

Village of Potsdam

Financial Condition

MAY 2017



OFFICE OF THE NEW YORK STATE COMPTROLLER
Thomas P. DiNapoli, State Comptroller

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Report Highlights

Village of Potsdam

Audit Objective

Determine whether the Board effectively managed financial condition.

Key Findings

- The Board has taken actions to improve the Village's financial condition, but Village officials should remain vigilant.
- The Village's hydroelectric and sewer funds had deficit fund balances of \$223,006 and \$71,132, respectively, as of May 31, 2016.
- The general fund's unrestricted fund balance was relatively low, at approximately \$287,000 (4.5 percent of appropriations) as of May 31, 2016.
- The Board has not adopted multiyear financial and capital plans.

Key Recommendations

- Continue to work to eliminate deficits in the operating funds and to increase fund balance to the levels established in the Board's fund balance policy.
- Develop and adopt multiyear financial and capital plans.

Village officials generally agreed with our recommendations and indicated they planned to take corrective action.

Background

The Village of Potsdam (Village) is located in the Town of Potsdam in St Lawrence County. The Village Board of Trustees (Board) is the legislative body responsible for managing Village operations and for maintaining sound financial condition. The Board consists of five elected members: one Mayor and four Trustees. The Mayor serves as the chief executive officer. The Board appoints a Village Administrator who is responsible for the Village's day-to-day management. The Clerk-Treasurer is responsible for the receipt, disbursement and custody of Village moneys, maintaining accounting records and providing financial reports.

Quick Facts

Employees	72
Population	9,428
2016-17 Budgeted Appropriations	\$9.8 million

Audit Period

June 1, 2015 – November 30, 2016. We extended the audit period back to June 1, 2013 to analyze revenue and expenditure trends, budget-to-actual comparisons and fund balance levels. We also extended the period forward to February 28, 2017 to review certain year-to-date operating results.

Financial Condition

Financial condition may be defined as the ability to balance recurring expenditure needs with recurring revenue resources, while providing desired services on a continuing basis. A village in good financial condition generally maintains adequate service levels during fiscal downturns and develops resources to meet future needs. Conversely, a village in fiscal stress usually struggles to balance its budget, may suffer through disruptive service level declines, has limited resources to finance future needs and may have minimal cash available to pay current liabilities as they become due.

What is Effective Financial Condition Management?

To effectively manage financial condition, the Board must adopt realistic and structurally balanced budgets for all operating funds that provide sufficient recurring revenues to finance recurring expenditures. Once the budget has been adopted, the Board should monitor year-to-date revenues and expenditures against corresponding budget estimates to ensure budget amendments are implemented before financial condition is negatively affected.

The Board should adopt a policy to establish the level of fund balance to be maintained in each fund and also create multiyear financial and capital plans. Planning on a multiyear basis allows Village officials to identify developing revenue and expenditure trends, set long-term priorities and goals and consider the impact of current budgeting decisions on future fiscal years. It also allows Village officials to assess the impact and merits of alternative approaches to address financial issues, such as the use of fund balance to finance operations. Effective multiyear plans project operating and capital needs and financing sources over a three- to five-year period. Long-term financial plans work in conjunction with Board-adopted policies and procedures to provide necessary guidance to employees on the financial priorities and goals set by the Board. Also, the Board must monitor and update long-term financial plans on an ongoing basis to ensure that its decisions are guided by the most accurate information available.¹

Maintaining a reasonable level of unrestricted fund balance² is a key element of effective long-term financial planning. If the amount retained is too low, the Village may not have a sufficient financial cushion for emergencies. It is important for the Board to adopt a policy that addresses the level of fund balance to be maintained in each fund and to use the policy in the annual budgeting process to help ensure that fund balance levels are adequate.

