



# Town of Babylon

## Financial Condition and Internal Controls Over Selected Town Operations

Report of Examination

Period Covered:

January 1, 2011 — July 31, 2012

2013M-115



Thomas P. DiNapoli

# Table of Contents

	<b>Page</b>
<b>AUTHORITY LETTER</b>	2
<b>EXECUTIVE SUMMARY</b>	3
<b>INTRODUCTION</b>	6
Background	6
Objective	6
Scope and Methodology	7
Comments of Local Officials and Corrective Action	7
<b>FINANCIAL CONDITION</b>	8
Unexpended Surplus Fund Balance	9
Budgeting Practices	10
Inter-Fund Loans	12
Recommendations	14
<b>ADMINISTRATIVE CHARGES</b>	15
Recommendations	17
<b>HEALTH INSURANCE BENEFITS</b>	18
Recommendations	19
<b>LABOR CONSULTANT</b>	20
Recommendation	20
<b>INFORMATION TECHNOLOGY</b>	21
Computer Use Policy	21
Breach Notification Policy	21
Disaster Recovery	22
User Access Controls	22
Recommendations	23
<b>APPENDIX A</b> Response From Local Officials	24
<b>APPENDIX B</b> OSC Comments on the Town's Response	35
<b>APPENDIX C</b> Town's Interoffice Memorandum Dated January 23, 2004	39
<b>APPENDIX D</b> Audit Methodology and Standards	40
<b>APPENDIX E</b> How to Obtain Additional Copies of the Report	43
<b>APPENDIX F</b> Local Regional Office Listing	44

# State of New York Office of the State Comptroller

---

## **Division of Local Government and School Accountability**

November 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 Babylon, entitled Financial Condition and Internal Controls Over Selected Town Operations. 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 Town of Babylon (Town) is located in western Suffolk County, covers an area of about 53 square miles, and serves approximately 213,600 residents. The Town is governed by the Town Board (Board), which comprises five elected members: the Town Supervisor (Supervisor) and four Board members. The Supervisor is the Town's chief executive officer and is responsible for the Town's daily operations. The Comptroller is the chief fiscal advisor to the Board and assists the Supervisor in the preparation of the budget. The Comptroller is also responsible for maintaining accounting records, preparing payroll, and overseeing the health insurance program.<sup>1</sup>

The Town's major operating funds' expenditures were approximately \$146 million and \$145 million in 2011 and 2012, respectively.

#### **Scope and Objective**

The objective of our audit was to examine the Town's financial condition and internal controls over selected financial operations for the period January 1, 2011, to July 31, 2012. We extended our scope back to January 1, 2008, and forward to September 30, 2012, for the purpose of analyzing various aspects of financial condition. We also extended the scope to January 1, 2010, for the review of administrative charge backs. Our audit addressed the following related questions:

- Is the general fund in good financial condition?
- Is the Town using a suitable method for allocating general fund administrative costs to other funds?
- Did the Town provide health insurance benefits to only eligible current and former employees?
- Did a labor consultant perform duties that are generally executed by Town employees?
- Did the Town adopt a comprehensive computer policy and implement adequate controls to ensure that computerized data is safeguarded?

#### **Audit Results**

The Board has not taken appropriate actions to maintain the general fund's sound financial condition. From 2008 through 2011, the general fund's results of operations aggregated to net operating deficits

---

<sup>1</sup> Prior to February 19, 2013, the Supervisor oversaw the functions of the health insurance program.

of \$8.9 million, mainly due to over-estimation of certain revenues in adopted budgets. Although the general fund reported an operating surplus of almost \$1.5 million in 2011, this surplus resulted from \$4.5 million of questionable inter-fund revenues. Had the Town not recognized this revenue, the general fund would have reported an operating deficit of \$3 million for 2011.

From 2008 through 2011, the general fund's unexpended surplus fund balance<sup>2</sup> decreased from a surplus of \$6.1 million to a deficit of \$10.5 million.<sup>3</sup> This decline resulted from adopting budgets that were not structurally sound and using temporary loans to purchase investment properties held for resale. These temporary loans required \$26.5 million of fund balance to be reclassified from unexpended/unassigned to restricted and non-spendable. In the event those properties are sold, most of the fund balance will remain as non-spendable until the general obligation bonds issued to finance the purchase of the properties are liquidated. Between 2008 and 2011, the residential garbage district fund made 17 cash advances to the general fund, totaling almost \$28 million, to purchase property. None of the 17 cash advances were authorized by the Board, the advances were not paid by the end of each fiscal year, and no interest was paid on these temporary loans as required by law. Because of these practices, the Board cannot ensure that the Town is in sound financial condition.

The Town only allocated administrative charges to its residential garbage district (RGD) fund and commercial garbage district fund (CGD). This allocation method created taxpayer inequities. Furthermore, 96 percent of the operational expenditures for the RGD and the CGD funds are for routine contractual and debt service payments, which require minimum use of general fund support services. We question whether the \$5.7 million allocated to the RGD and the CGD funds during fiscal years 2010 and 2011 are legitimate charges attributable to those funds.

The Town also paid \$203,848 in health insurance premiums for nine officials and employees and \$30,751 to four other employees and officials who opted out of the health insurance plan during the audit period, even though none of these individuals were eligible, or otherwise authorized by the Board, to receive such benefits. As such, the risk is increased that unnecessary costs were incurred. We also found that a labor consultant initiated communication and authorized financial transactions, which are generally discretionary functions performed by Town officers. The Board's ability to monitor Town finances and operations may be compromised when there is lack of clarity as to whether independent contractors are carrying out discretionary duties conferred upon Town officers.

Finally, the Board has not adopted a comprehensive computer use policy, breach notification policy, or formal disaster recovery plan. In addition, users of the financial software have access rights to sections of the software that are not necessary for their job duties. As a result, the Town's IT system and electronic data are susceptible to an increased risk of loss, misuse, and manipulation.

<sup>2</sup> The Governmental Accounting Standards Board (GASB) issued Statement 54, which replaces the fund balance classifications of reserved and unreserved with new classifications: nonspendable, restricted, and unrestricted (comprising committed, assigned, and unassigned funds). The requirements of Statement 54 are effective for fiscal years ending June 30, 2011, and beyond. To ease comparability between fiscal years ending before and after the implementation of Statement 54, we will use the term "unexpended surplus funds" to refer to that portion of fund balance that was classified as unreserved, unappropriated (prior to Statement 54), and is now classified as unrestricted, less any amounts appropriated for the ensuing year's budget (after Statement 54).

<sup>3</sup> We did not include the Town's 2012 financial information as part of our review because the information included in the Town's 2012 annual update document submitted to OSC was unreliable and the Town's 2012 independently audited financial statements were not completed – and were therefore unavailable – during our audit.

## **Comments of Local Officials**

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 disagreed with the findings and recommendations in our report. Our comments on issues Town officials raised in their response letter are included in Appendix B.

# Introduction

## Background

The Town of Babylon (Town) is located in western Suffolk County, covers an area of about 53 square miles and serves approximately 213,600 residents. The Town is governed by the Town Board (Board), which comprises five elected members: the Town Supervisor (Supervisor) and four Board members. The Board, as the legislative body responsible for the general management and control of the Town's financial affairs, provides guidance through the enactment of laws, policies, and procedures. The Supervisor is the Town's chief executive officer and is responsible for the general administration, coordination, and supervision of Town operations. The Comptroller is the chief fiscal advisor to the Board and assists the Supervisor in the preparation of the budget. The Comptroller is also responsible for maintaining accounting records, preparing payroll, and overseeing the health insurance program.<sup>4</sup>

The Town provides various services to its residents, including sanitation, highway, parks, public safety, and general government support. The majority of funding to finance these services comes from real property taxes, fees, and State aid. The Town accounts for most of its financial activity in the town-wide general and highway funds, the part-town highway fund, the residential and commercial garbage district funds, and other special district funds. The Town's major operating funds' expenditures were approximately \$146 million and \$145 million in 2011 and 2012, respectively.

## Objective

The objective of our audit was to examine the Town's financial condition and internal controls over selected financial operations. Our audit addressed the following related questions:

- Is the general fund in good financial condition?
- Is the Town using a suitable method for allocating general fund administrative costs to other funds?
- Did the Town provide health insurance benefits to only eligible current and former employees?
- Did a labor consultant perform duties that are generally executed by Town employees?

<sup>4</sup> Prior to February 19, 2013, the Supervisor oversaw the functions of the health insurance program.

- Did the Town adopt a comprehensive computer policy and implement adequate controls to ensure that computerized data is safeguarded?

## **Scope and Methodology**

We examined the Town's financial condition and internal controls over selected financial operations for the period January 1, 2011, to July 31, 2012. We extended our scope back to January 1, 2008, and forward to September 30, 2012, for the purpose of analyzing various aspects of financial condition. When reviewing administrative charge backs, we extended the scope back to January 1, 2010. Our audit determined that the Town needs to improve information technology controls. Certain information technology vulnerabilities are not discussed in this report but were communicated confidentially to Town officials so they could take 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 is included in Appendix D 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 disagreed with the findings and recommendations in our report. Our comments on issues Town officials raised in their response letter are included in Appendix B.

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 Condition

A local government is in sound financial health when it can consistently generate sufficient revenues to finance anticipated expenditures, maintain service levels, and retain sufficient cash flow to pay bills and obligations when due without relying on short-term borrowings. Conversely, local governments in poor financial condition often experience unplanned operating deficits<sup>5</sup> and are unable to maintain current service levels without relying on short-term borrowing.

Although operating deficits can sometimes be planned by prudently using surplus fund balances to finance operations, persistent and recurring operating deficits are usually indicative of structurally imbalanced budgets and are an early indicator of financial stress. Therefore, local governments must adopt budgets that are structurally balanced, with reasonable estimates for revenues and appropriations, and must continually monitor the budget and fund balance levels to ensure that sufficient cash flow is maintained to fund operations. If temporary advances from other funds are necessary to meet general fund obligations, the advances must be approved by Board resolution, the loans must be repaid by the end of the fiscal year, and interest must be charged if the advances originate from a fund with a different tax base.

