



Village of Cuba Sewer Fund Financial Condition and Records and Reports

Report of Examination

Period Covered:

June 1, 2011 — October 31, 2012

2013M-15



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

March 2013

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 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 Cuba, entitled Sewer Fund Financial Condition and Records and Reports. 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 Village of Cuba (Village) is located in Allegany County and has a population of 1,575. For the fiscal year ending May 31, 2013, budgeted appropriations totaled \$784,000 for the general fund, \$205,000 for the water fund, and \$282,000 for the sewer fund. Expenditures are funded primarily by real property taxes, sales taxes, State aid and user fees. The Village is governed by an elected Board of Trustees (Board) consisting of a Mayor and four Trustees who are responsible for the general oversight of Village operations. The appointed Clerk-Treasurer is the chief financial officer and is responsible for the custody of all Village moneys and maintaining the accounting records, as well as preparing reports and the annual operating budget for Board approval and adoption.

Scope and Objectives

The objectives of our audit were to review the financial condition of the sewer fund and the internal controls over financial records and reports for the period June 1, 2011, through October 31, 2012. We extended our review of the sewer fund back to June 1, 2007. Our audit addressed the following related questions:

- Did the Board adopt structurally balanced budgets for the sewer fund that provided sufficient recurring revenues to finance recurring expenditures?
- Did the Village prepare and maintain adequate financial records and reports?

Audit Results

The Board did not adopt budgets for the sewer fund that provided sufficient revenues to finance expenditures, because revenues were consistently overestimated. As a result, the sewer fund balance has declined dramatically from approximately \$20,000 as of May 31, 2008 to a fund deficit of approximately (\$54,000) as of May 31, 2012. To compensate for the lack of sufficient revenues, the sewer fund borrowed \$40,000 from other funds, which has not been repaid, and improperly used \$30,000 from a repair reserve.

We found that the Clerk-Treasurer did not maintain the Village's accounting records in a complete and accurate manner. Specifically, we found that cash, accounts receivable and accounts payable were misstated, which resulted in the operating funds' fiscal health appearing to be more favorable. In addition, the Treasurer does not provide, and the Board does not request, monthly reports that would provide essential information such as each fund's budget-to-actual activity and cash position, significantly diminishing the Board's ability to monitor and manage the Village's financial resources.

Had the Board requested this information, it may have noted that cash balances exceeded reconciled bank balances. Furthermore, the Board did not ensure that the annual report was filed with our Office within 60 days of fiscal year end, as required. The Village hired an independent accounting firm to perform an audit and compile the information for the Clerk-Treasurer to file the annual report. However, as of January 16, 2013, the annual report for the 2011-12 fiscal year had not been filed, which is more than five months late.

Comments of Local Officials

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 that they have initiated or plan to initiate corrective action.

Introduction

Background

The Village of Cuba (Village) is located in Allegany County in the western part of New York State and has a population of 1,575. The Village provides various services to its residents including street maintenance, snow removal, water distribution, sewage collection, garbage collection and general government administration. For the fiscal year ending May 31, 2013, budgeted appropriations totaled \$784,000 for the general fund, \$205,000 for the water fund, and \$282,000 for the sewer fund. Expenditures are funded primarily by real property taxes, sales taxes, State aid and user fees.

The Village is governed by an elected Board of Trustees (Board) consisting of a Mayor and four Trustees who are responsible for the general oversight of Village operations. The Mayor is the chief executive officer of the Village and is responsible for, among other duties, appointing the Village Clerk-Treasurer, subject to the approval of the Board. The Clerk-Treasurer is the chief financial officer and is responsible for the custody and care of all Village moneys and maintaining the accounting records, as well as preparing reports and the annual operating budget for Board approval and adoption.

Objectives

The objectives of our audit were to review the financial condition of the sewer fund and the internal controls over financial records and reports. Our audit addressed the following related questions:

- Did the Board adopt structurally balanced budgets for the sewer fund that provided sufficient recurring revenues to finance recurring expenditures?
- Did the Village prepare and maintain adequate financial records and reports?

Scope and Methodology

We evaluated the financial condition of the sewer fund and the records and reports of the Village for the period June 1, 2011, through October 31, 2012. We extended our review of the sewer fund back to June 1, 2007.

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 that they have initiated or 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 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-Treasurer's office.

