **General Fund**

The general fund's financial condition relies on the Board's ability to adopt realistic budgets and manage the Village's financial operations throughout the year within the budget's parameters. Such management requires timely and accurate financial data. General Municipal Law states that moneys advanced between funds are to be repaid as soon as the funds become available, but no later than the close of the fiscal year in which the advance was made. While the use of interfund advances is a permissible form of short-term borrowing to meet current cash flow needs, it is not intended to be used as a long-term approach to provide financial resources from one operating fund to another.

Although the general fund's reported unreserved fund balance at May 31, 2011 was \$475,041, it was significantly overstated. After adjustment for accounting errors, it was reduced to \$290,041. These accounting errors resulted from a failure to write-off advances made by the general fund to two capital projects totaling \$185,000 after the

projects were completed and resources were not available to repay them. As of May 31, 2011, general fund advances to the water fund totaled \$105,000 after adjustment for erroneous entries. The water fund does not repay interfund advances by the end of the fiscal year, and due to the water fund's current financial condition, this amount may not be collectible.<sup>3</sup>

We examined the budgets and corresponding results of operations for the fiscal years ending in 2009, 2010, and 2011 and found that the general fund experienced no unplanned operating deficits during that period. Except for a material overestimation of expenditures (\$145,330) in the last year of the period,<sup>4</sup> general fund budget estimates were reasonable and structurally balanced. Preliminary data for the 2011-12 fiscal year indicates that the general fund continues to operate within the adopted budget and maintain reasonable levels of fund balance.

However, even though the general fund adopts realistic budgets, the water fund's continued reliance on the general fund for operating costs is impairing the general fund's financial condition. As currently configured, water fund resources are insufficient to fund water-related debt. This debt primarily was funded by the general fund through a mix of budgetary appropriations and interfund loans. For example, in the fiscal year ended May 31, 2011, water-related debt that was budgeted, paid, and reported by the general fund totaled \$414,107, which was 23 percent of total general fund expenditures. In the fiscal year ending May 31, 2012, payments by the general fund for water-related debt totaled \$274,504 at December 31, 2011.<sup>5</sup> This amount still comprises 13 percent of total budgeted general fund expenditures.

The current method of providing for and reporting water-related debt distorts general fund operations and puts the general fund at risk during times of financial stress.

## Long-Term Plan

Multi-year financial planning is a tool for local governments struggling with impending difficult financial situations. It allows decision-makers to set long-term priorities and work toward goals, rather than reacting to the fiscal crisis of the moment. Having a plan

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<sup>3</sup> Advances were made from the general fund to the water fund during both the 2009-10 and 2010-11 fiscal years; neither advance was repaid by the end of the fiscal year, as required.

<sup>4</sup> In the fiscal year ending May 31, 2011, general fund appropriations totaled \$1,989,141; however, actual expenditures totaled \$1,843,811, which was only 92.7 percent of total appropriations. This was due to an accumulation of several individual overestimated accounts.

<sup>5</sup> The last of the water-related debt payments in the 2011-12 fiscal year were paid on December 27, 2011.

allows local government officials to see the impact of their decisions over time, alter some of the variables in the governing equation and project various outcomes. Officials can then make the most prudent choice in the best interest of the taxpayers.

Village officials informed us that the water system has an aging infrastructure (old water lines, dysfunctional meters, etc.) and that the Village will have to address future capital requirements. As infrastructure improvements and replacements can be quite costly, it is important to plan ahead so that funds will be readily available when needed. However, the Board has not yet adopted a long-term financial and capital plan for the water fund. Without a long-term capital plan, the Village may be unable to replace the aging infrastructure in a timely, cost-effective manner.

### **Recommendations**

1. The Board should consider establishing water rates that are sufficient to finance water fund operations, including water-related debt payments.
2. The Board should review and address the outstanding interfund advance balance owed to the general fund by the water fund by either forgiving the loan or providing for its repayment. Future interfund advances should be repaid no later than the close of the fiscal year in which the advance was made.
3. The Board should develop a plan to address long-term infrastructure improvements to the water system.

**APPENDIX A**  
**RESPONSE FROM LOCAL OFFICIALS**

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



# VILLAGE OF FORT EDWARD

118 Broadway, P.O. Box 345, Fort Edward, N.Y. 12828  
Phone (518) 747-4023

November 16, 2012

Mr. Jeffrey Leonard  
Office of the State Comptroller  
Division of Local Government  
1 Broad Street Plaza  
Glens Falls, NY 12801

Dear Mr. Leonard,

I appreciate the opportunity for the Village Clerk-Treasurer and myself to meet with the State Comptrollers office on November 7<sup>th</sup> to discuss the examination of the period of June 1, 2010 through October 2011.

We ask that the letter serve as the Village's response and action plan.

The following content of this letter will detail the states recommendation and the village's response to the recommendations:

1) The board should consider establishing water rates that are sufficient to finance water fund operations, including water related debt payments. *The Board along with the Village Engineer will look at the rate analysis of residential, commercial and industrial users. We are currently looking at replacing the thirty (30) year old meters with new, more accurate meters. Replacement of inaccurate industrial meters is also in the works. We are developing a plan to gain additional customers from outside the village to increase revenues.*

2) The board should review and address the outstanding interfund loan balance owed to the General Fund by the water fund by either forgiving the loans or providing for its repayment. Future interfund loans should be paid no later that the close of the fiscal year it was made.

*Unfortunately, the Water Fund does not and will not have the funds to repay the General Fund. The board will pass a resolution to "forgive" the outstanding loan to the General Fund.*

3) The board should develop a plan to address long-term infrastructure improvements to the water system.

*Work on the infrastructure is underway now. This year we replaced over 2000 foot of water lines, with another 5000 plus to be done next year. A plan has started and we are working on a long term plan for additional work. These improvements, along with implementing a new rate schedules and new meters will allow the village board to have an accurate cost of water services for the Village of Fort Edward.*

The Village of Fort Edward hopes that even though the finances were not correctly labeled that it is apparent that our intentions are to keep the Village of Fort Edward in the best financial condition.

Sincerely,

Matthew Traver  
Mayor  
Village of Fort Edward

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## APPENDIX B

### AUDIT METHODOLOGY AND STANDARDS

Our overall goal was to assess the adequacy of the internal controls put in place by Village officials to safeguard Village assets and monitor financial activities. To accomplish this, we performed an initial assessment of the internal controls so that we could design our audit to focus on those areas most at risk.

During the initial assessment, we interviewed Village officials, performed limited tests of transactions, and reviewed pertinent documents such as Village policies, Board minutes, and financial records and reports. After reviewing the information gathered during our initial assessment, we determined where weaknesses existed, and evaluated those weaknesses for the risk of potential fraud, theft and/or professional misconduct. We then decided upon the reported objectives and scope by selecting for audit those areas most at risk. We selected financial condition for further review.

To review the Village's financial condition, we performed the following steps:

- We interviewed officials to gain an understanding of the Village's budget process and financial accounting system.
- We reviewed the results of operations, determined their impact on fund balances, and projected the water fund deficit at May 31, 2012.
- We reviewed the Village's periodic financial reports.
- We reviewed budgets to determine if they were reasonable and structurally balanced.
- We analyzed interfund borrowings.
- We reviewed the Village's 2011 tax limit calculation.
- We reviewed water fees to determine if they adequately covered the cost of operations.
- We reviewed the Village's periodic financial reports and meeting minutes.

We conducted this 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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