The Board has not taken appropriate actions to maintain the general fund's sound financial condition. From 2008 through 2011, the general fund's results of operations aggregated to net operating deficits of \$8.9 million, mainly due to over-estimation of certain revenues in adopted budgets. Although the general fund reported an operating surplus of almost \$1.5 million in 2011, this surplus resulted from \$4.5 million of questionable inter-fund revenues. Had the Town not recognized this revenue, the general fund would have reported an operating deficit of \$3 million for 2011.

<sup>5</sup> Unplanned operating deficits occur when appropriations are over-expended, expected revenues are not received, or a combination of both. By contrast, planned operating deficits occur when governing boards knowingly adopt budgets where the appropriations are greater than the expected revenues, with the difference being funded by unexpended surplus funds.

From 2008 through 2011, the general fund's unexpended surplus fund balance<sup>6</sup> decreased from a surplus of \$6.1 million to a deficit of \$10.5 million. This decline resulted from adopting budgets that were not structurally sound and using temporary loans to purchase investment properties held for resale. These temporary loans required \$26.5 million of fund balance to be reclassified from unexpended/unassigned to restricted and non-spendable. In the event those properties are sold, most of the fund balance will remain as non-spendable until the general obligation bonds issued to finance the purchase of the properties are liquidated. Between 2008 and 2011, the residential garbage district fund made 17 cash advances to the general fund, totaling almost \$28 million, to purchase property. None of the 17 cash advances were authorized by the Board, the advances were not paid by the end of each fiscal year, and no interest was paid on these temporary loans as required by law. Because of these practices, the Board cannot ensure that the Town is in sound financial condition.

### **Unexpended Surplus Fund Balance**

Unexpended surplus fund balance provides a cushion to help deal with revenue shortfalls or expenditure overruns. A deficit unexpended fund balance indicates that the municipality has reserved more fund balance than available and/or is incurring operating deficits. As indicated in Table 1, the general fund's unexpended fund balance declined substantially since 2008, from a surplus of \$6.1 million to a deficit of \$10.5 million. The Town reported deficit unexpended fund balances from 2009 through 2011, which were largely due to annual operating deficits and the acquisition of assets held for resale, which required unexpended fund balance to be reclassified as restricted or non-spendable. In either case, the reclassified portion of fund balance was not available to fund current operations.

The Town has undertaken a revitalization program in Wyandanch since 2008, funded primarily with proceeds from general obligation bonds (GOBs). However, GOBs were not issued until 2011; by that time, the Town had acquired land properties costing \$26.5 million, initially funded mostly by inter-fund loans from the residential garbage district (RGD) fund. In 2011, the Town issued GOBs of \$8.45 million, which were used to partially repay the outstanding loan to the RGD fund. At December 31, 2011, the general fund still owed the RGD fund \$17.6 million.

<sup>6</sup> The Governmental Accounting Standards Board (GASB) issued Statement 54, which replaces the fund balance classifications of reserved and unreserved with new classifications: nonspendable, restricted, and unrestricted (comprising committed, assigned, and unassigned funds). The requirements of Statement 54 are effective for fiscal years ending June 30, 2011 and beyond. To ease comparability between fiscal years ending before and after the implementation of Statement 54, we will use the term "unexpended surplus funds" to refer to that portion of fund balance that was classified as unreserved, unappropriated (prior to Statement 54), and is now classified as unrestricted, less any amounts appropriated for the ensuing year's budget (after Statement 54).

The Town intends to resell the land to private developers to complete the revitalization program. Under generally accepted accounting principles, land held for resale is recorded as an investment asset on the general fund's balance sheet. Since this asset is not liquid and not available to fund current operations, a corresponding amount of fund balance<sup>7</sup> has been reclassified in part as nonexpendable, to reflect the outstanding inter-fund loan, and as restricted to the extent of GOBs issued. However, the Town has reclassified more fund balance than it had available and reported annual unexpended fund deficits in the general fund since 2009.

<b>Fund Balance</b>	<b>2008</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>
Reserved for Land Purchased For Resale	\$3,575,864	\$10,495,690	\$13,844,539	N/A
Reserved for Encumbrances and Prepaid Expenses	\$277,515	\$331,745	\$596,007	N/A
<b>Reserved Fund Balance</b>	<b>\$3,853,379</b>	<b>\$10,827,435</b>	<b>\$14,440,546</b>	<b>N/A</b>
Nonexpendable				\$18,016,705
Restricted				\$8,450,000
Appropriated	\$2,004,800	N/A	N/A	N/A
Unexpended Surplus Funds/(Deficit)	\$6,103,336	(\$3,486,049)	(\$8,460,760)	(\$10,548,439)
<b>Total Fund Balance</b>	<b>\$11,961,515</b>	<b>\$7,341,386</b>	<b>\$5,979,786</b>	<b>\$15,918,266</b>

Town officials indicated that the Town intends to sell the land for no less than the book value. However, the proceeds from any eventual land sale may not necessarily eliminate the \$10.5 million unexpended fund balance deficit reported in 2011 because \$8.45 million of fund balance will still remain restricted until the related GOBs are paid off. It is imperative that Town officials closely monitor the Town's financial condition because deficit fund balances can seriously affect the Town's ability to provide cash flow and maintain services at current levels.

## **Budgeting Practices**

A structurally balanced budget accommodates a local government's ability to provide sufficient recurring revenues to fund needed services for the long term. Therefore, Board members must ensure that there is a process to prepare, adopt, and amend budgets based on reasonably accurate assessments of recurring revenue sources sufficient to fund annual budget appropriations. When estimating revenues in the annual budget, the Board and Town officials must have current and accurate information and use historical data, such as prior years' actual results of operations, to guide them in determining the reasonableness of revenue estimates.

<sup>7</sup> Property held for resale is considered a non-current asset because the asset is not available to fund current operations. Depending on how the purchase of the asset was financed, generally accepted accounting principles require that a corresponding amount of fund balance be designated either as nonexpendable or restricted.

Continuous reductions in fund balance can be an indication of poorly structured budgets, even if fund balance is positive. When preparing the budget, Town officials must estimate the total fund balance that will be available to fund the ensuing year's budget.

The general fund's unexpended fund balance decreased from a surplus of \$6.1 million in 2008 to a deficit of \$10.5 million in 2011.<sup>8</sup> This decline resulted from adopting budgets that were not structurally sound and from reclassifying fund balance from unexpended to restricted and nonexpendable to reflect the Town's investment in property held for resale, which is not liquid or available to fund operations. Table 2 shows results of operations for the general fund. Other financing sources and uses related to bond proceeds are shown separately because the proceeds were used to finance property held for resale and not for recurring operating expenditures.

The Town's results of operations from 2008 through 2011 aggregated to a net operating deficit of \$8.9 million. Although 2011 shows an operating surplus of almost \$1.5 million, this surplus resulted from questionable inter-fund revenues of \$4.5 million for administrative charges allocated to the RGD and commercial garbage district funds, which we discuss separately in this report. Had the Town not recognized this questionable revenue, the general fund would have reported an operating deficit of \$3 million for 2011.

	<b>2008</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>Total</b>
Original Budgeted Revenues	\$43,871,154	\$43,827,713	\$43,022,587	\$45,684,245	
Actual Revenue	\$41,126,888	\$39,873,494	\$40,318,621	\$46,551,448	
Revenue Variance	(\$2,744,266)	(\$3,954,219)	(\$2,703,966)	\$867,203	(\$8,535,248)
Original Budgeted Expenditures	\$45,223,892	\$45,860,025	\$44,709,152	\$45,708,291	
Actual Expenditures	\$45,529,624	\$44,493,620	\$41,680,221	\$45,062,968	
Expenditure Variance	(\$305,732)	\$1,366,405	\$3,028,931	\$645,323	\$4,734,927
Appropriated Fund Balance	(\$1,352,738)	(\$2,032,312)	(\$1,686,565)	(\$24,046)	(\$5,095,661)
Operating Surplus/(Deficit)	(\$4,402,736)	(\$4,620,126)	(\$1,361,600)	\$1,488,480	(\$8,895,982)
Other Financing Sources/ Uses – Bond Proceeds	(\$425,472) <sup>a</sup>	\$0	\$0	\$8,450,000	\$8,024,528
Combined Operating Surplus/(Deficit) and Financing Sources/Uses	(\$4,828,208)	(\$4,620,126)	(\$1,361,600)	\$9,938,480	(\$871,454)

<sup>a</sup> This amount represents the difference between proceeds of refunding bonds of \$10,446,093 and \$10,871,565 of prior years bonds refunded. Premiums on the issuance of refunding bonds of \$505,064 were included as operating revenue.

<sup>8</sup> We did not include the Town's 2012 financial information as part of our review because the information included in the Town's 2012 annual update document submitted to OSC was unreliable and the Town's 2012 independently audited financial statements were not completed – and were therefore unavailable – during our audit.

The operating deficits from 2008 through 2011 were caused by the annual appropriation of fund balance totaling \$5.1 million and unrealistic estimated revenues totaling \$8.5 million, which prevented the Town from replenishing any of the fund balance it had appropriated to balance the budgets. Positive expenditure variances of \$4.7 million mitigated some of the impact of the negative revenue variances on results of operations. However, the total negative revenue variances exceeded the positive expenditure variances by \$3.8 million.

From 2008 through 2011, the Town consistently over-estimated revenues from mortgage taxes, interest on earnings, rental of real property/beach leases, and operating transfers in adopted budgets by almost \$18 million. The decline in the mortgage tax revenue is directly related to the downturn in the economy and the housing market. While Town officials decreased the 2009 budget estimate by \$2.3 million to reflect this revenue's decline in the prior year, they did not adjust revenue estimates in subsequent adopted budgets to reflect its continued decline. As a result, \$8.4 million in mortgage tax revenue was not realized during this period.

Interest on earnings revenue was over-estimated by almost \$3 million, or 75 percent, during this period. Although the revenue realized from rental of real property/beach leases was consistently under \$700,000, budget estimates were set at \$900,000 from 2008 through 2010 and at \$750,000 in 2011. During this period, almost \$800,000 was not realized for this revenue. Town officials included significant estimated revenue from operating transfers in the adopted budgets but they seldom made these transfers. As a result, these revenue variances ranged from a negative 76 percent to a negative 100 percent, for an aggregate negative variance of \$5.8 million over this period.

