



City of Lockport

Fiscal Stress

Report of Examination

Period Covered:

January 1, 2012 — October 9, 2013

2013M-330



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

December 2013

Dear City 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 Common Council 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 City of Lockport, entitled Fiscal Stress. This audit was conducted pursuant to Article V, Section 1 of the State Constitution and the State Comptroller's authority as set forth in Article 3 of the General Municipal Law.

This audit's results and recommendations are resources for local government officials to use in effectively managing operations and in meeting the expectations of their constituents. If you have questions about this report, please feel free to contact the local regional office for your county, as listed at the end of this report.

Respectfully submitted,

*Office of the State Comptroller
Division of Local Government
and School Accountability*

Introduction

Background

The City of Lockport (City) is located in Niagara County. It is approximately 8.4 square miles and serves approximately 21,100 residents. The elected Common Council (Council) is the legislative body responsible for managing City operations, including establishing internal controls over financial operations and for maintaining sound financial condition. The Mayor is a member of the Council and serves as the City's chief executive officer. The Mayor ensures that any legislation adopted by the Council is implemented. The elected City Treasurer (Treasurer), as chief financial officer, oversees accounting and financial reporting controls, supervises the preparation of accounting records, produces financial reports and ensures compliance with various State and Federal laws.

As of October 2013, the City had 240 employees. The City's budgeted appropriations for the 2013 fiscal year are approximately \$32 million,¹ which are funded primarily with real property taxes, sales tax and State aid. The City provides services for its residents including police and fire protection, public works, recreation, water, sewer, refuse collection and general government support.

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

Objective

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

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

¹ \$22.5 million in the general fund, \$4 million in the water fund, \$4.2 million in the sewer fund and \$1.2 million in the refuse fund

**Scope and
Methodology**

We examined the City’s financial condition for the period January 1, 2012 through October 9, 2013.

We conducted our audit in accordance with generally accepted government auditing standards (GAGAS). More information on such standards and the methodology used in performing this audit are included in Appendix C of this report.

**Comments of
Local Officials and
Corrective Action**

The results of our audit and recommendations have been discussed with City officials and their comments, which appear in Appendix A, have been considered in preparing this report. Except as specified in Appendix A, City officials generally agreed with our recommendations and indicated they planned to take corrective action. Appendix B includes our comments on the issues raised in the City’s response letter.

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 Council to make this plan available for public review in the City Clerk’s office.

Fiscal Stress

Financial condition may be defined as a City's ability to fund recurring expenditures with recurring revenues while continuing to provide desired services. A City in good financial condition generally maintains adequate service levels during fiscal downturns and develops resources to meet future needs. Conversely, a City in fiscal stress usually struggles to balance its budget, suffers through disruptive service level declines, has limited resources to finance future needs and has minimal cash available to pay current liabilities as they become due. City officials have a responsibility to taxpayers to ensure that their tax burden is no greater than necessary. To fulfill this responsibility, it is essential that City officials develop reasonable budgets, manage fund balance responsibly, and monitor and adjust the budget as the fiscal year progresses. Finally, City officials should develop detailed multiyear plans to set long-term priorities and work toward goals, rather than respond only to more immediate needs.

We estimate that the City will realize operating deficits in the general fund (\$1.5 million), water fund (\$275,000), sewer fund (\$370,000) and refuse fund (\$212,000) for the fiscal year ending December 31, 2013, totaling \$2,357,000. These operating deficits occurred because City officials did not include realistic estimates in the 2013 adopted budget. In addition, the City's December 31, 2012 financial position was misstated in its financial statements, which provided City officials with an inaccurate representation of the City's financial condition. This inaccurate reporting likely contributed to the continuing cash flow problems the City experienced in its 2012 and 2013 fiscal years. We found that asset accounts reported as of December 31, 2012 were unsupported and overstated, and liabilities were underreported. Our analysis indicated that the City should have reported fund balance deficits in the general, water and refuse funds as of December 31, 2012. Further, these deficits will be substantially greater as of December 31, 2013, as a result of the operating deficits we forecast for the 2013 fiscal year.

