



Town of Horseheads

Financial Management

Report of Examination

Period Covered:

January 1, 2012 – July 30, 2015

2015M-211



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

December 2015

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 Horseheads, entitled Financial Management. 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 Horseheads (Town) is located in Chemung County (County). The Town includes the Village of Horseheads (Village) within its boundary and serves approximately 19,500 residents. The Town provides services for its residents, including highway maintenance, snow removal, street lighting and general government support. The Town's budgeted appropriations for 2015 for the town-wide (TW) general, town-outside-village (TOV) general and TOV highway funds total \$5.5 million, which are funded primarily with sales tax and State aid. The TW fund encompasses the entire Town, including the Village. The TOV funds encompass only the portion of the Town that lies outside of the Village.

The Town is governed by an elected Town Board (Board), which is composed of four Board members and a Supervisor. The Board is responsible for the general management and control of the Town's financial affairs. The Supervisor serves as the Town's chief fiscal officer and is responsible for receiving, disbursing and maintaining custody of Town money, maintaining accounting records and providing financial reports to the Board. The Supervisor employs a bookkeeper to assist with these duties. The Supervisor also serves as the Town's budget officer.

Objective

The objective of our audit was to review the Town's financial operations. Our audit addressed the following related question:

- Did Town officials ensure the Town was fiscally stable?

Scope and Methodology

We examined the Town's financial management for the period January 1, 2012 through July 30, 2015. 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. Unless otherwise indicated in this report, samples for testing were selected based on professional judgment, as it was not the intent to project the results onto the entire population. Where applicable, information is presented concerning the value and/or size of the relevant population and the sample selected for examination.

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 A, have been considered in preparing this report. Town 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 Clerk's office.

Financial Management

The Board is responsible for the Town's financial oversight. To ensure the Town is fiscally stable, the Board must adopt structurally balanced budgets for all operating funds that provide sufficient revenues to finance recurring expenditures, while providing desired services on a continuing basis. An important aspect of budget preparation is estimating the amount of fund balance that will be available at year-end. Monitoring the budget against actual results of operations during the year is also a critical part of the Board's budgeting responsibilities. In addition, Town officials should develop multiyear financial and capital plans to address revenue and expenditure trends, reserve funds and capital assets and set long-term priorities and goals. Sound budgeting practices and multiyear plans help ensure that sufficient funding will be available to finance current and long-term obligations and address unexpected occurrences.

The Town has historically experienced a strong financial position due in part to the sales tax revenues it receives from the County. The Supervisor and Board have not focused on developing budgets that mirror the actual results of Town operations because the revenues, in particular sales tax, were always abundant. As a result, the Town has not levied a Town real property tax in over 20 years. However, in recent years the Town has relied on appropriating fund balance to continue operating without a tax levy. Such a strategy of meeting recurring expenditures with a one-shot financing source like fund balance cannot be continued indefinitely. This strategy will be further tested in the future by the County's decision to modify its sales tax sharing agreement, which will reduce the amount of sales tax revenue the Town will receive, thus placing new revenue constraints on Town operations.¹ The change in the Town's fiscal environment had an immediate impact on the TW funds which have seen an 82 percent decline in fund balance over the last three years. While the TOV funds still have substantial resources, their continued fiscal health is still at risk because of the Board's decision to replace declining sales tax revenue with fund balance. The Board has not developed multiyear financial plans to address the use of fund balance to finance operations, the continued reduction of sales tax revenues, establishing reserve funds or purchasing and financing future capital assets.