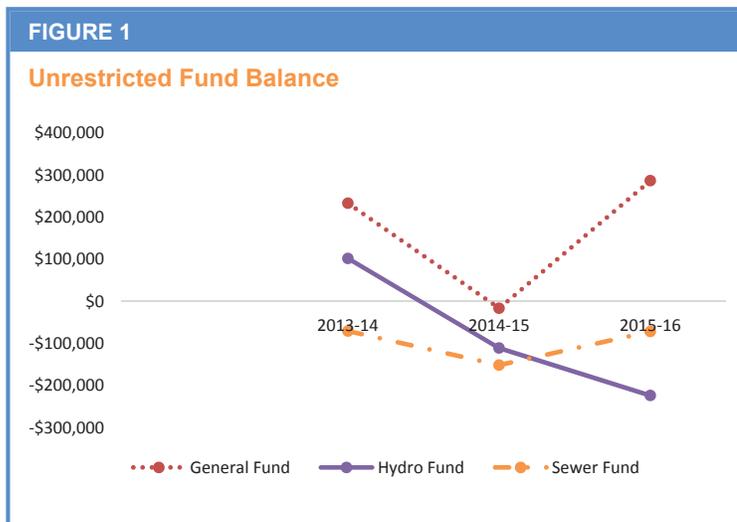
¹ See <http://www.osc.state.ny.us/localgov/planbudget/>

² For the purpose of this report, unrestricted fund balance represents the total of assigned and unassigned fund balance classifications. It does not include the portions of fund balance that are classified as restricted (i.e., reserves) and nonspendable (for example, inventories, long-term portions of loans receivable).

The Village's Financial Condition Is Improving, But It Still Has Deficit Fund Balances

The Board has taken actions to improve the Village's financial condition, but Village officials should remain vigilant to continue these improvements. In February 2015, the Board adopted a fund balance policy that established the minimum desired fund balance levels the Board wants to maintain in each operating fund and budgetary procedures to help the Village achieve and maintain those levels. The policy sets a minimum fund balance target of \$500,000 for the general fund, \$250,000 for the water and sewer funds, \$100,000 for the hydroelectric fund and \$50,000 for the refuse fund.³ Each month, the Board receives detailed budget versus actual reports for all funds. In addition, the Board approves budget modifications at regular Board meetings as necessary. However, even though the Board is actively engaged in monitoring the budget, the Village's hydroelectric and sewer funds had deficit fund balances as of May 31, 2016. In addition, the general fund's unrestricted fund balance was relatively low, leaving the Village vulnerable to cash flow concerns and fiscal stress. As indicated in Figure 1, as of May 31, 2016:

- The general fund's unrestricted fund balance was \$286,896 (4.5 percent of the ensuing year's appropriations of \$6,371,746).
- The hydroelectric fund had an unrestricted fund balance deficit of \$223,006. This deficit represents more than half of the ensuing year's appropriations of \$420,535.
- The sewer fund had an unrestricted fund balance deficit of \$71,132, which is (4.2) percent of the ensuing year's appropriations of \$1,681,851.



³ According to the policy, reserves and fund balance used for budgetary purposes (appropriated fund balance) shall not be included in the fund balance minimum for the general fund. Also, reserves are excluded from the desired fund balance minimum for the water and sewer funds.

General Fund — The Board did not appropriate any fund balance in the general fund budgets for fiscal years 2014-15 through 2016-17. Although the general fund ended 2014-15 with a deficit unrestricted fund balance of \$15,911,⁴ it generated an operating surplus of about \$410,000 in 2015-16, which helped replenish the unrestricted fund balance to \$286,896. Even with this improvement, it is important for the Board and Village officials to continue to closely monitor the budget because this level of fund balance provides the Village with a limited financial cushion for unexpected events and maintaining cash flow.