2013 Results of Operations

The Council is responsible for adopting the City's budget. The revenue estimates and appropriations should be conservative and realistic. Overly optimistic revenue estimates or overly aggressive appropriations can result in operating deficits that require the use of fund balance to finance expenditures, which deteriorates fund balance.

As indicated in Table 1, we estimate that the City will realize operating deficits in the general fund, water fund, sewer fund and refuse fund for the fiscal year ending December 31, 2013. These operating deficits

will further deplete the City's declining fund balance levels, resulting in deficit fund balances in three of these funds² as of December 31, 2013.

| Table 1: 2013 Results of Operations- Estimated | | | | |
|---|----------------------|--------------------|--------------------|--------------------|
| | General | Water | Sewer | Refuse |
| Projected Revenues | \$21,788,456 | \$3,503,234 | \$3,647,557 | \$1,042,419 |
| Projected Expenditures | \$23,347,234 | \$3,778,155 | \$4,017,704 | \$1,254,298 |
| Projected Operating Surplus (Deficit) | (\$1,558,778) | (\$274,922) | (\$370,147) | (\$211,879) |
| Projected Surplus (Deficit) Fund Balance | (\$2,674,767) | (\$691,996) | \$492,600 | (\$530,201) |

These operating deficits occurred because City officials did not include realistic estimates in the 2013 adopted budget. For example, in the general fund, we forecast that the City's real property tax revenue for 2013 will be almost \$500,000 less than budgeted, because the City's tax levy calculation did not include a tax overlay.³ In addition, we forecast that the City will overspend budgeted appropriations for police and fire department overtime by a total of \$513,000⁴ and health insurance by \$717,000. City officials stated that these appropriations were underestimated in the adopted budget because they anticipated concessions from the respective unions, which never materialized. City officials also overestimated water rents by \$716,000, sewer rents by \$574,000 and refuse revenues by \$217,000.

The Council's Finance Committee⁵ receives monthly financial reports that include year-to-date budget-to-actual comparisons for the general, water, sewer and refuse funds; however, the Council failed to address the budget deficiencies. The Council authorized only one budget adjustment, when the City received one-time revenue from the rental of property in the amount of \$222,000, increasing police and fire overtime budgets in total by this amount. If these appropriations were not increased, they would have been overexpended by more than \$771,000 for 2013.

Short-Term Borrowing and Cash Flow

The Council should ensure that the City's cash balances are sufficient to liquidate current obligations, without relying on short-term debt to address cash flow needs. This would require the routine preparation of a cash flow analysis.

² These fund balance deficits are based on the revised December 31, 2012 fund balances discussed later in this report.

³ A tax overlay is an amount of additional real property taxes to be raised to compensate for taxes that may be delinquent or not collected. A tax overlay is typically used by municipalities that enforce their own delinquent taxes.

⁴ We forecast that police department overtime will be overexpended by \$267,000 and fire department overtime will be overexpended by \$246,000.

⁵ The Finance Committee is a committee of the whole, along with the City Treasurer, City Auditor and City Budget Director (the duties of this position are currently performed by an external auditor).

During 2012, the City officials did not routinely prepare a cash flow analysis. As a result, the City's general fund experienced cash flow problems in December 2012, which led City officials to inappropriately transfer \$2.3 million⁶ in bond anticipation note (BAN) proceeds, originally issued for capital projects, to the general fund to fund City operations. Although this "loan" was repaid to the capital projects fund in January 2013, Local Finance Law provides that the proceeds of a BAN may only be used for the purpose for which the BAN was issued.