Had Town officials based their budget estimates on historical trends and actual results of operations, budgets would have been more realistic and the significant operating deficits could have been avoided.

## **Inter-Fund Loans**

General Municipal Law (GML) allows municipalities to temporarily advance moneys held in any fund to any other fund, with limited exceptions. The Board must authorize each advance in the same manner in which it authorizes budgetary transfers between appropriations, ensure that suitable records are maintained, and ensure that repayment is made, with interest,<sup>9</sup> no later than the close of the fiscal year in which the advance was made. Effective recordkeeping is required to account for these inter-fund advances. Adjustment to the advance balances should be supported either by a direct payment or by journal entries that are justified and sufficiently documented to ensure the validity of the charges.

<sup>9</sup> GML requires that temporary advances be paid by the end of each fiscal year with interest if the tax basis of the two funds is not the same.

Between 2008 and 2011, the RGD fund made 17 cash advances to the general fund, totaling almost \$28 million, to purchase most of the Wyandanch revitalization project's property that is held for resale<sup>10</sup> in the general fund. None of the 17 cash advances were authorized by the Board, the advances were not repaid by the end of each fiscal year, and no interest was paid on these temporary loans as required. Table 3 shows the temporary loan balances and loan reductions made during fiscal years 2008 through 2011.

	<b>2008</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>Loan Total</b>
Loan Balance	\$5,829,229	\$18,465,596	\$17,433,600	\$17,611,167	\$17,611,167
Loan Reduction	\$73,553	\$963,634	\$1,031,996	\$8,272,433	\$10,341,616
<b>Total Loans</b>					<b>\$27,952,783</b>

Although \$10.3 million was repaid during this period, partly with proceeds from GOBs, no interest<sup>11</sup> was paid on these loans and a \$17.6<sup>12</sup> million balance still remained at December 31, 2011. We are also concerned because almost \$1.1 million of the loan reductions was not adequately documented or explained. We also found no basis for the Town allocating almost \$4.3 million of general fund administrative charges to the RGD fund, which further questions the validity of this loan reduction (discussed separately in this report) as shown on Table 4.

<b>Fiscal Year</b>	<b>Cash Payments</b>	<b>Administrative Charges</b>	<b>Undocumented Reductions</b>	<b>Total Reduction</b>
2008	\$0	\$0	\$73,553	\$73,553
2009	\$0	\$615,807	\$347,827	\$963,634
2010	\$0	\$804,335	\$227,661	\$1,031,996
2011	\$5,000,000	\$2,839,230	\$433,203	\$8,272,433
<b>Totals</b>	<b>\$5,000,000<sup>a</sup></b>	<b>\$4,259,372</b>	<b>\$1,082,244</b>	<b>\$10,341,616</b>

<sup>a</sup> Paid from proceeds of GOB

According to Town officials, the non-cash loan reductions aggregating almost \$5.4 million consist of various inter-fund transactions, which Town officials characterized as the “netting” of inter-fund activities between the general fund and the RGD fund at year end. Although the journal entries were not adequately documented and did not provide

<sup>10</sup> Town officials also stated that they used surplus funds from the general fund to finance the project. The property is recorded in the 2011 financial statements at \$26.5 million and the total amount borrowed from the RGD fund was \$27.9 million.

<sup>11</sup> Since general fund taxes and RGD fund taxes are raised from different tax bases, a reasonable amount of interest must be paid on the loan.

<sup>12</sup> An additional \$8.5 million was repaid with proceeds of obligations in September 2012, reducing the loan balance to \$9.1 million at that date.

a clear audit trail to justify the adjustments, we were provided with information suggesting that about \$4.3 million is related to general fund administrative charges booked at year end. No documentation was provided to justify the additional undocumented loan reductions of almost \$1.1 million.

The Board did not authorize the loans and did not provide proper oversight to ensure that the interest of taxpayers of different tax bases was protected. As a result, there is no assurance that the \$5.3 million of non-cash loan reductions is accurate or legitimate.

## **Recommendations**

1. The Board should develop a long-term financial plan to mitigate the negative impact of its recurring operating deficits and to eliminate deficit fund balances.
2. The Board should adopt budgets that are structurally balanced. Recurring revenues should be reasonably estimated and attainable, and sufficient to cover the cost of recurring expenditures.
3. The Board should authorize all temporary advances in the same manner that it authorizes budget transfers.
4. The Board and Town officials should ensure that all temporary advances are repaid by the end of each fiscal year and with interest, when required.
5. The Board and Town officials should maintain proper documentation to justify any non-cash reduction in temporary loan balances.
6. The Board should review the non-cash reductions in the temporary loans, determine their legitimacy, and ensure that the interests of RGD fund taxpayers are protected.

## Administrative Charges

Municipalities must maintain financial and accounting systems to ensure they use public funds legally and appropriately. It can be challenging for local governments to correctly allocate the costs of general overhead services used by all funds and departments. When allocating overhead costs, municipalities should develop and maintain an overhead allocation plan that outlines which overhead costs will be allocated to which funds or departments and on what basis. Departments and funds should be charged only for the actual cost of services received.

Appropriate documentation should be maintained to show what overhead costs were allocated to each department or fund, the amount of the charges, and how they were calculated. The plan should ensure that certain general government costs or costs that do not clearly benefit other funds or departments are charged entirely to the general fund. To the extent that the general fund provides services to departments that are accounted for in other funds, the general fund is entitled to be reimbursed for those costs.

From 2008 through 2011, Town officials included \$5 million in estimated inter-fund revenue in general fund budgets for administrative charges allocated to other funds or departments. However, the amount of revenue realized has not been consistent with budget estimates, resulting in significant revenue variances that fluctuated from a negative \$1.2 million to a positive \$3.8 million, as shown in Table 5.

<b>Table 5: General Fund - Administrative Charges Allocated to Other Funds</b>					
<b>Inter-Fund Revenue</b>	<b>2008</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>Total</b>
Budget	\$1,500,000	\$1,850,000	\$850,000	\$850,000	\$5,050,000
Actual	\$317,408	\$1,506,718	\$1,588,764	\$4,687,751	\$8,100,641
Revenue Variance (Negative)	(\$1,182,592)	(\$343,282)	\$738,764	\$3,837,751	\$3,050,641

Town officials have not developed an allocation plan based on the direct relationships between cost of services provided by the general fund and the actual services received by the benefitting funds or departments. Instead, the allocation method is based on the relative percentage of the various funds' adopted budgets and bears no relationship between the services provided, if any, and the cost of those services. Further, of the 10 funds included in the cost allocation schedule, the RGD and commercial garbage district (CGD) funds were allocated the vast majority of administrative charges. In the 2010 and 2011 fiscal years, the general fund realized revenues from administrative charges allocated to other funds of \$1.6 and \$4.7



million,<sup>13</sup> respectively. However, instead of allocating the charges to each fund based on their relative percentage of the total budget, Town officials allocated administrative charges of \$1.3 million and \$4.5 million in 2010 and 2011, respectively, to the RGD and CGD funds, as indicated in Table 6.

<b>Fund</b>	<b>2010 Budget</b>	<b>Administrative Charges Allocated</b>	<b>2011 Budget</b>	<b>Administrative Charges Allocated</b>
General	\$44,709,152	\$0	\$45,684,245	\$0
Part Town	\$6,271,194	\$0	\$6,315,811	\$0
Highway #1	\$14,675,082	\$0	\$14,536,996	\$0
Highway #3	\$2,691,278	\$0	\$2,685,967	\$0
Highway #4	\$1,363,339	\$0	\$1,437,061	\$0
Residential Garbage District	\$46,719,343	\$804,335 <sup>a</sup>	\$42,920,605	\$2,839,230
Commercial Garbage District	\$27,162,063	\$467,631 <sup>b</sup>	\$24,625,930	\$1,629,024
Special Lighting District	\$2,272,069	\$0	\$2,129,011	\$0
Special Districts	\$15,313,744	\$0	Excluded	\$0
East Farmingdale Water District	\$1,647,013	\$0	Excluded	\$0
<b>Total</b>	<b>\$162,824,277</b>	<b>\$1,271,966</b>	<b>\$140,335,626</b>	<b>\$4,468,254</b>

<sup>a</sup> Due to calculation error, the 2010 allocation to the RGD fund was understated by \$464,415.  
<sup>b</sup> Due to calculation error, the 2010 allocation to the CGD fund was understated by \$270,006.

Town officials stated that they did not allocate administrative charges to funds other than the RGD and CGD because the charges were not considered material. However, materiality should not be a factor in determining whether or not to allocate the actual cost of services provided to other funds, especially those funds with different tax bases. We also found that the RGD and CGD funds do not require extensive administrative services from the general fund because 96 percent of these funds' expenditures are routine contractual and debt service payments, which require minimum use of general support services.

Allocating the administrative charges based solely upon the weighted average of a fund's budget is generally not a reasonable method for determining the cost of services provided, if any, from one fund to

<sup>13</sup> The Town made separate calculations to allocate administrative charges to the East Farmingdale Water District and the Town of Babylon Housing Assistance Agency. Those charges aggregated to \$316,798 and \$219,497 in 2010 and 2011, respectively, and were not included in our review.

another. Town officials can quantify the actual cost of services by either maintaining complete and accurate accounting of each service provided or using an acceptable allocation method for calculating administrative charges, such as basing personnel charges on the number of full-time employees.

When Town officials allocate administrative charges without using a reasonable allocation method, the Town may be either over-charging or under-charging for such services. In either case, using an inappropriate cost allocation method created an inequity because one fund was benefitting at the expense of the other fund. We question whether the charges of \$5.7 million allocated to the RGD and the CGD funds during 2010 and 2011 are legitimate charges attributable to those funds.

## **Recommendations**

7. Town officials should discontinue using the current method for allocating administrative charges to other funds and develop an allocation plan based on the direct relationship between the services provided by the general fund and the actual cost of services received by the benefitting department or fund.
8. The Board should review the administrative charges allocated to the RGD and CDG funds and determine whether they represent a legitimate cost of general fund services provided to these funds. The Board should refund any unnecessary charges to the RGD and the CGD funds.