Sewer Fund Financial Condition

The Board is responsible for adopting structurally balanced budgets for all operating funds that provide for sufficient recurring revenues to finance recurring expenditures. The annual budget for each fund is expected to provide a reasonable estimate of appropriations, revenues, and other financing sources. Additionally, current billing rates should be reviewed to determine if they will generate the level of revenue estimated in the budget. Sound budgeting practices, together with prudent fund balance management, ensure that sufficient funding will be available to sustain operations, address unexpected occurrences, and satisfy long-term obligations or future expenditures.

The Board did not adopt budgets for the sewer fund that provided sufficient revenues to finance expenditures, because revenues were consistently overestimated. As a result, the sewer fund balance has declined dramatically from approximately \$20,000 as of May 31, 2008¹ to a fund deficit of approximately (\$54,000) as of May 31, 2012. To compensate for the lack of revenues, the sewer fund borrowed \$40,000 from other funds, which have not been repaid, and improperly used \$30,000 from a repair reserve. While cash balances in the Village's other operating funds appear to be adequate, their operations could become affected in the event the sewer fund continues to be unable to repay the interfund loans.

We found that the Board did not use historical data when estimating revenues and analyzing rates for the sewer fund. According to the Clerk-Treasurer, after the Board had made decisions on expected expenditure levels for the following fiscal year, she would simply adjust the budgeted revenues as needed to balance the budget. Even though the Clerk-Treasurer indicated several times that current sewer rates were not adequate to cover treatment costs, the Board did not periodically review rates and make adjustments to help ensure revenues were sufficient to cover costs. Although the Board increased rates in 2010, it must continue to routinely monitor the adequacy of sewer rates to fund recurring expenditures. The failure to review sewer rates and make adjustments as needed, coupled with inadequate budgeting practices, has led to several years of revenue shortfalls and operating deficits as illustrated in Tables 1 and 2:

¹ The fiscal year of the Village is June 1st through May 31st.

Table 1: Revenue Shortfalls					
	2007-08	2008-09	2009-10	2010-11	2011-12
Budgeted Revenues	\$265,091	\$262,326	\$269,082	\$262,859	\$271,588
Reported Revenues	\$211,932	\$206,968	\$226,490	\$253,653 ^a	\$251,255
Shortfall	(\$53,159)	(\$55,358)	(\$42,592)	(\$9,206)	(\$20,333)

^a Revenues received in the 2010-11 fiscal year and thereafter will be increased as a result of the newly established Cuba Lake Sewer District in the Town of Cuba, which sends its sewage to the Village for treatment.

Table 2: Operating Results					
	2007-08	2008-09	2009-10	2010-11	2011-12
Reported Revenues	\$211,932	\$206,968	\$226,490	\$253,653	\$251,225
Reported Expenditures	\$267,835	\$245,233	\$231,134	\$258,754	\$239,177
Operating Surplus/ (Deficit)	(\$55,903)	(\$38,265)	(\$4,644)	(\$5,101)	\$12,048 ^a

^a According to the Clerk-Treasurer, spending was closely monitored to eliminate any non-critical expenditures.

The operating deficits caused reported fund deficits for the fiscal years 2008-09 through 2011-12, with the Village's records showing a fund deficit of (\$24,032) as of May 31, 2012. However, due to the condition of the accounting records (see related finding entitled Records and Reports), we analyzed the sewer fund's balance sheet accounts as of May 31, 2012 and found that the accumulated fund deficit was approximately (\$54,000),² or more than \$30,000 greater than the deficit in the accounting records.

To compensate for the decrease in cash flow due to the lack of sufficient sewer revenues, we found that the Clerk-Treasurer improperly used approximately \$30,000³ in cash from an \$80,000 repair reserve,⁴ which was commingled in the sewer operating checking account. Further, the Board approved interfund loans from other operating funds to the sewer fund totaling approximately \$40,000. Statute requires that such interfund loans be repaid by the end of the fiscal year. However, these loans have been outstanding since at least May 31, 2010.

While the Board, according to the Clerk-Treasurer, has been continually made aware of the poor financial condition of the sewer fund, it has failed to adequately address the annual operating deficits and the accumulated fund deficit. As a result, sewer operations and the

² Unreserved fund balance as of May 31, 2008 of approximately \$20,000 less net operating deficits through May 31, 2012 of approximately \$36,000 less net overstated assets as of May 31, 2012 of approximately \$38,000 (see Tables 3, 4 and 5).