Budgeting and Fund Balance

It is essential the Board adopt structurally balanced realistic annual budgets in which recurring revenues finance recurring expenditures and reasonable levels of fund balance are maintained. An appropriation of fund balance is the use of unexpended resources from prior years

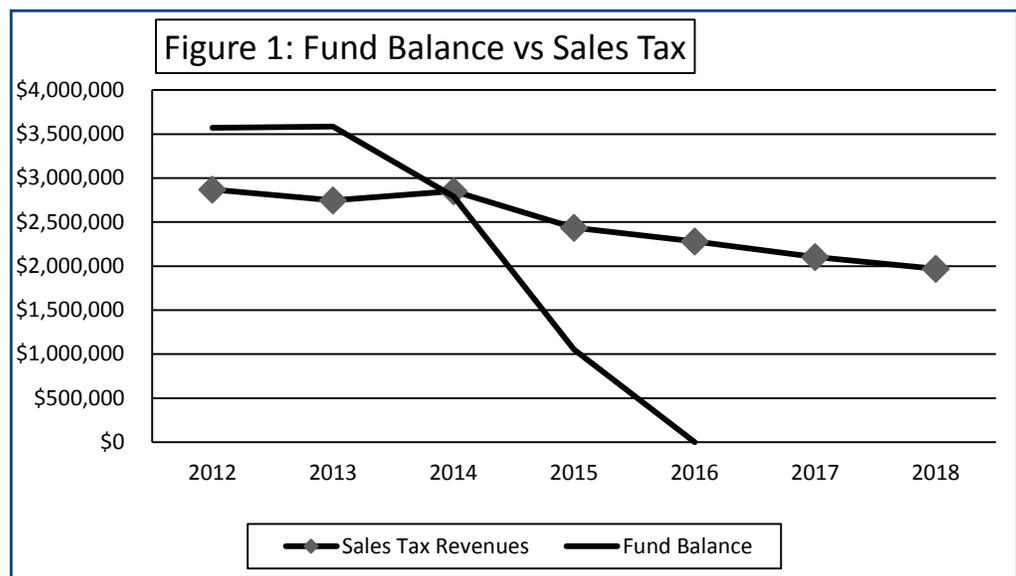
¹ The modified sales tax agreement was scheduled to begin in 2014 but Town officials told us it was delayed until 2015.

to finance current year appropriations and is considered a one-time financing source. This is an acceptable and reasonable budget practice when the Town has accumulated an adequate level of unrestricted fund balance. However, it is not a sustainable source of funding and will start to impact cash flow and then financial condition if a reasonable cushion is not maintained.

The Town has historically maintained a strong and healthy financial position. The Supervisor told us the Town has not levied real property taxes in at least 28 years. Due to the Town’s fiscal health and the fact that the Town’s sales tax revenues were always more than sufficient to fund its operations, the Board has not developed procedures or financial plans to monitor Town finances, including its budget practices. As a result, the Board continually adopted budgets that overestimated appropriations. In addition, the Board appropriated fund balance it didn’t have available to finance TW operations and did not use appropriated fund balance as planned for either the TW or TOV funds.

Because of the change in the County sales tax sharing agreement scheduled to take effect in 2014, the Board entered into various shared service agreements to reduce expenditures and used fund balance to fill the revenue gap and meet capital needs. Although the Board took these proactive measures, continued reliance on fund balance is not sustainable, especially considering that the County forecasted the Town’s sales tax revenues will drop from \$2.85 million in 2014 to \$2 million by 2018. If the Town uses all of the fund balance it has appropriated in 2015 and continues similar budgeting and usage practices in 2016, it will eliminate its fund balance within the next two years.

Figure 1 illustrates the downward trends for these two financing sources.



TW General Fund— From 2012 through 2014, there was a significant decline in TW general fund balance. The decline totaled \$915,944 with \$197,015 remaining as of December 31, 2014. The amount of unrestricted fund balance available was \$173,320, which was substantially less than the \$660,390 appropriated to finance the 2015 budget, leaving the fund with a \$487,070 budgetary deficit.²

This was not a one-time error. The Board also adopted budgets for 2013 and 2014 that appropriated fund balance that exceeded the amounts available to finance operations. In addition, the Board significantly overestimated appropriations by almost \$2 million during the three year period. Although the errors in estimating appropriations tended to partially offset the errors in estimating available fund balance, they were not enough to prevent the financial decline of the TW general fund.

