



# Town of Chautauqua

## Fiscal Stress

### Report of Examination

Period Covered:

January 1, 2012 — July 16, 2013

2013M-220



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**

September 2013

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 Chautauqua, entitled Fiscal Stress. 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 Town of Chautauqua is located in Chautauqua County, is approximately 73 square miles in size, and serves about 4,460 residents. The elected five-member Town Board (Board) is the legislative body responsible for managing Town operations, including establishing internal controls over financial operations and for maintaining sound financial condition. The Town Supervisor (Supervisor) is a member of the Board and serves as the chief executive officer. The Supervisor is also the chief fiscal officer and is responsible for the receipt, disbursement, and custody of Town moneys; maintaining accounting records; and providing financial reports. Although the Board is primarily responsible for the effectiveness and proper functioning of internal controls, the Supervisor and department heads share this responsibility.

The Town's general fund budgeted appropriations for the 2013 fiscal year were approximately \$1.3 million, funded primarily with real property taxes, sales tax, and State aid. The Town provides services for its residents including highway maintenance, snow removal, water, sewer, street lighting, fire protection, and general government support.

Fiscal stress is a judgment about the financial condition of an individual entity that must take into consideration the entity's unique circumstances, but can be generally defined as a local government's or school district's inability to generate sufficient revenues within a fiscal period to meet expenditures (budget solvency). The Office of the State Comptroller's Fiscal Stress Monitoring System evaluates local governments (counties, cities, towns, and villages) and school districts, based on both financial and environmental indicators, to determine if these entities are in or nearing fiscal stress. The Town has been classified as susceptible to fiscal stress.

## Objective

The objective of our audit was to evaluate the Town's financial condition and addressed the following related question:

- Does the Board adopt realistic budgets that are structurally balanced and do Town officials adequately monitor the Town's financial operations to ensure fiscal stability?

## Scope and Methodology

We examined the Town's financial condition for the period January 1, 2012, through July 16, 2013. We extended our scope back to January 1, 2006 to include the purchase of a building and the establishment and closing of an enterprise fund.

**Comments of  
Local Officials and  
Corrective Action**

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.

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 findings and recommendations and 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 Town Clerk's office.

## Fiscal Stress

It is essential that the Board adopt structurally balanced budgets for all of its operating funds so that recurring revenues finance recurring expenditures and a reasonable fund balance is maintained. Once adopted, it is necessary to monitor the budget with actual operating results to prevent unplanned operating deficits. An unplanned operating deficit results from over-expended appropriations, receiving revenues in amounts less than budgeted, or a combination of the two. Recurring unplanned operating deficits usually indicate a failure to ensure that budgets are realistic and/or properly monitored. The Board should amend the budget to address revenue shortfalls or costs that are expected to exceed appropriations. In addition, it is important for the Board and Town officials 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 and allow Town officials to identify developing revenue and expenditure trends, set long-term priorities and goals, and avoid large fluctuations in tax rates.

The Board did not develop reasonable budget estimates for the general town-wide fund and did not properly monitor and control actual activity against those estimates, allowing appropriations to be over-expended. The Board aggregately over-estimated revenues for mortgage tax by \$154,157 and the rental of real property by \$77,580 in the three most recent fiscal years (2010-2012). The Board established rental charges for current occupants of the town hall, and therefore, should have been in a position to establish more accurate budget estimates. Further, the Supervisor included \$50,000 in the 2012 budget for the sale of property that was not sold in 2012.<sup>1</sup> In addition, the Board failed to recognize that a debt payment totaling \$62,649 was not included in the 2012 budget. The Board also reduced the tax levy in 2011 by five percent and appropriated \$6,495 of non-existent fund balance in the 2012 budget.<sup>2</sup>

The Board elected to close an enterprise fund to the general town-wide fund as of January 1, 2010, which has subsequently negatively impacted the general town-wide fund. The enterprise fund was established to account for the acquisition, improvements to, and rental of surplus space in the town hall. In 2005, the Town issued bonds

<sup>1</sup> Fifty thousand dollars also was included in the 2013 budget and it is unlikely that the property will be sold by year-end.