To reduce costs, the Board abolished the Village justice court as of December 2015, which was estimated to provide annual net savings of approximately \$152,500. In an effort to address the general fund's financial condition, the Board has increased real property taxes 32 percent over the past three years, from \$2,660,359 in 2013-14 to \$3,521,690 in 2016-17. However, the Village is nearing its Constitutional Tax Limit (CTL), which is the maximum amount of real property tax that may be levied in any fiscal year. The amount of real property taxes that the Village can raise each year to finance its budget is limited by the State Constitution to 2 percent of its five-year average full property value.⁵

For 2016-17, the Village has exhausted 85.92 percent of its taxing authority, and its tax margin (the difference between the CTL and taxes subject to the limit) is \$538,193. Consequently, the Village's ability to rely on real property taxes as an increased revenue source in the future is limited. If the Village exceeds its tax limit, the State Comptroller is required to withhold State aid in an amount equal to the tax limit exceeded. We caution Village officials that if property values do not increase, the ability to increase taxes may be reduced in the future.

Further, the general fund has been loaning money to the hydroelectric fund to help subsidize its operations. As of May 31, 2016 the hydroelectric fund owed the general fund about \$222,000, and it had no cash available to repay the loan (see Hydroelectric Fund section). While General Municipal Law allows the Village to temporarily advance (loan) moneys from one fund to another, the borrowed cash must be repaid by the close of the fiscal year in which the advance was made. The use of interfund advances is a permissible form of short-term borrowing to meet current cash flow needs, but it is not intended to be used as a long-term approach to provide financial resources from one fund to another fund. If the

4 The general fund had outstanding interfund receivables (loans) from the hydroelectric fund totaling \$110,282 at the end of 2014-15 and \$222,028 at the end of 2015-16. Because the hydroelectric fund has had an ongoing deficit fund balance and was unable to pay off the loans, the Village categorized the \$222,028 interfund receivable as nonspendable fund balance in the general fund at the end of the 2015-16 fiscal year. For consistency, we recategorized the \$110,282 interfund receivable as nonspendable fund balance in the general fund for 2014-15. This adjustment reduced the unrestricted fund balance in the general fund from \$94,371 to a deficit of \$15,911 at the end of 2014-15.

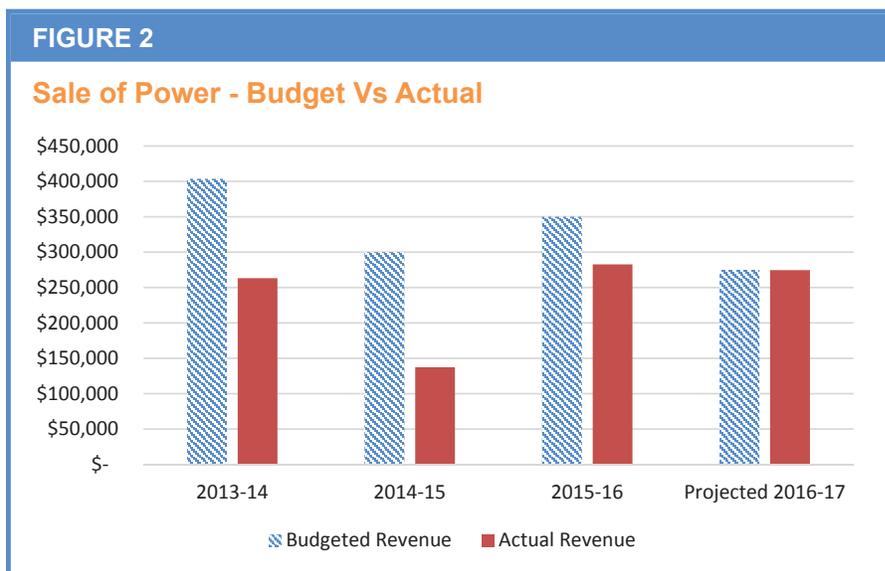
5 The State Constitution and related statutes allow for taxes in the amount of certain appropriations to be excluded when determining the amount of levy that must be below the tax limit. This tax levy amount (total levy minus exclusions) is often referred to as taxes subject to the limit.

hydroelectric fund continues to experience financial difficulty, it could further impact the general fund's financial condition.