³ Sewer repair reserve cash of \$80,000 less our calculation of total sewer fund cash of \$49,736 as of May 31, 2012.

⁴ Although a Board resolution establishing the reserve could not be provided for our review, the Village has reported a sewer repair reserve since May 31, 2001, which was reported as having \$80,000 in it since May 31, 2005.

funding of repairs may be impacted. While the cash balances in the Village's other operating funds appear to be adequate, their operations could become affected in the event the sewer fund continues to be unable to repay the interfund loans.

Recommendations

1. The Board should adopt budgets with reasonable estimates for revenues, based on historical information.
2. The Board should periodically review and adjust sewer rates as needed to fund recurring operating expenditures.
3. The Board should develop a plan to address the sewer fund deficit, replenish the repair reserve and repay outstanding interfund loans.

Records and Reports

The Clerk-Treasurer, as chief fiscal officer, is responsible for maintaining up-to-date, accurate and detailed accounting records, and for providing adequate monthly financial reports to the Board. The Board is responsible for the fiscal oversight of the Clerk-Treasurer, which includes ensuring that she files the annual financial report with the Office of the State Comptroller (OSC) in a timely manner, and performing, or causing to be performed, an annual audit of her records.

Accounting Records – The Clerk-Treasurer’s records should provide accurate information for the Mayor and Board to manage the Village and monitor its financial operations. Accordingly, general ledgers, cash receipt and disbursement journals, and revenue and expenditure subsidiary ledgers must be maintained in a complete, accurate and timely manner.

We found that the Clerk-Treasurer did not maintain the Village’s accounting records in a complete and accurate manner. For example, the Treasurer did not ensure that account balances for cash, accounts receivable and accounts payable were accurate and supported. We analyzed the balance sheet accounts for the three operating funds and found significant discrepancies as detailed in Tables 3, 4, and 5:

Table 3: Cash as of May 31, 2012			
Fund	Village Trial Balance	OSC Calculated^a	Variance
General	\$511,229	\$437,090	\$74,139
Water	\$128,498	\$125,052	\$3,446
Sewer	\$65,745	\$49,736	\$16,009
Totals	\$705,472	\$611,878	\$93,594

^a Using bank statements, canceled checks and certificates of deposit

Table 4: Accounts Receivable^a as of May 31, 2012			
Fund	Village Trial Balance	OSC Calculated^b	Variance
Water	\$48,896	\$10,193	\$38,703
Sewer	\$52,443	\$13,435	\$39,008
Totals	\$101,339	\$23,628	\$77,711

^a Village officials process quarterly combined bills for water and sewer rents. Sewer rents are based on a percentage of water usage. No general fund receivables were recorded, nor did we identify any during our testing.
^b Using billing registers and collection deposits

Table 5: Accounts Payable as of May 31, 2012			
Fund	Village Trial Balance	OSC Calculated^a	Variance
General	\$170,428	\$8,324	\$162,104
Water	\$ 4,498	\$1,040	\$3,458
Sewer	\$18,221	\$1,062	\$17,159
Totals	\$193,147	\$10,426	\$182,721
^a The Clerk-Treasurer could not provide a detailed list of accounts payable as of May 31, 2012. We used canceled checks and expenditure subsidiary ledger account postings.			

The Clerk-Treasurer attributed these substantial discrepancies to previous fiscal years' adjusting entries that she did not process correctly. She indicated that, while attempting to make the entries provided by the Village's independent accounting firm, she didn't completely understand all of them, and made the entries incorrectly as a result. She requested the assistance of the independent accounting firm to correct the entries but a meeting has not yet been scheduled.

Financial Reports – The Clerk-Treasurer should prepare and provide the Board with monthly financial reports so it can properly manage Village finances. These reports, at a minimum, should include budget-to-actual results, cash balances and cash flow projections by fund. The budget-to-actual results would assist the Board in monitoring account balances, so that timely action could be taken when revenues are not meeting projections or appropriation accounts are almost exhausted.

We found that the Clerk-Treasurer does not provide, and the Board does not request, appropriate monthly reports. Currently the Clerk-Treasurer only provides Board members with quarterly income and expense reports comparing budget-to-actual revenues and expenditures. Moreover, we found that, as of December 31, 2012, the last such report to the Board was presented in July 2012 for May 2012 year-end activity. As a result, the Board's ability to monitor and manage the Village's financial resources is significantly diminished.