<sup>2</sup> Appropriating fund balance reduces the amount of taxes to be raised.

totaling \$1.7 million to purchase a former school building to house municipal offices and rent out office space. It was anticipated that rental income would offset the expenses associated with the building.<sup>3</sup> Some of the office space was rented through two 99-year leases, which required large payments totaling approximately \$300,000 that were received in 2006 and 2007, rather than an annual lease payment of \$3,100. Given the deficit cash position in the enterprise fund when it was closed, the cash from these payments had already been spent by the end of the 2009 fiscal year.

Upon closing the enterprise fund, the general town-wide fund absorbed the enterprise fund's deficit cash position<sup>4</sup> of approximately \$44,000 and annual debt payments of approximately \$200,000.<sup>5</sup> In addition, annual maintenance and personnel costs in the general town-wide fund increased by approximately \$67,000, while associated revenues (rental income) increased by only \$102,000. We also noted that the Town issued a bond anticipation note for \$400,000 in 2011 for a roof repair project. The Town paid \$50,000 in principal and \$12,649 in interest on this note in 2012 and expects to redeem \$25,000 in principal and pay \$11,725 in interest during 2013. Therefore, this note will have a balance due of \$325,000 at the close of the 2013 fiscal year.

Because of the revenue shortfalls and over-expended appropriations the general town-wide fund experienced operating deficits in the 2010, 2011, and 2012 fiscal years. Consequently, the general town-wide unrestricted fund balance declined from \$450,949 at January 1, 2010, to a deficit of \$107,587 at December 31, 2012.

<b>Table 1: General Town-Wide Fund Results of Operations</b>			
	<b>FY 2010<sup>a</sup></b>	<b>FY 2011</b>	<b>FY 2012</b>
Beginning Unrestricted Fund Balance	\$450,949	\$189,252	(\$76,919)
Revenues	\$852,098	\$ 846,689	\$1,170,039 <sup>b</sup>
Expenditures	\$1,069,488	\$1,112,860	\$1,200,707
Operating Surplus/(Deficit)	(\$217,390)	(\$266,171)	(\$30,668)
Year-End Unrestricted Fund Balance	\$233,559 <sup>c</sup>	(\$76,919)	(\$107,587)
<sup>a</sup> Includes unbudgeted revenues of approximately \$102,000 and expenditures of approximately \$266,500 due to the closure of the enterprise fund into the general fund <sup>b</sup> Includes approximately \$170,000 in sales tax not included in the budget <sup>c</sup> Does not agree with beginning 2011 fund balance due to deficit cash position (\$44,307) closed to general fund			

<sup>3</sup> Enterprise funds account for operations where the intent of the governing body is that the cost (expenses, including depreciation) of providing goods or services be financed primarily through user charges.

<sup>4</sup> The enterprise fund was in effect borrowing cash from other Town funds to pay its bills.

<sup>5</sup> Final payment due in 2014

While the Supervisor provided monthly financial reports to the Board that included year-to-date budget-to-actual comparisons, the Board failed to address the over-estimation of revenues and continued to adopt unrealistic budgets. In addition, the Board and Town officials have not developed a comprehensive multiyear financial plan to adequately address the Town's operational and capital needs. We discussed the Town's financial condition with Board members and although they realized that the general fund's finances were deteriorating, they were unclear on what specifically contributed to the decline. Several Board members stated that the building purchase was a critical factor. None, however, mentioned unrealistic budget estimates as a contributing factor. Moreover, Board members stated that once the debt issues related to the original acquisition and roof repair project are fully redeemed, the general fund's fiscal stress will be reduced. That is not the case. Unless Board action is taken to ensure that recurring expenditures are funded entirely by recurring revenues, the general town-wide fund balance will continue to decline. The cumulative fund balance deficit will need to be addressed either through identifying other sources of revenue, substantially reducing expenditures, or significantly increasing real property taxes for the general town-wide fund. This also assumes that other capital projects are not needed to address the building condition, which may require a large capital outlay and possibly the issuance of additional debt.