The City also experienced cash flow problems in 2013. A cash flow analysis prepared by the Treasurer's office indicated that the City would have insufficient cash to fund operations in September 2013, and the deficiency would increase to \$2.4 million as of December 31, 2013. In October 2013, the City issued a \$2.7 million revenue anticipation note (RAN). The RAN was issued in anticipation of the collection of water and sewer rents billed during the remainder of the 2013 fiscal year.⁷ We anticipate that the City will only collect \$2.2 million in water and sewer rents during the remainder of 2013; as a result, all of these collections must be set aside to redeem the RAN.⁸ If City officials do not collect sufficient water and sewer rents to repay the debt, they may either renew the RAN in the amount of the uncollected rents, or include an appropriation in the 2014 budget to redeem the note.

The Treasurer's Office should continue to update cash flow projections on a routine basis and present them to the Council for consideration. A large State aid payment will be received in December 2013 and the 2014 property tax collections will begin to be received in January 2014 to provide cash for operations in early 2014. However, the Council will need to increase revenue and/or decrease appropriations in the 2014 budget to help avoid future cash shortages later in the 2014 fiscal year.

⁶ The City made several advances from the capital projects fund to the general fund, and subsequently made a journal entry adjusting the amount advanced; the net advance was \$2.3 million.

⁷ The Treasurer's office prepared the cash flow projection in late September 2013. We reviewed this analysis to determine if the projections were reasonable and noted that the beginning cash balance as of August 31, 2013 was incorrect. We also identified other variances that resulted in our projection of a cash deficiency of \$2 million as of December 31, 2013. The difference between our projection (\$2 million) and the City's projection (\$2.4 million), and the fact that the City delayed payments to vendors, may explain why the City was able to delay the issuance of the RAN until October 2013, approximately one month later than the City's cash flow analysis indicated cash would be insufficient to finance operations.

⁸ When the amount of the RAN (\$2.7 million) equals the amount of revenue remaining to be collected, all collections thereafter (water and sewer rents in this case) must be deposited in a separate bank account and restricted only for debt service on the RAN.

2012 Financial Statements

The Treasurer is responsible for ensuring that financial reports provided to the Council members and other City officials provide a realistic representation of the City's financial condition.

As indicated in Table 2, the City's general fund assets were overstated and liabilities were understated in its financial statements as of December 31, 2012.⁹ The City's reported unassigned fund balance in the general fund should have been reported as a deficit of \$1.1 million. Similarly, the water fund should have reported an unassigned fund balance deficit of \$222,000, and the refuse fund an unassigned fund balance deficit of \$318,000. The financial position of the sewer fund was also misstated, but unassigned fund balance remained positive. Had the City's December 31, 2012 financial position been properly recorded and reported, it is likely that City officials would have been aware of the City's declining financial condition and impending cash flow problems and could have taken corrective action much sooner than September 2013.

| Table 2: Most Significant December 31, 2012 Financial Report Misstatements | | | |
|--|----------------------|---------------|---------------|
| | Financial Statements | Supported | Difference |
| General Fund | | | |
| Taxes Receivable (Asset) | \$3,384,431 | \$3,043,756 | (\$340,675) |
| Due to Other Governments (Liability) | \$3,510,164 | \$1,816,503 | (\$1,693,661) |
| Deferred Revenue (Liability) | \$47,413 | \$2,700,827 | \$2,653,414 |
| Unassigned Surplus (Deficit) Fund Balance | \$37,308 | (\$1,115,989) | (\$1,153,297) |
| Water Fund | | | |
| Water Rents Receivable (Asset) | \$759,952 | \$739,929 | (\$20,023) |
| Deferred Revenues (Liability) | \$0 | \$282,826 | \$282,826 |
| Fund Balance - Not in Spendable Form | \$0 | \$194,953 | \$194,953 |
| Unassigned Surplus (Deficit) Fund Balance | (\$13,862) | (\$222,121) | (\$208,259) |
| Sewer Fund | | | |
| Sewer Rents Receivable (Asset) | \$931,168 | \$609,378 | (\$321,790) |
| Due from Other Governments (Asset) | \$173,156 | \$0 | (173,156) |
| Deferred Revenues (Liability) | \$0 | \$251,119 | \$251,119 |
| Fund Balance - Not in Spendable Form | \$0 | \$200,378 | \$200,378 |
| Unassigned Surplus (Deficit) Fund Balance | \$1,608,812 | \$662,369 | (\$946,443) |
| Refuse Fund | | | |
| Refuse Receivable (Asset) | \$820,498 | \$466,261 | (\$354,237) |
| Unassigned Surplus (Deficit) Fund Balance | \$287,508 | (\$318,322) | (\$605,830) |

