



Town of Salem

Financial Management

Report of Examination

Period Covered:

January 1, 2013 — June 30, 2015

2015M-295



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

January 2016

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 Salem, 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 Salem (Town) is located in Washington County and has a population of approximately 2,700. The Town provides various services to its residents, including street maintenance, lighting, fire protection and a Justice Court. The Town's 2015 budgeted appropriations totaled approximately \$1.12 million, which were primarily funded through real property taxes, sales tax and State aid.

The Town Board (Board) consists of the Town Supervisor (Supervisor) and four Board members. The Board is the legislative body responsible for the Town's overall management, including oversight of Town operations and finances and adopting and monitoring the budget. The Supervisor serves as the Town's chief fiscal officer and is responsible for maintaining a record of all receipts, expenditures and account balances, and providing the Board with timely, accurate and useful financial information. The Supervisor oversees a bookkeeper who carries out the Supervisor's responsibilities of maintaining the accounting records. The bookkeeper also provides financial reports to the Supervisor and the Board. The Supervisor, as budget officer, is also responsible for compiling the initial annual budget estimates and submitting a tentative budget to the Board for its review, modification and approval.

Objective

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

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

Scope and Methodology

We examined the Town's financial management and budgeting practices for the period January 1, 2013 through June 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.

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 Town Clerk's office.

Financial Management

The Board is responsible for making sound financial decisions that are in the best interests of the Town and its residents. This requires the Board to balance the level of services desired and expected by Town residents with the ability and willingness of the residents to pay for such services. A key measure of the Town's financial condition is its level of fund balance, which is the difference between revenues and expenditures accumulated over time. When maintained at reasonable levels, fund balance can be used to help finance the next fiscal year's operations. Additionally, Town officials should ensure that the level of fund balance maintained is reasonable to provide for unanticipated contingencies that may arise throughout the year.

It is essential that the Town adopt structurally balanced budgets that contain realistic appropriations and the resources available to fund them. The Board should also develop a detailed multiyear plan to allow officials to set long-term priorities for providing services and addressing capital acquisitions and improvements, along with ensuring there is a plan for funding the costs of the services and capital needs.

The Board needs to improve its budget development practices. The Board consistently budgeted to appropriate more fund balance in the town-wide general fund than was actually available to finance operations. These practices caused deficits of \$15,192 in 2014 and a projected deficit of \$8,437 in 2015. The Board also appropriated substantial fund balance in the town-wide highway fund to finance operations, which caused this fund's unrestricted fund balance to decrease by \$98,592, or 52 percent, from 2013 through 2015. The Board must be careful when appropriating fund balance in future budgets to ensure that it does not get depleted. Additionally, the Board has not developed a multiyear financial and capital plan to address the Town's long-term priorities. Lack of this plan diminishes the Board's ability to manage Town finances.

Budgeting and the Use of Fund Balance

Local governments must adopt structurally balanced budgets that provide for sufficient recurring revenues to finance recurring expenditures. A local government may choose to appropriate some of its fund balance to offset a planned imbalance between estimated revenues and expenditures. This is an acceptable budgeting practice, provided that the local government reasonably estimates that it will have an adequate level of unrestricted fund balance at the end of the fiscal year. However, when a local government appropriates too much fund balance or consistently has annual operating deficits, fund

balance is gradually depleted until it becomes a deficit. Therefore, there will be no fund balance available to be used for unforeseen events or financing successive budgets. This could cause the local government to experience fiscal stress.

Town-Wide General Fund – The adopted budgets for fiscal years 2013 through 2015 included an appropriation of fund balance to finance operations. The estimates for revenues and expenditures were generally reasonable during this time. However, the Board appropriated a significant amount of available fund balance for 2014 and an excessive amount of fund balance for 2015, as indicated in Figure 1. For example, at the end of 2013, total fund balance was \$51,752, of which the Board appropriated \$39,000, or 75 percent of available fund balance, to finance 2014 operations. At the end of 2014, total fund balance was \$24,808. However, the Board budgeted to appropriate \$40,000 of fund balance to finance operations in 2015. By appropriating more fund balance than what was actually available, the Board created a budget deficit of \$15,192 at the onset of the 2015 fiscal year.