Village officials have applied to the New York State Financial Restructuring Board for Local Governments (FRB) for advice and recommendations on solving the Village's ongoing fiscal concerns. The FRB works with fiscally eligible municipalities that have requested help and makes recommendations to improve the respective municipality's fiscal stability, management and delivery of public services. In addition, the FRB may offer grants, or loans or both to the municipality. If the municipality agrees to undertake the FRB's recommendations, it would be contractually bound to fulfill those terms to receive the aid.

Hydroelectric Fund — The Village accounts for the financial activity of two hydroelectric dams (East Dam and West Dam) in its hydroelectric fund. The primary revenue source for this fund is the sale of power. The Village had a reconstruction project of the West Dam that was ongoing for many years. Construction began in 2009 and was expected to be completed in 2010. However, due to various construction issues and problems, the project was delayed and not completed until May 2014. As a result of the project delays, the Village was not able to realize as much revenue from the sale of power as Village officials had planned. When the West Dam became operational, the East Dam broke down, requiring additional costly repairs. Revenue from the sale of power was approximately \$370,000 (35 percent) less than budgeted in the last three fiscal years combined (2013-14 through 2015-16), because the two facilities were not operating as anticipated by Village officials (Figure 2).

The Board reduced the 2016-17 budgeted revenue from the sale of power to \$275,000, which appears to be a realistic estimate based on revenues received as of December 2016 (\$160,200) and fiscal year-end projections.



In addition, the Board included a transfer of \$145,535 from the Empire Zone account to the hydroelectric fund in the 2016-17 budget and transferred the funds during the year. This left the Empire Zone account with a balance of about \$123,000 as of February 28, 2017. The moneys in this account originated from payments the Village collected pursuant to a service agreement with a company that received benefits under the New York State Empire Zone Program. Due to changes to the program, the Village has not received any payments since 2013. Therefore, this is not a recurring financing source, and the Village will not be able to continue to rely on it to finance the hydroelectric budget to the same extent in the 2017-18 budget or in future years. The Board will need to find other recurring revenues to finance operations or take other steps to make the hydroelectric fund self-sufficient. Village officials told us they are currently negotiating a contract with the New York Power Authority to study the dams, prepare a cost-benefit analysis and develop a plan to get the East Dam operating.

Sewer Fund — The sewer fund's unrestricted fund balance improved from a deficit balance of \$150,847 at the end of 2014-15 to a deficit balance of \$71,132 at the end of 2015-16. The sewer fund generated an operating surplus of about \$80,000 in 2015-16 primarily because the Board increased sewer rates by 15 percent effective August 1, 2015, and the Village spent about \$40,000 (2.5 percent) less than budgeted for the year. Based on year-to-date operating results as of February 28, 2017, it is likely that the sewer fund will generate another small operating surplus in the 2016-17 fiscal year.

At present, Village officials are working with the Village Attorney to prepare a local law to change the sewer user fees from metered only to a combination of Equivalent Dwelling Units⁶ (EDUs) and metered usage. The EDU portion of the bill will cover the sewer plant's fixed costs, such as debt payments, while the billing based on metered water usage will continue to cover the cost of personal services, employee benefits, chemicals, etc. Officials believe this will help make it easier to develop more accurate revenue estimates in the future.

Although Village officials have taken steps to improve the Village's financial condition, the Board has not developed and adopted comprehensive, written multiyear financial or capital plans. It also does not have any other mechanism in place to adequately address the Village's long-term operational needs. Such plans would provide the Board with a valuable resource to make informed financial decisions and continue its work to improve the Village's fiscal health.

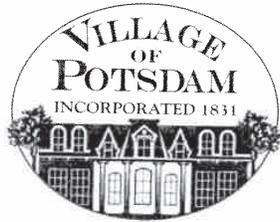
⁶ By definition, an EDU is the level of service in gallons per day for an average residential dwelling, or the typical volume of the wastewater generated by a single family home.