Figure 2 summarizes the effect of the Board’s poor budgeting on the general fund balance.

Figure 2: TW General Fund Budget-to-Actual Comparison and Operating Results				
	2012	2013	2014	Total
Budgeted Revenues	\$1,785,400	\$1,863,200	\$1,757,000	\$5,405,600
Actual Revenues	\$1,741,762	\$1,895,858	\$1,927,659	\$5,565,279
Variance	(\$43,638)	\$32,658	\$170,659	\$159,679
Actual as a Percentage of Budget	98%	102%	110%	103%
Appropriations	\$2,961,440	\$2,902,055	\$2,587,800	\$8,451,295
Expenditures	\$2,362,754	\$2,105,242	\$2,013,227	\$6,481,223
Variance	\$598,686	\$796,813	\$574,573	\$1,970,072
Actual as a Percentage of Budget	80%	73%	78%	77%
Total Budget Variance	\$642,324	\$829,471	\$745,232	\$2,217,027
Operating Surplus/(Deficit) ^a	(\$620,992)	(\$209,384)	(\$85,568)	(\$915,944)
Beginning Fund Balance	\$1,112,959	\$491,967	\$282,583	
Ending Fund Balance	\$491,967	\$282,583	\$197,015	
Less: Nonspendable Fund Balance	\$28,002	\$4,782	\$23,695	
Budgeted Fund Balance Appropriation	\$1,038,855	\$830,800	\$660,390	
Allowable Fund Balance Appropriation	\$463,965	\$277,801	\$173,320	
Budgetary Deficit for Ensuing Year	\$574,890	\$552,999	\$487,070	

^a Actual revenues less expenditures

The Board continued its ineffective budgeting practices when adopting the 2015 budget by again appropriating unavailable fund balance and overestimating appropriations. Therefore, to prevent the TW general fund from ending the current year in a deficit position, the Board needs to monitor budget-to-actual results in a close and timely manner. Additional reductions in expenditures and alternative revenues may be needed.

² The budgetary deficit was 24 percent of actual 2014 expenditures.

TOV Funds — Historically, the TOV ending fund balances have been excessively high as a percentage of expenditures.³ These excessive balances were caused by the Board estimating appropriations at unreasonable amounts for two of the last three years.

When fund balances are in excess of needs, it can be prudent to use the fund balances to finance one-shot expenditures, such as debt reduction, capital improvements or special projects, or to help cover one-time budget shortfalls. The Board took a reasonable step in 2014 by appropriating fund balance to finance a capital improvement for a new truck wash bay that was required. This resulted in the TOV funds experiencing their first operating deficit, \$708,001, and reduction of fund balance in years.⁴

Figure 3 illustrates the result of the Board’s budgeting practices over the past three years.

Figure 3: TOV Funds Budget-to-Actual Comparison and Operating Results				
	2012	2013	2014	Total
Budgeted Revenues	\$2,097,700	\$2,217,700	\$2,545,200	\$6,860,600
Actual Revenues	\$1,996,066	\$2,042,538	\$2,415,706	\$6,454,310
Variance	(\$101,634)	(\$175,162)	(\$129,494)	(\$406,290)
Actual as a percentage of Budget	95%	92%	95%	94%
Appropriations	\$2,448,610	\$3,027,380	\$3,028,640	\$8,504,630
Expenditures	\$1,713,408	\$1,818,489	\$3,123,707	\$6,655,604
Variance	\$735,202	\$1,208,891	(\$95,067)	\$1,849,026
Actual as a percentage of Budget	70%	60%	103%	78%
Total Budget Variance	\$836,836	\$1,384,053	\$224,561	\$2,445,450
Operating Surplus/(Deficit) ^a	\$282,658	\$224,049	(\$708,001)	(\$201,294)
Beginning Fund Balance	\$2,795,898	\$3,078,556	\$3,302,605	
Ending Fund Balance	\$3,078,556	\$3,302,605	\$2,594,604	
Less: Nonspendable and Restricted Fund Balance	\$12,721	\$0	\$15,675	
Less: Assigned Unappropriated Fund Balance	\$2,256,155	\$2,819,165	\$1,499,055	
Budgeted Fund Balance Appropriation	\$809,680	\$483,440	\$1,079,875	
Allowable Fund Balance Appropriation	\$3,065,835	\$3,402,105 ^b	\$2,578,929	
^a Actual revenues less expenditures. ^b Allowable fund balance appropriation is higher than ending fund balance because the Board appropriated a deficit fund balance amount of (\$99,500) in the TOV Highway fund to reduce revenues. This practice is not allowed.				