## Health Insurance Benefits

Fringe benefits comprise a significant portion of the Town's budget. All benefits provided to Town officials and employees must be properly authorized either by the Board through resolution, policy, or local law, or through a negotiated employment contract. Without such express authority, employees are not entitled to receive fringe benefits.

The Town provides health insurance benefits to eligible employees who belong to one of two bargaining units and to employees covered under the Town's Administrative Salary Plan. The bargaining agreements and the Administrative Salary Plan preclude part-time employees from being eligible to receive health insurance coverage. Eligible employees are also offered compensation in the event they opt out of the Town's health insurance provided under their collective bargaining agreement or the Administrative Salary Plan.

The Town paid \$203,848 in health insurance premiums for nine officials and part-time employees and \$30,751 to four officials who opted out of the health insurance plan during the audit period, even though none of these individuals were eligible, or otherwise authorized by the Board, to receive such benefits.<sup>14</sup> Town officials could not provide us with a resolution or local law authorizing health insurance benefits for part-time employees and Town elected officials, who are not covered by the Town's bargaining agreements and Administrative Salary Plan. The nine employees who received health insurance coverage without Board authorization included four part-time assistant Town attorneys at a cost of \$75,069,<sup>15</sup> a member of a Town municipal board costing \$16,625, two Board members at a cost of \$55,454, the Receiver of Taxes at a cost of \$29,107 and a part-time senior citizen aid at a cost of \$27,593.

Town officials indicated that health insurance for the senior citizen aid was authorized by the Town's labor consultant who, through an interoffice memorandum to the Director of Employee Benefits, stated that the employee was authorized to receive cost-free coverage under the Town's health insurance plan. However, the memo did not indicate who, other than the consultant, authorized this benefit. There was no indication that the Board had authorized this benefit.

<sup>14</sup> Under the bargaining agreements and the Administrative Salary Plan, only full-time employees are entitled to receive health insurance coverage.

<sup>15</sup> This amount does not include employees' contributions toward their health insurance plans of \$19,382.

The Town also paid the former Town Supervisor, the Town Clerk and two Councilmen a total of \$30,751 for opting out of the Town's health insurance program, even though Town officials could not document that these officials were eligible to receive this benefit. Elected officials are not covered by provisions of the bargaining agreements or Administrative Salary Plan, and no resolution or local law was provided to us to show that elected officials were entitled to this benefit.

In addition, Town officials were not consistent when calculating the health insurance buy-out payments to the four individuals. For example, the \$9,083 payments each to the former Town Supervisor, Town Clerk, and one Board member were calculated based on provisions in the Blue and White Collar Bargaining Agreements,<sup>16</sup> while the payment of \$3,500 to the other Council member was calculated in accordance with provisions in the Administrative Salary Plan.<sup>17</sup>

When the Town provides health insurance benefits without Board approval, there is an increased risk that costs are incurred unnecessarily and not as the Board intended.

## **Recommendations**

9. Town officials should review the questionable health insurance opt-out payments identified in this report and attempt to recover them, if possible.
10. Town officials should ensure that only eligible employees are provided health insurance coverage in accordance with the terms of their respective bargaining agreement, local law, resolution, or Town-wide policies. If the Board intends to extend health insurance benefits to Town officials and employees who are otherwise ineligible to receive such benefits, the Board must formally authorize them.
11. Town officials should ensure that payments in lieu of health insurance are calculated and paid based on provisions of the employees' respective bargaining agreements or Board approved policy.

<sup>16</sup> Full-time employees of both bargaining agreements are authorized to receive 50 percent of the cost of the insurance premiums annually to opt out of the Town's health insurance plan.

<sup>17</sup> Full-time employees in the Administrative Salary Plan are paid \$3,500 in the event they opt of the Town's health insurance plan.

## Labor Consultant

The Town may retain independent contractors and consultants to advise and assist Town officials and employees in the performance of their duties. In addition, the Town may contract with private entities to perform certain functions that are purely ministerial in nature. However, absent express statutory authority, the discretionary duties and responsibilities of public officers, conferred upon them by law, may not be discharged by contracting with private parties. In general, a discretionary function requires the exercise of judgment which can produce varying results, while a ministerial function requires adherence to a definite standard without any “latitude of choice.”<sup>18</sup>

The Director of Labor Relations retired from Town service effective December 29, 1995. The Town engaged the Director, effective January 1, 1996, as an independent contractor to serve as a labor consultant. Based upon his contract with the Town, the consultant was retained to consult on various labor-related issues, review and advise on collective bargaining issues, act as hearing officer in grievance hearings, and assist and advise on Civil Service issues.

However, we found that the consultant sent correspondence on the Town letterhead and signed off on documents and correspondence which indicated he was acting on behalf of the Town Personnel Department or Office of Personnel and Labor Relations. These actions created at least an ambiguity as to whether his role included solely the performance of merely ministerial and advisory functions, or whether he was permitted to perform discretionary functions on behalf of the Town. This lack of clarity as to his role was further demonstrated by Town officials and employees, who indicated that the duties this individual performed as a consultant are the same as those performed in his former capacity as Director of Labor Relations. During the audit period, the consultant was paid \$50 per hour for a total amount of \$78,681 (\$47,700 in 2011 and \$30,981 through July 2012).

The Board’s ability to monitor Town finances and operations may be compromised when there is lack of clarity as to whether independent contractors are carrying out discretionary duties conferred upon Town officers.

### Recommendation

12. The Board should clarify and monitor the functions of the labor consultant to ensure that, in appearance and fact, he does not perform discretionary functions conferred upon Town officers.

<sup>18</sup> See 1990 Op St Comp No. 90-53

# Information Technology

The Town relies on its information technology (IT) system for accessing the internet, communicating by e-mail, storing data, maintaining financial records, and reporting to State and Federal agencies. Therefore, the Town's IT system and the data it holds are valuable resources. If the IT system fails, the results could range from inconvenient to catastrophic. Even small disruptions in IT systems can require extensive effort to evaluate and repair. For this reason, it is important that Town officials adopt written policies and procedures to effectively safeguard IT resources. Town officials must also limit and monitor computer system access, as well as adopt a breach notification policy and formal disaster recovery plan.

The Board has not adopted a detailed comprehensive computer use policy, a breach notification policy or a formal disaster recovery plan. Additionally, financial software users have access rights to sections of the software that are not necessary for their job duties. Because of these weaknesses, the risk is increased that the Town's system and data it holds could be compromised.

## **Computer Use Policy**

Computer policies and procedures address key security areas such as acceptable computer use, data and virus protection, password security, disposing of and sanitizing equipment, remote access, and acceptable internet use. Policies must be implemented, enforceable, concise, and easy to understand, and should balance IT protection with employees' productivity. Town officials are responsible for establishing procedures that outline how to carry out policy requirements and define mechanisms to enforce compliance. Although the Board has adopted a computer, e-mail, and internet use policy, the policy does not address such areas as data and virus protection, password security, disposing of and sanitizing equipment, and remote access.

Although comprehensive computer use policies do not guarantee the safety of the Town's electronic information, the lack of such policies significantly increases the risk that hardware and software systems and the data they contain may be lost or damaged by inappropriate use.

## **Breach Notification Policy**

An individual's private and/or financial information, along with confidential business information, could be severely impacted if security is breached or data is improperly disclosed. New York State Technology Law requires cities, counties, towns, villages, and other local agencies to establish an information breach notification policy. The policy should detail how the Town would notify individuals

whose private information was, or is reasonably believed to have been, acquired by a person without a valid authorization. The disclosure should be made in the most expedient time possible and without unreasonable delay, consistent with the legitimate needs of law enforcement or any measures necessary to determine the scope of the breach and restore the reasonable integrity of the data system.

The Board has not adopted a breach notification policy. By failing to adopt such a policy, in the event that private information is compromised, Town officials and employees may not understand or be prepared to fulfill their legal obligation to notify affected individuals quickly.

## **Disaster Recovery**

A disaster recovery plan is intended to identify and describe how Town officials will deal with potential disasters. Such disasters may include any sudden, unplanned catastrophic event (e.g., fire, computer virus, or inadvertent employee action) that compromises the availability or integrity of the IT system and data. Contingency planning is used to avert or minimize the damage that disasters would cause to operations. Such planning consists of the precautions to be taken to minimize the effects of a disaster so officials and responsible staff will be able to maintain or quickly resume day-to-day operations. Typically, disaster recovery planning involves an analysis of business processes and continuity needs and should include significant focus on disaster prevention. The plan should also address the roles of key individuals, and be distributed to all responsible parties, periodically tested, and updated as needed.

The Board has not developed a disaster recovery plan to address potential disasters. Consequently, in the event of a disaster, Town personnel have no guidelines or plan to follow to help minimize or prevent the loss of equipment and data or to appropriately recover data. Without a disaster recovery plan, the Town could lose important financial data and suffer a serious interruption in Town operations.

## **User Access Controls**

To protect computer resources from unauthorized use or modification, user rights should be assigned to officials and employees based on their job responsibilities. Therefore, access to specific components of an IT system should be restricted to the functions that employees need to perform their jobs. It is important for user accounts to be established and maintained so that access rights are matched to job responsibilities. Town officials can restrict access to some users while allowing greater access to others based on their job responsibilities. Town officials should periodically review user access rights to help ensure access is properly controlled and revise those rights as necessary.

We found that user permissions, as listed on the Town's financial software's access report, were not reliable because they did not match the actual level of access available to the users. Because we could not rely on the access reports to assess user access controls, we tested user access to the financial software by observing four employees in the Comptroller's office accessing the computer system. We determined that the employees did not need access to two of the four modules they had access to in order to perform their job responsibilities. In addition, the Town's financial software is not capable of producing audit trail reports, preventing Town officials from monitoring user access, and detecting unauthorized or unusual activity. This increases the risk that inappropriate transactions can be made in the computerized financial system without detection.

## **Recommendations**

13. Town officials should adopt a comprehensive computer policy addressing key security issues such as data and virus protection, password security, disposal and sanitizing of equipment, and remote access.
14. Town officials should adopt an information breach notification policy.
15. Town officials should establish a formal disaster recovery plan that provides guidance to maintain Town operations or restore data as quickly as possible in the event of a disaster.
16. Town officials should monitor users' access to the Town's financial software and restrict access to what the users need to perform their job responsibilities.