In 2012, the Supervisor re-allocated the amount of sales tax originally budgeted for the general town-wide fund, which increased revenues by approximately \$170,000<sup>6</sup> and the Board approved a substantial property tax increase for the 2013 fiscal year. However, this \$190,000 tax increase only offset the increased appropriation for workers' compensation (\$140,000) and the debt service payment on the bond (\$62,000). Further, our review of the 2013 budget found that the Board continued to over-estimate revenues. Based upon information provided to us by the Town, we estimate that the general town-wide fund will have a 2013 operating deficit of approximately \$58,000, resulting in a deficit unrestricted fund balance of approximately \$165,000 as of December 31, 2013.

The failure to monitor the budget during the fiscal year can lead to unplanned operating deficits, which can quickly deplete fund balance, leaving nothing to finance unanticipated costs or to help fund future budgets. To address these deficits and adopt a structurally balanced budget, the Board must increase revenues and/or decrease appropriations.

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<sup>6</sup> This reallocation of sales tax reduced the amount provided to the general part-town and highway funds. If this reallocation is continued in future years it will negatively impact the financial condition of those funds. Each of these funds had operating losses in 2012 due in large part to the reallocation of sales tax.

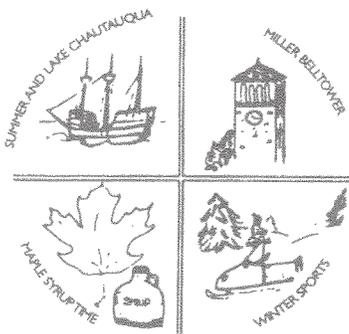
## **Recommendations**

1. The Board should ensure that the annual budget includes all necessary appropriations and that the amounts budgeted are reasonable.
2. The Board should monitor the actual revenues received against the revenue estimates in the adopted budgets and make amendments, as necessary, to the budget when revenue shortfalls become known.
3. The Board should implement a plan to eliminate the unrestricted fund balance deficit.
4. The Board should develop a comprehensive multiyear financial plan to establish long-term objectives for funding long-term needs.

## **APPENDIX A**

### **RESPONSE FROM LOCAL OFFICIALS**

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



## TOWN OF CHAUTAUQUA

Community Municipal Building • 2 Academy Street • Mayville, New York 14757  
Phone: (716) 753-7342 • Fax: (716) 753-5239

August 27, 2013

Robert Meller, Chief Examiner  
Office of the State Comptroller  
Buffalo Regional Office  
295 Main Street, Room 1032  
Buffalo, New York 14203

**Re: Town of Chautauqua Fiscal Stress Report**

Dear Mr. Meller:

This letter is in response to the preliminary draft report of the fiscal stress audit performed by your office for January 1, 2012 through July 16, 2013.

The Town Board has reviewed the draft report. We have no objections to the draft findings and look forward to formulating and submitting a Corrective Action Plan at the appropriate time.

Sincerely,

Donald D. Emhardt, Supervisor

## APPENDIX B

### AUDIT METHODOLOGY AND STANDARDS

The Office of the State Comptroller's Fiscal Stress Monitoring System evaluates local governments based on financial and environmental indicators. These indicators are calculated using a local government's annual update document<sup>7</sup> and information from the United States Census Bureau, the New York State Department of Labor, and the New York State Education Department, among other sources. The Town has demonstrated signs of fiscal stress in several areas. Due in part to these fiscal stress indicators, we selected the Town for audit.

Our overall goal was to assess the Town's financial condition. To accomplish this, our initial assessment included a comprehensive review of the Town's financial condition.

To achieve our financial condition objective and obtain valid audit evidence, we performed the following audit procedures for the period January 1, 2012, through July 16, 2013:

- We interviewed Town officials to determine what processes were in place and to gain an understanding of the Town's financial situation and budget.
- We reviewed and analyzed the Town's financial records and reports for all funds, including annual budgets, annual reports, bank statements, and general and subsidiary ledgers.
- We determined the reasonableness of budget estimates by comparing the adopted budgets to actual revenue and expenditures.
- We calculated operating losses over a three-year period and projected fund balance for the fiscal year ending December 31, 2013.

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.

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<sup>7</sup> Required to be submitted annually by the Town to the Office of the State Comptroller

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Andrew A. SanFilippo, Executive Deputy Comptroller  
Nathalie N. Carey, Assistant Comptroller

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