While fund balance remained substantial at the end of 2014, the Board appropriated an additional \$1,079,875 to finance 2015 expenditures to offset the decline in sales tax revenue as previously discussed. We reviewed the 2015 budget and operations through the end of our field

³ Ending fund balances were 179 percent of 2012 expenditures, 182 percent of 2013 expenditures and 83 percent of 2014 expenditures.

⁴ The Town had significant resources in the TOV funds at this time; therefore, this was considered to be a reasonable use of resources. However, with the future reduction in sales tax revenues, Town officials will need to be more careful with their spending.

work and found that the Town will likely need to use most or all of the amount appropriated for 2015. The continued use of fund balance to make up the structural differences between declining sales tax revenue and recurring expenditures cannot be repeated beyond 2016 at the present rate of use.⁵

The Board has taken steps to improve the accuracy of, and bring structural balance to, its budgets. For example, the Supervisor and a Board member told us that, although they like to budget conservatively, the Board members are reducing the built-in cushions (overestimated appropriations) in the budgets. They also chose not to fill one position that opened when an employee retired. The Supervisor also requested that each department reduce its appropriations by 10 to 15 percent for 2016. To provide additional savings, the Board is exploring additional shared services⁶ with surrounding municipalities.

Finally, although the Board received monthly budget-to-actual reports, budget modifications were not made in a timely manner. The Supervisor told us the Board made all budget modifications at year-end because it was easier to do them all at once rather than a couple each month. This improper practice defeats the purpose of the New York State Town Law prohibition on expenditures exceeding appropriations. The law seeks to assure that resources are available for expenditures. As resources become scarcer, due to declining fund balance and sales tax revenues, this practice carries more risk, especially because the Supervisor stated the Board would like to continue to operate without instituting a real property tax. To make such a goal realistic without exhausting fund balance, the Town will require additional cuts in expenditures, accurate budgeting, close monitoring of actual results and a multiyear financial plan.

Multiyear Financial Planning

Town officials can use multiyear financial planning to improve the budget development process. It is important to develop comprehensive multiyear financial and capital plans to estimate the future costs of ongoing services and capital needs. Effective multiyear plans project operating and capital needs and financing sources over a three- to five-year period. Such plans enable Town officials to identify revenue and expenditure trends, set long-term priorities and goals, consider the impact of near-term budgeting decisions on future fiscal years and avoid large fluctuations in tax rates.

⁵ Between both the TW and TOV funds. The TW funds will require a higher allocation of the sales tax revenues in the future, thus reducing the revenues to the TOV funds, making it more likely that the TOV funds will use the appropriated fund balance.

⁶ The Town is negotiating to share the following services with other municipalities: code enforcement, assessing and animal control. The Town previously shared assessing with another municipality but that agreement was terminated in February 2015.