**APPENDIX A**  
**RESPONSE FROM LOCAL OFFICIALS**

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

# Town of Babylon

Office of the Comptroller  
200 E. Sunrise Highway  
Lindenhurst, New York 11757  
(631) 957-3000



**RICH SCHAFFER**  
SUPERVISOR

October 10, 2013  
Mr. Ira McCracken, Chief Examiner  
Office of the State Comptroller  
110 State Street  
Albany, New York 12236

RE: OSC Draft Report of Examination: Town of Babylon, New York

Dear Mr. McCracken:

Thank you for providing the Town of Babylon (“Town”) with an opportunity to review and comment on the New York State Office of the State Comptroller’s (“OSC”) draft Financial Condition and Internal Controls Over Selected Town Operations; Report of Examination (2013M – 115) covering the period 1/1/2011 to 7/31/2012 (the “Draft Report”). We are pleased with the input of your office and are always interested in hearing of ways to improve upon the Town’s internal financial controls and budgetary management.

The purpose of this letter is to provide comments to the Draft Report in anticipation of a final report. The methodology used in this review and comment letter is to work through the Draft Report sequentially beginning with the Executive Summary and move through the specific findings of the Draft Report. Our understanding is that the Town’s comments on the Draft Report will be included as Appendix A in the Final Report. We have focused specifically on factual information presented in the Draft Report and have attempted to provide any back-up data necessary to substantiate our findings.

In general, the Town is in agreement with most material, factual representations made in the Draft Report; what we take issue with in the detailed comments below have more to do with the wording and meaning of the conclusions reached in the Draft Report and believe a more thorough understanding of the Town’s budgetary objectives over the recent past will assist in clarifying the findings and conclusions contained in the Draft Report.

Over the past 10 to 15 years, as the Town emerged from a period of significant historical budgetary stresses in its major funds, the Town has been focused on a few major goals that we believe have been largely achieved. These include i) improving the fund balances of the Town’s major funds to provide budgetary flexibility so that varying economic requirements can be met without drastic tax implications for our ratepayers; ii) reducing the Town’s reliance on bonded indebtedness thereby mitigating the need to allocate scarce economic resources to pay debt service to outside parties; iii) increasing our credit ratings to provide much lower interest costs for the debt that is issued; and iv) responding quickly and measurably to adjust tax rates among

*Enio A. Martinez*  
Councilman  
Deputy Supervisor

*Thomas Donnelly*  
Councilman

*Jacqueline A. Gordon*  
Councilwoman

*Lindsay Patrick Henry*  
Councilman

*Corinne DiSomma*  
Receiver of Taxes

*Carol A. Quirk*  
Town Clerk

the Town's funds when varying budgetary needs change (from cutting tax rates when the Town has sufficient reserves to raising new revenues when the need occurs).

While we have been largely successful in achieving these goals, they have only occurred with the benefit of long term planning that has stretched the Town's planning horizon to five and in some instances more than ten years. Part of our comments on the Draft Report detailed below necessarily touches on the friction between the need for this long term planning and the relatively small window of results reviewed in the Draft Report. We believe that some of the conclusions reached in the Draft Report do not take into account the wisdom and benefit of longer term planning that can help smooth the vicissitudes of radically changing macro economic conditions (e.g., the negative pressures exerted as a result of the recent recession and the massive swings in revenues generated from mortgage taxes). The commentary below attempts to provide a broader context which hopefully can illuminate and clarify the budgetary actions taken by the Town Board in managing the Town's finances and specifically counter any notion that the Board is not in complete control of its budgetary planning.

While recognizing that there is always opportunity for the Town to improve upon its budgetary management, we would like to note that the Town's success in achieving its goals are best exemplified by:

1. The Town's credit rating from Moody's being upgraded on five separate occasions over the past decade, going from a precarious Baa3 to a remarkable Aa2 (and to AA+ by Standard & Poor's);
2. The Town's cumulative fund balance (and fund balances within each of the major Town funds) has gone from precarious deficits to well within the targets set by the Town Comptroller and the Town Board;
3. The significant reduction in labor costs driven by far less full time equivalent employees on staff (from 650 full time employees in 1995 to 328 today);
4. The successful re-negotiation of the Town's major labor contracts that requires for the first time in modern history employee contributions to health insurance premiums and lower starting salaries for new employees and smaller step increases within job titles;
5. The significant reduction in bonded indebtedness and an associated reduction in debt service obligations (the Town's outstanding indebtedness is over \$35 million less today than ten years ago); and
6. The Town's early success at redeveloping the Downtown Wyandanch community and the significant first phase of shifting the ambitious project from public to private financing (i.e., the Town's capital investment in the community centered around acquiring

October 10, 2013

Mr. Ira McCracken, Chief Examiner

RE: OSC Draft Report of Examination: Town of Babylon, New York

Page 3

---

properties and constructing a sewer line is now essentially complete and future development costs are borne by the Master Developer with private funding).

All of these representations of the Town's recent financial improvement point to a Town Board that is constantly focused on its budgetary needs and consumed with responding quickly and aggressively to meet new economic challenges. Over the past 10 to 15 years, the Town Board's proactive budgetary planning has greatly reduced the risk to its taxpayers and has paved the way for a future that builds on smoothing the impact of outside budgetary fluctuations.

Finally, while the Draft Report focuses primarily on the Town's General Fund, the Town Board recognizes that it accounts for only one-third of the Town's total budget and that the Board's custodial obligations for managing its complicated budget extends to all funds including the two critical garbage improvement funds which, together, are larger than the General Fund.

See  
Note 1  
Page 35

Below are the Town's specific comments on the Draft Report.

1. EXECUTIVE SUMMARY

- 1<sup>ST</sup> ¶, last sentence: The Town Comptroller does not oversee the functions of the Town's health insurance program.

See  
Note 2  
Page 35

**Audit Results:** We disagree with or take exception to the following comments:

- *“The Board has not taken appropriate actions to maintain the general fund's sound financial condition.”* [First sentence of section.]
- *“This [General Fund fund balance] decline resulted from adopting budgets that were not structurally sound...”* [Second sentence of second paragraph of section.]
- *“Because of these practices, the Board cannot ensure that the Town is in sound financial condition.”* [Last sentence of second paragraph of section.]
- *“The Town only allocated administrative charges to its residential garbage district fund and commercial garbage district fund. This allocation method created taxpayer inequities.”* [First and second sentences of third paragraph of section.]
- *“We did not include the Town's 2012 financial information as part of our review because the information included in the Town's 2012 annual update document submitted to OSC was unreliable and the Town's 2012 independently audited financial statements were not completed – and were therefore unavailable – during our audit.”* [Footnote 2 of Executive Summary.]

See  
Note 3  
Page 35

We respectfully draw OSC’s attention to the recent history of the General Fund’s year end fund balance summarized in the table below:

<b>TOWN of BABYLON</b>								
<b>RESULTS of OPERATIONS: GENERAL FUND<sup>1</sup></b>								
	2005	2006	2007	2008	2009	2010	2011	2012
Beg. Fund Balance	\$9,024,714	\$11,151,317	\$15,325,301	\$16,648,129	\$11,961,512	\$7,341,386	\$5,979,786	\$15,918,266
Revenues	44,406,149	46,369,796	45,260,389	40,621,824	39,504,765	39,706,168	46,773,948	48,623,589
Expenses	(40,370,981)	(42,195,813)	(44,294,811)	(45,458,828)	(44,445,620)	(41,625,725)	(45,107,396)	(46,475,985)
Other Financing Uses	1,908,565	N/A	357,250	150,388	320,729	557,957	(178,072)	3,654,907
Results of Operations	2,126,603	4,173,984	1,322,828	(4,686,616)	(4,620,126)	(1,361,600)	1,488,480	5,802,511
<b>Ending Fund Balance</b>	<b>\$11,151,317</b>	<b>\$15,325,301</b>	<b>\$16,648,129</b>	<b>\$11,961,512</b>	<b>\$7,341,386</b>	<b>\$5,979,786</b>	<b>\$15,918,266</b>	<b>\$21,720,777</b>
Fund Bal. as % of Expenses	26.4%	36.3%	37.6%	26.3%	16.5%	9.5%	35.3%	46.7%

<sup>1</sup> Source: Independent, certified audited financial statements.

See Note 4  
Page 35

All other independent reviews of the Town’s finances – whether by independent certified public accountants or outside credit rating agencies like Moody’s Investors Service or Standard & Poor’s – have reached considerably different conclusions about the Town’s condition and management of its budget and finances. Indeed in its recent (August 2013) review of the Town’s finances, Moody’s states, *“The Aa2 rating reflects the Town’s historically strong Operating Funds despite recent declines...”* And, *“Moody’s believes the Town’s financial position will remain stable given its conservative budgeting practices and sound fiscal policies... The Town’s General Fund has ample liquidity, with cash balance at \$16.1 million... 2012 financial statements show the Operating Fund balance will remain stable at approximately \$55.7 million, largely the result of the General Fund’s improvements... fiscal 2012 results indicate that these fund reserves have declined in step with management’s expectations.”*

In its August 13, 2013 review of the Town’s finances and credit, Standard & Poor’s (in giving the Town a credit rating of AA+, one of the highest on Long Island) states, *“The...rating reflects our opinion of Babylon’s strong finances and interfund liquidity, with good financial management practices.”* And *“we believe Babylon’s financial position is strong, despite the negative unassigned fund balance in its general fund. We attribute the deficit to governmental accounting standards board (GASB) rules governing economic development activities related to the town’s general fund investment in the Wyandanch Rising project... We understand that while classified as restricted or nonspendable, the balances may be used for liquidity or debt service, and are not restricted on a budgetary basis of accounting. In addition, the town in our opinion maintains healthy reserves across its major operating funds, providing it with additional liquidity. Unrestricted governmental cash totaled \$71 million at 2012 year-end... which we consider very strong.”*

While we understand that several of the comments cited above from credit rating agencies include results of operations outside of the period covered in the Draft Report (specifically referencing the fiscal year 2012 independent audit), the OSC report is in draft form and we

See Note 5  
Page 36

October 10, 2013

Mr. Ira McCracken, Chief Examiner

RE: OSC Draft Report of Examination: Town of Babylon, New York

Page 5

---

believe it would be short-sighted and not representative of the Town's financial condition to ignore reference to what is now the completed certified audit of the Town for 2012. Because of the Town's expanded planning horizon discussed above, many of the comments contained in the Draft Report are rendered moot upon review of the 2012 audit results and we encourage the OSC to include results of operations from 2012 in its Tables 1 and 2 of the Draft Report.