What Do We Recommend?

The Board should:

1. In conjunction with Village management, continue to work to eliminate the deficits in the hydroelectric and sewer funds and to increase fund balance to the levels established in the fund balance policy.
2. Ensure that the outstanding interfund loans are repaid as soon as possible.
3. Develop and adopt multiyear financial and capital plans to establish the goals and objectives for funding long-term operating and capital needs. These plans should be monitored and updated on an ongoing basis.

Appendix A: Response From Village Officials



VILLAGE OF POTSDAM

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May 15, 2017

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RE: Village of Potsdam
Financial Condition
2017M-061

Dear Ms. Wilcox:

Please consider this letter to be the Village of Potsdam's response to the preliminary draft findings for the Village of Potsdam Audit.

The Village of Potsdam's position concerning the draft findings and recommendations is that we agree with your findings and recommendations. We have taken actions to improve our financial condition and will remain vigilant. We are working to eliminate the deficit fund balance in the hydro and sewer funds and to increase the general fund's relatively low fund balance. The Board and Village staff are currently working on multiyear financial and capital plans.

Thank you for taking the time to review the Village's financial condition and to provide your valuable findings and recommendations.

Sincerely,

Reinhold J. Tischler
Mayor

Appendix B: Audit Methodology and Standards

We conducted this audit 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. To achieve the audit objective and obtain valid audit evidence, we performed the following audit procedures:

- We reviewed the Village's policies and procedures relevant to financial and budgeting activities. We interviewed Village officials to determine what processes were in place and to gain an understanding of the Village's financial situation and budget.
- We reviewed the Village's externally audited financial statements, budget reports and balance sheets as of May 31, 2016.
- We analyzed revenue and expenditure trends, budget-to-actual comparisons and fund balance levels for fiscal years 2013-14 through 2015-16 for all the operating funds to evaluate financial condition. We also analyzed revenue and expenditure trends and budget-to-actual comparisons for 2016-17 through November 30, 2016 to gain an understanding of the Village's current financial condition. We extended our review of certain revenues and expenditures through February 28, 2017.

We conducted this performance audit in accordance with GAGAS, generally accepted government auditing standards. 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.

A written corrective action plan (CAP) that addresses the findings and recommendations in this report should be prepared and provided to our office within 90 days, pursuant to Section 35 of General Municipal Law. For more information on preparing and filing your CAP, please refer to our brochure, Responding to an OSC Audit Report, which you received with the draft audit report. We encourage the Board to make the CAP available for public review in the Clerk's office.

Appendix C: Resources and Services

Regional Office Directory

www.osc.state.ny.us/localgov/regional_directory.pdf

Cost-Saving Ideas – Resources, advice and assistance on cost-saving ideas

www.osc.state.ny.us/localgov/costsavings/index.htm

Fiscal Stress Monitoring – Resources for local government officials experiencing fiscal problems

www.osc.state.ny.us/localgov/fiscalmonitoring/index.htm

Local Government Management Guides – Series of publications that include technical information and suggested practices for local government management

www.osc.state.ny.us/localgov/pubs/listacctg.htm#lmgm

Planning and Budgeting Guides – Resources for developing multiyear financial, capital, strategic and other plans

www.osc.state.ny.us/localgov/planbudget/index.htm

Protecting Sensitive Data and Other Local Government Assets – A non-technical cybersecurity guide for local government leaders

www.osc.state.ny.us/localgov/lgli/pdf/cybersecurityguide.pdf

Required Reporting – Information and resources for reports and forms that are filed with the Office of the State Comptroller

www.osc.state.ny.us/localgov/finreporting/index.htm

Research Reports / Publications – Reports on major policy issues facing local governments and State policy-makers

www.osc.state.ny.us/localgov/researchpubs/index.htm

Training – Resources for local government officials on in-person and online training opportunities on a wide range of topics

www.osc.state.ny.us/localgov/academy/index.htm

Contact

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