In addition to the misstated account balances, the City's accounting records had a separate fund entitled "Capital Reserve." In each year's budget, the Council included transfers to this reserve from the City's operating funds. The reserve had a balance of \$1.1 million as of

⁹ The City's Independent Public Accountant rendered an unqualified opinion on the 2012 financial statements.

December 31, 2012, which included primarily workers' compensation moneys totaling \$960,000 and a capital reserve for the water system of \$163,000. These reserves should not be accounted for in a separate fund, but should be reported in the City's operating funds. We asked the City's external auditor where these moneys were reported on the City's audited financial statements, because we only found \$118,000 reported as reserves. He stated that they were included with other moneys in the City's capital projects fund. Furthermore, we noted that the Treasurer's office had not posted journal entries to close the 2012 fiscal year records for any of the City's funds by the end of our fieldwork in October 2013. There were also a number of bank accounts that had not been reconciled to the corresponding general ledger account balances since June 30, 2013. Accurate and timely accounting records are critical components for discerning the City's financial condition at any point in time. Given the City's tenuous financial condition, accurate and timely financial information is particularly important to manage City finances.

Interfund Loans

General Municipal Law (GML) allows the City to temporarily advance moneys from one fund to another. Journal entries must be made in the accounting records to document these transactions. Repayment must be made as soon as moneys are available, but no later than the close of the fiscal year in which the advance was made.

The City's financial statements included interfund loans totaling nearly \$5.7 million as of December 31, 2012. This included more than \$1.5 million owed to the general fund from the refuse fund (\$450,000), water fund (\$390,000), sewer fund (\$340,000), special grant fund (\$250,000) and agency fund (\$83,000). Moreover, the refuse, water and special grants funds reported insufficient cash balances as of December 31, 2012 to repay the interfund loans.¹⁰ Therefore, the collectability of the interfund receivable reported in the general fund is doubtful. If fund balance were reserved for these uncollectible accounts, the general fund deficit would increase.

The City's failure to adopt a realistic budget for the 2013 fiscal year and maintain accurate and reliable accounting records resulted in operating deficits and the depletion of the City's fund balances. These conditions can be remedied by adopting structurally balanced budgets that include realistic estimates of revenues and expenditures, maintaining reliable accounting records and preparing financial reports that are accurate and supported by the accounting records.

Budget for 2014 — We reviewed the City's 2014 preliminary budget. Some of the same concerns we discussed above were again noted in this proposed spending plan. In the general fund, the City's real

¹⁰ For perspective, the cash balances reported in these funds were: refuse fund - \$183,304, water fund - \$0, sewer fund - \$494,467, and special grant fund - \$0.

property tax levy calculation did not include a tax overlay; therefore, general fund real property tax revenues as estimated in the budget may not be realized. Furthermore, budgeted appropriations for police overtime are less than the projected total expenditures for 2013. City officials stated that they anticipate concessions from the police union. If these concessions do not materialize, police overtime costs in the 2014 preliminary budget could be underestimated. In the water and sewer funds, rent revenue estimates in the budget may be overestimated. The budgeted revenue for 2014 is greater than projected rent revenues for 2013. City officials indicated they do not plan to raise water and sewer rates. Finally, neither the water fund nor the sewer fund included an appropriation for contingencies. We communicated the results of our review to City officials on November 19, 2013 so that they could adjust the preliminary budget prior to adoption by the Council.