See  
Note 5  
Page 36

During the course of the OSC audit, the Town explained in detail the historic budgetary goals and objectives that have guided it through the fiscal years covered by the Draft Report (and that extend to the current fiscal year). Specifically, the Town has adhered to its articulated goal of having its major funds (General, Combined Highway and the two Garbage District funds) maintain a *minimum* fund balance of between 15 and 25 percent of annual expenditures. Additionally, the Town has responded to repeated written recommendations from the OSC in numerous reports associated with Chapter 448 of the Laws of 1999 regarding deficit financing to "spend down" its surpluses in certain funds. The Town's very deliberate and publicly-stated, multi-year efforts to reduce the General Fund surplus – which has been very successful – seems to belie the OSC conclusions in the Draft Report.

See  
Note 6  
Page 36

See  
Note 7  
Page 36

In its November 6, 2007 report to the Town concerning the Town's fiscal year 2008 Preliminary Budget (Report Number B8-7-22), the OSC states:

*Town Law allows the Town to retain a reasonable amount of unappropriated unreserved fund balance for each fund that is consistent with prudent budgeting practices, and is necessary to ensure the orderly operation of the government and the continued provision of services. While the maintenance of a reasonable fund balance can represent a measure of a municipality's financial health and a cushion against unexpected occurrences, the portion of fund balance that is not reserved for a specific purpose should be considered as a financing source to support operations in the subsequent year. Therefore, governing boards should establish thresholds defining the retention of a reasonable amount of fund balance for each fund so that when the board prepares the preliminary budget for the ensuing fiscal year, it can consider fund surplus and the projected current year's operating surplus, if any, as a funding source.*

See  
Note 8  
Page 36

*The Board should take action to reduce the amount of unreserved fund balance to a reasonable level by either appropriating fund balance to reduce the real property tax levy in the ensuing year's budget or by establishing legal reserves as provided by law...the Board should appropriate a portion of fund balance in adopted budgets to finance operations.* [Emphasis added.]

Again in its October 31, 2008 report on the Town's 2009 Preliminary Budget (Report Number B7-8-22), the OSC used identical language to recommend the Town reduce its General Fund

fund balance (among other funds) and incorrectly stated that, “In 2004, the Town adopted a written policy indicating it would maintain a fund balance of 20 to 25 percent of the next year’s budget.” While the Town Comptroller, in coordination with the Town Board, has targeted a goal of achieving a *minimum* fund balance of between 15 and 25 percent of fund expenses for each of its major funds, the OSC has misrepresented this to be i) a resolution adopted by the Town Board *requiring it* to maintain this fund balance; and ii) that in certain instances when the fund balance exceeds these values the Town has somehow violated its own directive. Specifically, in this same report, the OSC incorrectly paraphrases the Town’s fund balance policy by stating, “The Board should reduce the amount of unreserved fund balance in all these funds to within 20 to 25 percent of the 2009 budgeted appropriations, as required by its policy, by using the fund balance to pay one-time costs, reducing debt, establishing legal reserves for known future costs or by reducing the real property tax levy in the ensuing year’s budget.” [Emphasis added.] These are simply incorrect representations of the Town goal regarding fund balance and, once corrected, would not lead to the conclusion that the Town somehow manages its General Fund in an unsound financial condition.

See  
Note 9  
Page 37

Finally, in its November 9, 2009 report to the Town (Report Number B7-9-28), the OSC again recommends a reduction in fund balance and again mischaracterizes Town goal by stating, “In 2004, the Town Board established a written policy limiting the amount of fund balance retained in each fund to 20 to 25 percent of total expenditures.” And later in the same report the OSC states, “...the fund balance retained in each of these three funds at the end of 2008 fiscal year was also over the limit established by Board [sic].” [Emphasis added.] So what was stipulated by the Town Comptroller and Town Board as a goal developed in response to stinging criticism from the credit rating agencies (namely that the Town needed to substantially *increase* its fund balances in order to achieve better credit ratings thereby lowering its borrowing costs) is being construed by the OSC as a policy that was designed to *limit* the Town’s fund balances; this is simply an incorrect characterization.

See  
Note 10  
Page 37

We belabor this point because its misunderstanding is informing the conclusions of the Draft Report and we believe a proper understanding of the Town goal on fund balance would yield substantially different conclusions. Based on these recent OSC recommendations, this is exactly what the Town has done and yet it seems to now be generating almost the complete opposite recommendation from the OSC.

See  
Note 11  
Page 37

For your information, during the period covered by the Draft Report and in subsequent periods, the Town has used surplus fund balances to i) materially reduce taxes to residents and businesses; ii) substantially mitigate its need to incur costly bonded debt by funding myriad capital projects; and iii) respond aggressively to the devastation of Superstorm Sandy by expending in excess of \$17 million to help residents and businesses recover and to secure and repair revenue-generating Town facilities such as its beaches, parks, marinas and pools. Without the financial flexibility afforded these fund surpluses, the Town simply would not have had the critical resources available to provide for its citizens and businesses.

The issues regarding interfund transfers and the potential for taxpayer inequalities is addressed in greater detail below, under the heading “Administrative Charges.” However, notwithstanding that, pursuant to the OSC recommendation in the Draft Report, all temporary interfund advances will be authorized in the same manner as a budget transfer, via Town Board resolution. The corrective action plan will incorporate this element as well as address the other recommendations presented.

## 2. FINANCIAL CONDITION

We disagree with or take exception to the following comments:

- *“The Board has not taken appropriate actions to maintain the general fund’s sound financial condition.”* [First sentence of third paragraph of section.]
- *“This decline resulted from adopting budgets that were not structurally sound...”* [Second sentence of fourth paragraph of section.]
- Table 1, General Fund – Classification of Fund Balance. [Table contained within the “Unexpended Surplus Fund Balance” sub-section.]
- *“According to Town officials, the non-cash loan reductions aggregating almost \$5.4 million consist of various inter-fund transactions, which Town officials characterized as the ‘netting’ of inter-fund activities between the general fund and the RGD fund at year end.”* [First sentence of fourth paragraph of “Inter-Fund Loans” sub-section.]
- *“This [the General Fund’s unexpended fund balance decrease] resulted from adopting budgets that were not structurally sound and from reclassifying fund balance from unexpended to restricted and nonexpendable to reflect the Town’s investment in property held for resale, which is not liquid or available to fund operations.”*
- Table 2, General Fund – Results of Operations. [Table contained within the “Budgeting Practices” sub-section.]
- *“1. The Board should develop a long-term financial plan to mitigate the negative impact of its recurring operating deficits and to eliminate deficit fund balances.”* [First numbered paragraph in the “Recommendations” sub-section.]
- *“2. The Board should adopt budgets that are structurally balanced. Recurring revenues should be reasonably estimated and attainable, and sufficient to cover the cost of recurring expenditures.”* [Second numbered paragraph in the “Recommendations” sub-section.]

With respect to the Draft Report’s characterization of the financial condition and adoption of budgets as not structurally sound, the Town respectfully submits that this conclusion is not in



October 10, 2013

Mr. Ira McCracken, Chief Examiner

RE: OSC Draft Report of Examination: Town of Babylon, New York

Page 8

---

keeping with the trends illustrated in Table 2 of the Draft Report. As detailed in Table 2, after the economic crisis late in 2008 and through 2011, the Town was quick to react and effectively limit the use of fund balance in fiscal year 2010. The Town budgeted \$1.687 million in that year but only applied \$1.362 million. This audit period, as annotated on Page 10 of the Draft Report, includes within its scope a dramatic undertaking by the Board to revitalize the hamlet of Wyandanch for the better of the Town in particular and Suffolk County as a whole. This project involved certain GASB-stipulated accounting treatments which, when applied, may have caused the Town's financial position to appear tentative. The Town utilized alternate funding (cash loans) for the Wyandanch project until it issued – or will issue – general obligation bonds or bond anticipation notes, thus delaying the issuance of debt for the properties purchased and avoiding the debt burden on the Town's taxpayers. Please be advised that, as of May 31, 2013, all outstanding loans from the Residential Garbage District to the General Fund have been repaid. We feel that if the Wyandanch project had been isolated and if the economic crisis had not occurred, it would be clear that the Town is and has been on sound financial footing.

See  
Note 12  
Page 37

### 3. ADMINISTRATIVE CHARGES

We disagree with or take exception to the following comments:

- *“Instead, the allocation method is based on the relative percentage of the various funds’ adopted budgets and bears no relationship between the services provided, if any, and the cost of those services.”* [Second sentence of fourth paragraph of section.]
- *“When Town officials allocate administrative charges without using a reasonable allocation method, the Town may be either over-charging or under-charging for such services. In either case, using an inappropriate cost allocation method created an inequity because one fund was benefiting at the expense of the other fund.”* [First sentence of seventh paragraph of section.]

We agree and accept the Draft Report's conclusion (numbered paragraph 8 on page 18 of the Draft Report) that states, “The Board should review the administrative charges allocated to the [garbage district] funds and *determine whether they represent a legitimate cost* of general fund services provided to these funds.” However, that OSC recommendation contradicts the apparent conclusion reached earlier in the Draft Report that the allocation methodology “created an inequity” and that “[t]his allocation method created taxpayer inequities.” In our opinion, it is premature for the Draft Report to make that determination prior to the Town following the report's recommendation to evaluate the methodology and make certain the allocation is correct. We respectfully request that the report modify these findings to indicate that the Town's current method may cause an inequity or that “this allocation method may create taxpayer inequities.”

See  
Note 13  
Page 38

The Town will review the Administrative Charges allocated to the other funds and determine whether they are representative of General Fund services provided. If at that time our results

October 10, 2013

Mr. Ira McCracken, Chief Examiner

RE: OSC Draft Report of Examination: Town of Babylon, New York

Page 9

---

indicate the Town's methodology is not representative of services provided, the review results and allocation method to be implemented will be outlined in the Corrective Action Plan.