Multiyear plans also allow Town officials to assess the effect and merits of alternative approaches to address financial issues, such as financing operations with fund balance, accumulating money in reserve funds or purchasing and financing capital assets. Long-term financial plans work in conjunction with Board-adopted policies and procedures to provide guidance to employees on the financial priorities and goals set by the Board. Any long-term financial plan must be monitored and updated on a continuing basis to provide a reliable framework for preparing budgets and ensure that information used to guide decisions is current and accurate.⁷

Although the Board is aware of the financial constraints the Town will continue to face due to the progressive reduction in sales tax revenue and has begun to take measures to address this loss, it has not developed written multiyear financial or capital plans. Formalizing its goals and actions will allow it to determine if the plan will sufficiently offset the Town's lost revenues while maintaining the desired level of services. In addition, the formalized plans will allow the Board to easily make adjustments as needed. Without such plans, the Board's ability to effectively manage the Town's finances is inhibited.

Recommendations

The Board should:

1. Adopt adequate procedures or financial plans to effectively monitor Town finances, including those governing its budget practices.
2. Adopt structurally sound budgets that include realistic estimates of revenues, appropriations and fund balance.
3. Monitor the budget-to-actual results throughout the year and make timely adjustments or modifications as necessary.
4. Develop comprehensive multiyear financial and capital plans to establish long-term objectives for funding long-term needs. Any long-term financial plan must be monitored and updated on a continuing basis.
5. Continue to evaluate and explore cost saving measures or revenue enhancements to help offset the Town's loss of sales tax revenues.

⁷ For guidance on preparing multiyear plans, Town officials should refer to the OSC publications entitled *Multiyear Financial Planning* and *Multiyear Capital Planning* available at <http://www.osc.state.ny.us/localgov/pubs/listacctg.htm#lmgg>.

APPENDIX A
RESPONSE FROM LOCAL OFFICIALS

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



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November 25, 2015

Edward V. Grant, Jr., Chief Examiner
The Powers Building - 16 W. Main St. - Suite 522
Rochester, NY 14614-1608

AUDIT RESPONSE

We have reviewed the Town of Horseheads Financial Management – Report of Examination for the period of July 1, 2012 – July 30, 2015 as prepared by the Office of the State Comptroller.

We concur with the overall examination report and the recommendations outlined in the report.

However, we would like to clarify the comments related to the budgeting process.

The reports indicate that the Town Officers and Town Supervisor have not used the budgeting process appropriately to manage the town's finances. We have and will continue to use the budgeting process to ensure the fiscal stability of the Town of Horseheads. The Town's future revenues from sales tax will be reduced per a plan implemented by Chemung County and we do not currently have a real property tax. Therefore, we are committed to refining our budget process to incorporate this reduction of revenue and to project expenses. Likewise, we will monitor the monthly budget variances and make the appropriate adjustments on a timely basis. The Town Board and Supervisor's goal is to continue to keep the town debt free and without a real property tax.

The excess expenditures were directly related to the Town's decision to repave additional roads due to the price of the materials available from the subcontractor performing the work. In addition to this, the town built a new truck wash and continues to spend funds on Koppers Pond. Both of these projects were mandated by the government.

In summary, we believe the Town of Horseheads is being prudently managed by the Town Board and Town Supervisor and will incorporate the recommendation outlined in the report to improve our performance. The Town of Horseheads has an excellent reputation in Chemung County for the services provided to our residents and we plan to maintain and enhance that reputation.

Michael W. Edwards, Supervisor

Town of Horseheads

APPENDIX B

AUDIT METHODOLOGY AND STANDARDS

To achieve our audit objective and obtain valid audit evidence, we performed the following audit procedures:

- We reviewed Board minutes to assess the Town's control environment, including oversight of financial operations.
- We interviewed Town officials to gain an understanding of financial operations and the budgeting process.
- We reviewed budgets, budget-to-actual reports and interfund transfer schedules to assess the Town's current and future financial position and prior-year trends.
- We reviewed the Town's adopted budgets for 2012 through 2015 to determine the amount of fund balance appropriated.
- We reviewed the Town's budget-to-actual variances for 2012 through 2015 to determine if the variances were significant.
- We compared the Town's records to its audited financial statements.
- We reviewed the OSC publication entitled *Local Government Sales Taxes in New York State: 2015 Update*.

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.

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