As a result of the Board consistently appropriating fund balance to finance annual operations, fund balance has decreased substantially. We project the town-wide general fund will realize an operating deficit of \$33,245 for 2015, which will cause fund balance to decrease to a deficit of \$8,437 at the end of 2015. Figure 1:

Figure 1: Town-Wide General Fund			
	2013	2014	Projected 2015
Beginning Fund Balance	\$60,589	\$51,552 ^a	\$24,808
Revenues	\$349,648	\$237,643	\$261,264
Expenditures	\$358,485	\$264,387	\$294,509
Operating Deficit	(\$8,837)	(\$26,744)	(\$33,245)
Ending Fund Balance Surplus/(Deficit)	\$51,752	\$24,808	(\$8,437)
Budgeted Fund Balance Appropriated to Finance Next Year's Operations	\$39,000	\$40,000	Not Available ^b
Budget Deficit for Ensuing Year	\$0	(\$15,192)	(\$8,437)

^a Contains a prior period adjustment of \$200.
^b The 2016 budget was not complete at the end of our audit fieldwork.

The practice of appropriating excessive amounts of fund balance to finance operations has also resulted in the fund's cash balance decreasing significantly during our audit period. It is projected to decrease by \$122,110, or 105 percent, from \$116,610 at the beginning

of 2013 to a projected deficit of approximately \$5,500 at the end of 2015. The town-wide general fund will have insufficient cash to pay all its obligations through the end of the year. Therefore, the Board will have to consider short-term financing methods to address its cash flow needs.

Town-Wide Highway Fund – The town-wide highway fund has had a substantial fund balance in recent years. However, it is projected to decrease by \$98,592, or 52 percent, from \$190,179 at the beginning of 2013 to a projected balance of \$91,587 at the end of 2015, as indicated in Figure 2.

Similar to the town-wide general fund, the Board has consistently appropriated fund balance to help fund town-wide highway operations each year. Although the Board appropriated fund balance for 2013, the fund realized an operating surplus of \$11,277 partially because the Board overestimated 2013 snow removal costs by \$33,732, or 22 percent. The estimates for revenues and expenditures for 2014 and 2015 were generally reasonable. However, in 2014, the Town used \$55,985 (76 percent) of the \$73,999 fund balance that was appropriated. Furthermore, we project the Town will use \$53,884 (84 percent) of the \$64,000 fund balance that was appropriated for 2015.

Figure 2: Town-Wide Highway Fund

	2013	2014	Projected 2015
Beginning Fund Balance	\$190,179	\$201,456	\$145,471
Revenues	\$238,901	\$237,626	\$222,559
Expenditures	\$227,624	\$293,611	\$276,443
Operating Surplus/(Deficit)	\$11,277	(\$55,985)	(\$53,884)
Ending Fund Balance	\$201,456	\$145,471	\$91,587
Less: Fund Balance Appropriated to Finance Next Year's Operations	\$73,999	\$64,000	Not Available ^a
Unrestricted Fund Balance	\$127,457	\$81,471	Not Available ^a
Unrestricted Fund Balance as a Percentage of Next Year's Budgeted Appropriations	41%	28%	Not Available ^a

^a The 2016 budget was not complete at the end of our audit fieldwork.

While the projected amount of fund balance totaling \$91,587 at the end of 2015 is considered financially healthy, the Board must be careful when appropriating fund balance going forward. The significant annual decreases and continued reliance on fund balance as a financing source for operations could lead to fund balance being

exhausted. Consequently, the Town's ability to address unforeseen circumstances could be diminished in future years.