4. HEALTH INSURANCE BENEFITS

This finding addresses the concern that nine individuals who received health insurance benefits did so without Board authorization. Please be advised that on November 15, 2012 resolutions were adopted and are attached here for your review.

See  
Note 14  
Page 38

The Town Board has always considered elected officials as Administrative for purposes of health insurance eligibility under the Town Code. The Town Code, Article 47-15, Health Insurance, is being specifically amended to include elected officials.

See  
Note 15  
Page 38

Regarding the Town's health insurance buy-out procedures, all payments were calculated correctly. However the Town Code did not reflect this practice which is being updated to include the provisions for elected officials as noted above. Attached for your information is the pending amendment.

5. LABOR CONSULTANT

Since the completion of the OSC Draft Report, the Town's Personnel Department has been placed under the authority of the Department of Town Comptroller. This move was codified by adoption of Resolution No. 115, February 2013, and is now part of the Town Code. Please see the attached resolution as well as a print out of the pertinent Town Code section. As a result of this change, the Labor Consultant functions are limited to advisory only to the Chief of Staff and Town Comptroller.

6. INFORMATION TECHNOLOGY

This area of the audit findings will be addressed as part of the Corrective Action Plan, to be submitted in accordance with the requirements of the OSC. As you are aware, some of these policies exist, but need further refinement and will be presented as part of the Corrective Action Plan.

We look forward to discussing these comments with you and to preparing the Town's Corrective Action Plan. In the meantime, if you have any questions or comments concerning this, please do not hesitate to contact me at your earliest opportunity.

Sincerely,

Richard Schaffer, Town Supervisor

October 10, 2013

Mr. Ira McCracken, Chief Examiner

RE: OSC Draft Report of Examination: Town of Babylon, New York

Page 10

---

Enclosures

VM:dj

cc: Victoria Marotta, Town Comptroller  
Joseph Wilson, Town Attorney  
Members of the Town of Babylon Town Board

## APPENDIX B

### OSC COMMENTS ON THE TOWN'S RESPONSE

#### Note 1

During our initial assessment of the Town's fiscal trends, we determined that the Town was in the process of spending down unexpended surplus fund balance in the CGD fund and concluded that this fund should not be included in the scope of our examination. We did initially consider including the RGD fund in our audit scope and met with the Town Comptroller and the Town's independent accountant to discuss excessive fund balance retained in the RGD fund. They explained that the Town intended to gradually spend down the fund balance over time by annually appropriating a significant amount to fund the ensuing years' budgets, thereby reducing the fund balance to a reasonable level. Since the Town's explanation appeared reasonable, and after considering that 37 percent of the RGD's fund balance at December 31, 2011, had been designated as nonspendable (due to the unpaid \$8.3 million cash advances owed by the general fund at December 31, 2011), we did not include the RGD fund in our audit.

#### Note 2

Town officials provided us with the amended Town Code that places the health insurance program under the authority of the Town Comptroller, effective February 19, 2013. We revised our report to include a footnote indicating that, prior to February 19, 2013, the Supervisor oversaw the functions of the Town's health insurance program.

#### Note 3

Town officials offered this vague list of disagreements that neglects to address the specific issues detailed in our draft report. By not presenting us with any specific information that addresses our findings, Town officials have not provided us with any specific data which indicates that our findings or conclusions are incorrect.

#### Note 4

The table included in the Town's response, presented as certified by the Town's independent accountant, is misleading because it gives the false impression that the total ending fund balance is expendable and, therefore, available to fund current operations. Our review of results of operations and evaluation of fund balance is not limited to total fund balance. Instead, it focuses on each of the fund balance components, with greater emphasis on the unexpended<sup>19</sup> portion which is unencumbered, liquid, and available to fund current operations. Table 1 of our report shows each component of fund balance that aggregates to – and agrees with – the total fund balance shown on the table presented in the Town's response for fiscal years 2008 through 2011.

<sup>19</sup> Town Law allows the Town to retain a reasonable amount of unexpended surplus fund balance to provide for cash flow and unexpected contingencies that may occur in future periods. Therefore, Town officials should set or calculate those reasonable levels or range of levels based on the Town's current financial position, its imminent cash flow needs, unexpected contingencies, or other events that may reasonably impact the Town's ability to meet its obligations.

Our draft report also explains that the general fund's unexpended fund balance decreased from a surplus of \$6.1 million at December 31, 2008, to a deficit of \$10.5 million at the end of 2011. This decrease was mainly due to the application of Generally Accepted Accounting Principles for the acquisition of capital assets (such as land) that was held for resale, which placed restrictions on unexpended surplus fund balance. The recurring annual operating deficits sustained during this period, as shown on Table 2 of our report, resulted from adopting annual budgets that were not structurally balanced. Negative results of operations contributed to the increase in the unexpended/unassigned fund balance deficit.

#### Note 5

Our audit scope was limited to the period January 1, 2011, to July 31, 2012, with the exception of analyzing certain aspects<sup>20</sup> of financial condition for the period January 1, 2008, through September 30, 2012. Our field work ended before the Town completed and filed its annual update document for the 2012 fiscal year and before the audited financial statements for that year had been issued. Therefore, we did not evaluate the Town's financial condition for the fiscal year ended December 31, 2012.

#### Note 6

During our audit, Town officials did not provide us with a record of any detailed explanation of the "historic budgetary goals and objectives" that guided them through the fiscal years covered by our report. We gathered background information to support our audit findings and confirm the bonding authorization for the Wyandanch revitalization project. In addition, Town officials provided verbal historical prospective and explanations on why the Wyandanch revitalization initiative, undertaken in 2008 by the prior Supervisor, was necessary to revitalize the local economy. We also met with the Town Comptroller and the Town's independent accountants to discuss the excessive levels of unexpended surplus fund balance maintained in the RGD fund, and the accounting treatment for the purchase of the real property related to the Wyandanch project.

#### Note 7

Pursuant to Chapter 448 of the Laws of 1999, the State Legislature authorized the Town to issue \$9.8 million in bonds to liquidate various fund deficits for the fiscal year ending December 31, 1998. In accordance with that law, we reviewed the annual preliminary budget for fiscal years 2002 through 2010 and reported our results to the Town. Throughout this period, the Town only submitted written responses to our review of the 2005 and 2006 preliminary budgets. Neither of the two budget review letters contained comments on reasonable levels of fund balance because, at that time, the Town was in the process of building up, rather than spending down, fund balance. Similarly, neither of the Town's responses addressed, nor commented on, fund balance issues.

#### Note 8

The reference to Town Law regarding the retention of a reasonable level of unexpended surplus fund balance in our 2008 budget review letter stemmed from the fact that the Town's financial position had increased substantially. The Town projected a fund balance of \$18.3 million on December 31, 2007

<sup>20</sup> The aspects of financial condition were limited to an update of cash advance balances, as of September 2012, that the general fund still owed the RGD fund.

for the general fund, which was more than 41 percent of the preliminary 2008 budget appropriations. The Garbage Improvement District fund balance was predicted to reach \$25.3 million by December 31, 2007, and the CGD Fund balance was projected to be \$7.8 million by the end of 2007, which represented more than 29 percent of the preliminary 2008 budget appropriations. Because of these significant accumulations of unexpended surplus fund balances in the above funds, we felt that it was appropriate at the time to suggest that the Town maintain reasonable levels of fund balance in accordance with provisions of Town Law.

#### Note 9

In 2008, Town officials provided us with documentation indicating that such a fund balance policy was implemented, and we acknowledged their good efforts in our budget review letter issued on October 31, 2008. It was our understanding that the Interoffice Memorandum dated January 23, 2004, (see Appendix C), represented Town policy. At no time during our review of the 2009 budget, or at the exit discussion, did Town officials object to our characterization of the 2004 Memorandum as a “written policy.”

#### Note 10

Town officials did not bring this to our attention in 2009 while we were conducting our budget review, did not mention any inconsistencies, misunderstandings, or misstatements of facts at the exit conference, and did not raise the issue after the budget review letter had been released. Had they identified this concern at any time during or soon after our review, we could have further discussed and addressed this issue. The substance and essence of the findings and recommendations in our November 9, 2009 budget review letter are consistent with the Town’s “written policy,” as represented to us in the January 23, 2004 Memorandum.

#### Note 11

We had no misunderstandings about Town officials’ intent when they presented the January 23, 2004 Memorandum regarding fund balances. There are no inconsistencies between what we said in the past and what we are reporting in this draft audit report. Further, Town officials’ long recitation on this issue, combined with their omission of the 2004 Memorandum from their response, is an attempt to exaggerate a minor incorrect reference made in our prior budget review and confuse the issues raised in our current draft report. Once again, Town officials did not address any of the specific issues and recommendations presented in our draft report either at the exit conference or in their written response.

#### Note 12

The utilization of “alternate funding” (cash advances or loans) on a temporary basis to bolster a fund’s liquidity is a common practice used by local governments. However, such practice is only permissible when certain legal requirements are met. General Municipal Law requires that the Board approves all temporary loans in advance, that the cash advances be repaid no later than the end of the fiscal year and, in certain instances, that the repayment must include interest. As stated in our draft report, the Town did not meet those legal conditions for the loans.

### Note 13

Town officials had ample time to evaluate and correct the methodology for allocating service charges to other funds on a cost basis or in an equitable manner. This issue also was addressed in a prior audit report (96M-117), issued on July 12, 1996. In that report, we made a recommendation regarding analyzing services provided by Town departments to the garbage improvement district to determine the appropriate costs to be allocated to the district. Town officials did not implement the recommendation made in the prior report and chose to continue using the questionable methodology without adequately considering the interests of the taxpayers being billed for those charges. The current methodology being used by the Town to allocate administrative costs is not equitable and does not meet the service cost allocation criteria as recommended by the Office of Management and Budget (OMB) Circular A-87: Cost Principles for State, Local and Indian Tribal Governments.