Annual Report – Local governments are required to annually complete and file with OSC a detailed report of all financial activity for the preceding year, no later than 60 days after the close of the fiscal year.

We found that the Board did not ensure the annual report was filed within the established time limit. The Village currently retains the services of an independent accounting firm to compile the information needed to file the report. This same firm was contracted to perform an audit of the Village for the year ending May 31, 2012. As of January 16, 2013, the annual report for the 2011-12 fiscal year had not been filed with OSC and is more than five months late. The Clerk-Treasurer

stated that, even though she had made multiple requests for the information, the firm indicated that, due to an increased workload, it had not finished compiling the information for her to file the annual report.

Board members did not receive and review necessary financial reports because they had not established policies to address the frequency and content of interim financial reporting. Had they received adequate reports, they may have identified the unauthorized use of reserve funds and the amount of interfund loans to the sewer fund needed to sustain its operations.⁵ Additionally, had Board members requested this information, they may have noted that general ledger cash balances were not supported by reconciled bank account balances. While the cash balances in the general and water fund appear to be adequate, we believe the combination of errors in the accounting records and the lack of adequate monthly and annual financial reports may significantly impact sewer fund operations on an ongoing basis.

Recommendations

4. The Clerk-Treasurer should ensure that the Village's accounting records are complete and accurate and are based on adequate supporting information. The Board should adopt procedures to periodically verify the accuracy of the financial reports received.
5. The Board should require the Clerk-Treasurer to provide Board member with monthly reports that provide budget-to-actual results, cash balances and cash flow projections by fund.
6. The Board should ensure the annual report is filed in a timely manner by the Clerk-Treasurer.

⁵ See related finding entitled Sewer Fund Financial Condition

APPENDIX A

RESPONSE FROM LOCAL OFFICIALS

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

CUBA VILLAGE

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March 19, 2013

Office of the State Comptroller
Division of Local Government
Robert Meller, Chief Examiner
Buffalo Regional Office
295 Main Street, Suite 1032
Buffalo, New York 14203-2510

Dear Mr. Meller;

I, Thomas Taylor, Mayor, Village of Cuba am writing a response to the Report of Examination for the period of June 1, 2011 through October 31, 2012.

First off I would like to say that the audit both oral and written has been useful and informative. Your representative, [REDACTED] was helpful and pleasant in his explanations and working with our Clerk/Treasurer Diane Wilson.

This audit of the Villages' Sewer Fund has reinforced the need for changes in this fund and more of a watchful eye by the Board of Trustees. Actions have already taken place and other will take time. Please note what was discussed at the exit conference was taken seriously and our Corrective Action Plan will reveal this.

Sincerely,

Thomas Taylor, Mayor
Village of Cuba

Cc Board of Trustees
Clerk/Treasurer

EQUAL OPPORTUNITY EMPLOYER

APPENDIX B

AUDIT METHODOLOGY AND STANDARDS

Our overall goal was to assess the adequacy of the internal controls put in place by 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 and procedures manuals, 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 for further review the financial condition of the sewer fund and financial records and reports.

For the financial condition of the sewer fund, we performed the following procedures:

- We interviewed Village officials responsible for budgeting to obtain an understanding of the Village's policies and procedures for estimating budgeted amounts and monitoring the budget against actual operations.
- We reviewed budget status reports and annual financial reports for the sewer fund to determine its financial condition and any trends.
- We reviewed the sewer fund's use of cash from reserves and interfund loans.
- We reviewed quarterly sewer bills to determine if approved rates were billed.
- We compared a sample of sewer collection reports and deposit compositions to determine if receipts were recorded and deposited timely and intact.
- We reviewed all sewer fund canceled checks to determine if any unauthorized payments were made to the Clerk-Treasurer.

For financial records and reports, we performed the following procedures:

- We interviewed Village officials responsible for financial oversight and maintaining accounting records, and reviewed Board minutes to obtain an understanding of the Village's policies and procedures.
- We reviewed bank reconciliations and significant general ledger accounts from the May 31, 2012, trial balance for accuracy.
- We interviewed the Clerk-Treasurer to determine the cause of the inaccurate trial balance amounts and the untimeliness of the annual report filing.

- We assessed the financial information provided to the Board and the Board's procedures to provide oversight of Village finances.
- We reviewed annual financial reports filed with the Office of the State Comptroller to determine if they were accurate and timely.

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

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