Multiyear Financial and Capital Planning

An important Board responsibility is to plan for the future by setting adequate long-term priorities and goals. To address this responsibility, it is important for the Board to develop a comprehensive multiyear financial and capital plan 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 the Board to identify developing revenue and expenditure trends, set long-term priorities and goals and avoid large fluctuations in tax rates. Multiyear plans also allow the Board to assess the effects and merits of alternative approaches to address financial issues, such as the use of unrestricted fund balance to finance operations and the accumulation of money in reserve funds. The Board should monitor and update long-term financial plans on an ongoing basis to help ensure that its decisions are guided by the most accurate information available.

The Board has not developed a comprehensive multiyear financial and capital plan and does not have any other mechanism to adequately address the Town's long-term operational and capital needs. Without a useful multiyear financial and capital plan, the Board's ability to effectively manage Town finances and adequately plan for future capital needs is diminished.

Recommendations

The Board should:

1. Review estimates of fund balance at year-end as part of the Town's budget process. The Board should not budget to appropriate fund balance to finance annual operations in excess of what is available or in a manner that could eventually exhaust fund balance.
2. Develop a comprehensive multiyear financial and capital plan that projects operating and capital needs and financing sources over a three- to five-year period. The Board should monitor and update this plan on an ongoing basis.

APPENDIX A
RESPONSE FROM LOCAL OFFICIALS

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



TOWN OF SALEM

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Town Clerk
Patricia Gilchrist

Town Council
Harold Gilchrist
Joseph Wever
Dorothy Schneider
Bruce Ferguson

January 20, 2016

Mr. Jeffrey P. Leonard, Chief Examiner
Office of State Comptroller
One Broad Street Plaza
Glens Falls, New York 12801-4396

Re: Town of Salem Financial Management Report of Examination

Dear Mr. Leonard,

Your teams recent audit of the Town of Salem was conducted in a very professional manner and the Town Board appreciates this and also with the help of developing a very difficult 2016 Town Budget which had to include the Village dissolution process.

The Town of Salem has strived over the past 5 years to reduce property taxes and keep spending at the lowest possible point and still maintain the best possible services for our taxpayers. To accomplish this and stay within the Tax cap guidelines using fund balances are critical. Also not having true guidelines as what is a sufficient fund balance makes it even more challenging.

I can agree with your findings that the Board should not budget to appropriate fund balance to finance annual operations to the degree that it would exhaust the balance, however as I stated above with the tax cap and school and county taxes raising every year makes it more and more difficult to operate efficiently.

I can also agree with your findings that a comprehensive multiyear financial and capital plan needs to be implemented. With the Village dissolution becoming effective on April 1, 2016 this will be even more important and will need to be a working document for us to go forward.

I will submit our Corrective Action plan for the Town in the coming weeks.

Sincerely,

Seth M. Pitts
Salem Town Supervisor

APPENDIX B

AUDIT METHODOLOGY AND STANDARDS

The objective of our audit was to assess the Town's financial management and budgeting practices for the period January 1, 2013 through June 30, 2015. We projected forward through December 31, 2015 to review fund balance levels and budgeting trends. To achieve our objective and obtain valid audit evidence, we performed the following audit procedures:

- We interviewed appropriate Town officials to gain an understanding of the Town's financial operations, budgeting, fund balance and long-term planning.
- We reviewed budget status reports and annual reports printed from the financial software and analyzed revenue and expenditure trends to determine if budgeted-to-actual variances were reasonable.
- We performed a financial analysis of Town operations for the years 2013 through 2014. This review included an assessment of fund balance for each Town fund, the determination of an operating surplus or deficit, a budget-to-actual analysis and a cash balance assessment.
- We projected the Town's results as of December 31, 2015. This included an assessment of fund balance for each Town fund, the determination of an operating surplus or deficit, a budget-to-actual analysis and a cash balance assessment.
- We reviewed pertinent documents, such as Town policies, Board minutes, financial records and reports.

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.

APPENDIX C

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