### Note 14

Town officials included attachments to their response showing that the Board adopted individual resolutions on November 15, 2012, granting eight part-time employees health insurance benefits effective on their respective dates of employment, which, in one instance, goes back to January 1, 1998. None of the resolutions provided were certified by, or displayed the official seal of, the Town Clerk.

### Note 15

Unless otherwise provided by law, Town officials may not grant health insurance benefits or payments in lieu of health insurance to elected officials. The Town's response included a resolution adopted on October 1, 2013, scheduling a public hearing in reference to amending Chapter 47 of the Town's Code. This proposed amendment includes elected officials as eligible to receive health insurance benefits and payments in lieu of health insurance in the same manner, and on the original effective dates, as administrative employees.


## APPENDIX C

### TOWN'S INTEROFFICE MEMORANDUM DATED JANUARY 23, 2004

Town of Babylon

#### Interoffice Memorandum

TO: All Commissioners/Department Heads

FROM: Victoria Marotta, Director of Finance 

SUBJECT: Policy Regarding Fund Balances

DATE: January 23, 2004

CC: Steve Bellone, Supervisor  
Ron Kluesener, Chief of Staff

---

As you are aware, it is the policy of the Town Supervisor, Steven Bellone, to insure that all fund balances as a percent of total expenses attain and remain at 20-25 percent. As a result of this expectation, we are implementing this into written policy for the Town of Babylon as of the date above. Should you have any questions or concerns, please feel free to contact me at X3043. Thanks for your time and assistance.

Commissioners/Elected Officials/Department Heads:

John Miller  
Constance Davis  
Peter Casserly  
Pat Kaphan  
Dennis Cohen  
Corrine DiSomma  
Nancy Delaney  
Janice Colbert  
Philip Berdolt  
Gil Hanse  
Mike Costanza  
Patrick Farrell  
Victoria Russell



## APPENDIX D

### AUDIT METHODOLOGY AND STANDARDS

Our overall goal was to assess the adequacy of the internal controls put in place by the Board and Town officials to safeguard Town assets. 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. Our initial assessment included evaluations of the following areas: financial condition, Town Clerk's office, capital projects, cash management, purchasing, claims processing, payroll and personal services, real property tax procedures, information technology, records and reports, highway services, and residential and commercial garbage collection services.

During the initial assessment, we interviewed appropriate Town officials, performed limited tests of transactions, and reviewed pertinent documents, such as the Town policies and procedures manual, Board minutes, and financial records and reports. In addition, we obtained information directly from the computerized financial databases and then analyzed it electronically using computer-assisted techniques. This approach provided us with additional information about the Town's financial transactions as recorded in its databases. Further, we reviewed the Town's internal controls and procedures over the computerized financial databases to help ensure that the information produced by such systems was reliable.

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 on the reported objectives and scope by selecting for audit those areas most at risk. We selected financial condition, administrative charges, health insurance benefits, the duties of a labor consultant, and information technology for further audit testing.

To determine if the Board and Town officials had properly designed and implemented internal controls over financial condition areas, we extended our scope back to January 1, 2008, and forward through September 30, 2012, and:

- Made inquiries of Town officials and the Town's independent accountants
- Reviewed Town budgets and results of operations for the general fund from the 2008 through 2011 fiscal years as reported in the Town's audited financial statements
- Reviewed inter-fund loan activities between the general fund and the residential and commercial garbage districts funds
- Reviewed financial records, general ledger transaction reports, and bank statements to determine if inter-fund loan balances were recorded accurately
- Reviewed the Town's schedule of properties held for resale related to the Wyandanch Revitalization project to determine how the properties were acquired and to verify that the land was recorded and reported accurately in the Town's audited financial statements

- Interviewed Town officials and the Town Clerk to ascertain whether the Board authorized the temporary cash advances from the residential and commercial garbage districts funds to the general fund.

To determine if general fund administrative charges were allocated to other funds based upon the cost of actual services or a generally accepted cost allocation method, we extended the scope to include the 2010 fiscal year and we:

- Interviewed Town officials regarding the methodology used to compute administrative charges to other funds
- Reviewed the Town's administrative charges allocation schedules to determine how administrative charges were calculated, and whether the allocation method was generally accepted and consistently applied
- Reviewed the Office of Management and Budget (OMB) *Circular A-87: Cost Principles for State, Local and Indian Tribal Governments* to identify best practices or generally accepted methods for allocating overhead costs across multiple funds and departments
- Reviewed audited financial statements to determine whether Town officials allocated administrative changes to all funds included in the cost allocation schedule.

To determine if the Board provided health insurance benefits to only eligible current and former employees, we:

- Reviewed the Town's collective bargaining agreements and salary administrative plan to determine which employees and Town officials were eligible to receive health insurance benefits
- Compared the list of elected officials, Board members, and administrative, blue collar, white collar, and contract hourly employees to the Town's May 2012 health insurance report and the 2011 health insurance buyout report to determine if the Town provided health insurance benefits to ineligible employees.

To determine if the Board and Town officials had properly designed and implemented internal controls over duties performed by a labor consultant, we:

- Reviewed the contract agreement between the Town and the consultant to determine the extent of services and duties he was hired to perform
- Interviewed Town officials and employees to determine the duties performed by the Director of Labor Relations while he was holding that office and the duties he later performed after retiring and being rehired as a consultant
- Reviewed interoffice memorandums and Board resolutions to determine when the Director of Labor Relations left Town employment and was rehired as a consultant.

We examined the Town's financial operations, records and reports, and its design of controls over IT for the period January 1, 2011, to July 31, 2012. To accomplish the objectives of this audit and obtain valid audit evidence, we:

- Interviewed relevant Town officials and personnel, and documented our observations of the computerized data system
- Reviewed Town policies and procedures related to computer use, IT, and system security
- Reviewed user permission reports and compared user access privileges to users' job responsibilities.

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.

**APPENDIX E**  
**HOW TO OBTAIN ADDITIONAL COPIES OF THE REPORT**

To obtain copies of this report, write or visit our web page:

Office of the State Comptroller  
Public Information Office  
110 State Street, 15th Floor  
Albany, New York 12236  
(518) 474-4015  
<http://www.osc.state.ny.us/localgov/>

**APPENDIX F**  
**OFFICE OF THE STATE COMPTROLLER**  
**DIVISION OF LOCAL GOVERNMENT**  
**AND SCHOOL ACCOUNTABILITY**

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

**LOCAL REGIONAL OFFICE LISTING**

---

**BINGHAMTON REGIONAL OFFICE**

H. Todd Eames, Chief Examiner  
Office of the State Comptroller  
State Office Building - Suite 1702  
44 Hawley Street  
Binghamton, New York 13901-4417  
(607) 721-8306 Fax (607) 721-8313  
Email: [Muni-Binghamton@osc.state.ny.us](mailto:Muni-Binghamton@osc.state.ny.us)

Serving: Broome, Chenango, Cortland, Delaware,  
Otsego, Schoharie, Sullivan, Tioga, Tompkins Counties

**BUFFALO REGIONAL OFFICE**

Robert Meller, Chief Examiner  
Office of the State Comptroller  
295 Main Street, Suite 1032  
Buffalo, New York 14203-2510  
(716) 847-3647 Fax (716) 847-3643  
Email: [Muni-Bufferalo@osc.state.ny.us](mailto:Muni-Bufferalo@osc.state.ny.us)

Serving: Allegany, Cattaraugus, Chautauqua, Erie,  
Genesee, Niagara, Orleans, Wyoming Counties

**GLENS FALLS REGIONAL OFFICE**

Jeffrey P. Leonard, Chief Examiner  
Office of the State Comptroller  
One Broad Street Plaza  
Glens Falls, New York 12801-4396  
(518) 793-0057 Fax (518) 793-5797  
Email: [Muni-GlensFalls@osc.state.ny.us](mailto:Muni-GlensFalls@osc.state.ny.us)

Serving: Albany, Clinton, Essex, Franklin,  
Fulton, Hamilton, Montgomery, Rensselaer,  
Saratoga, Schenectady, Warren, Washington Counties

**HAUPPAUGE REGIONAL OFFICE**

Ira McCracken, Chief Examiner  
Office of the State Comptroller  
NYS Office Building, Room 3A10  
250 Veterans Memorial Highway  
Hauppauge, New York 11788-5533  
(631) 952-6534 Fax (631) 952-6530  
Email: [Muni-Hauppauge@osc.state.ny.us](mailto:Muni-Hauppauge@osc.state.ny.us)

Serving: Nassau and Suffolk Counties

**NEWBURGH REGIONAL OFFICE**

Tenneh Blamah, Chief Examiner  
Office of the State Comptroller  
33 Airport Center Drive, Suite 103  
New Windsor, New York 12553-4725  
(845) 567-0858 Fax (845) 567-0080  
Email: [Muni-Newburgh@osc.state.ny.us](mailto:Muni-Newburgh@osc.state.ny.us)

Serving: Columbia, Dutchess, Greene, Orange,  
Putnam, Rockland, Ulster, Westchester Counties

**ROCHESTER REGIONAL OFFICE**

Edward V. Grant, Jr., Chief Examiner  
Office of the State Comptroller  
The Powers Building  
16 West Main Street – Suite 522  
Rochester, New York 14614-1608  
(585) 454-2460 Fax (585) 454-3545  
Email: [Muni-Rochester@osc.state.ny.us](mailto:Muni-Rochester@osc.state.ny.us)

Serving: Cayuga, Chemung, Livingston, Monroe,  
Ontario, Schuyler, Seneca, Steuben, Wayne, Yates Counties

**SYRACUSE REGIONAL OFFICE**

Rebecca Wilcox, Chief Examiner  
Office of the State Comptroller  
State Office Building, Room 409  
333 E. Washington Street  
Syracuse, New York 13202-1428  
(315) 428-4192 Fax (315) 426-2119  
Email: [Muni-Syracuse@osc.state.ny.us](mailto:Muni-Syracuse@osc.state.ny.us)

Serving: Herkimer, Jefferson, Lewis, Madison,  
Oneida, Onondaga, Oswego, St. Lawrence Counties

**STATEWIDE AUDITS**

Ann C. Singer, Chief Examiner  
State Office Building - Suite 1702  
44 Hawley Street  
Binghamton, New York 13901-4417  
(607) 721-8306 Fax (607) 721-8313