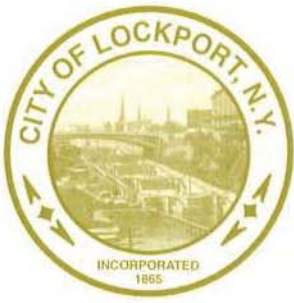
Recommendations

1. The Mayor and Council should adopt structurally balanced budgets that include realistic estimates of revenues and expenditures.
2. The Mayor and Council should monitor actual revenues and expenditures against budgeted amounts and amend the budget, as necessary, when significant variances become known.
3. The Mayor and Council should develop and implement a plan to eliminate the fund deficits.
4. The Mayor and Council should consider all appropriate options available to speed the receipt and delay the disbursement of cash.
5. City officials should ensure that the proceeds of BANs are used in accordance with Local Finance Law provisions and not used to support operations.
6. The Treasurer's Office should routinely update its cash flow projections for 2014 and present them to the Council for consideration.
7. The Treasurer should correct the accounting records and remove any unsupported balances to ensure that reports provided to the Council members and other City officials provide a realistic representation of the City's financial condition.
8. The Treasurer's Office should analyze interfund loan balances and make recommendations to the Council for consideration and authorization for action.
9. City officials should consider modifying revenue and expenditure estimates in the 2014 preliminary budget prior to adoption.

APPENDIX A

RESPONSE FROM CITY OFFICIALS

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



Office of the Mayor

Michael W. Tucker, Mayor



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December 5, 2013

Robert E. Meller
Chief Examiner of Local Government and School Accountability
NYS Office of the State Comptroller
110 State Street
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Dear Mr. Meller:

The City of Lockport has received the NYS Office of State Comptroller's Report of Examination on the City's Fiscal Stress. We appreciate the time and assistance that the OSC auditors have put in to help us determine the City's financial condition. We are committed to implementing strategies that will put the City back on sound financial footing and have already taken significant steps that will lead to a balanced 2014 budget. The City concurs with the OSC objective of the audit and will ensure that budgets are structurally balanced and that heightened monitoring of the City's financial operations are in place to ensure fiscal stability. The following is the City of Lockport Response.

Background

As indicated in the OSC Report, the 2013 adopted budget included overly optimistic revenue estimates and cost reductions anticipated from labor concessions – primarily in Overtime and Health Insurance. These concessions did not materialize and the budget became unbalanced. To compound the problem, in August 2013, City officials became aware of the fact that the City actually started 2013 with a negative fund balance. In previous years, unplanned spending resulted in the City's use of the fund balance to cover the difference. This was not possible in 2013. The Common Council's focus has been to be fiscally conscientious in these trying times. Over the last year, the Mayor and/or Common Council took several measures to address the fiscal challenges. These included the following measures:

1. Reduced the proposed capital improvement spending plan in 2012 by \$1 million, with an eye on the impact debt payments would have on the 2013 budget.

2. Released a Request For Proposals for health care broker in an effort to determine if savings could be made
3. Denied a request for the City Clerk to hire a temporary office worker to cover for a temporary leave of absence, because it was not budgeted
4. Terminated a new Police Officer in early 2013, when a retirement did not materialize
5. Released a Request For Proposals for budget development and subsequently hired an independent CPA firm, Lumsden and McCormick, to perform budget development services for 2014. They provided professional financial services and began with an analysis of previous years finances and budgeting. The Treasurer's Office supported the work of Lumsden and McCormick by providing prior year history and explanation of some of the figures and also providing data on which figures were one-time instances. This was an improvement in City budgeting.
6. Instituted a spending freeze effective September 9, 2013 – which included purchases, travel, and overtime. However, it should be noted that the Council is aware that a spending freeze does not result in significant cost savings due to the fact that 85% of City expenses are personnel and contractual obligations.
7. Decided to borrow under a RAN to provide operating capital for the balance of 2013 and make changes in 2014 so that necessary internal structural changes could be made and still provide expected services to the citizens. We also realize going forward, that problem areas needs to be investigated sooner and less expensive alternatives need to be sought out whenever possible.

Treasurer's Office

In 2010, the City offered early retirement incentives to staff in an effort to start to reign in expenses. The Finance area was particularly hard-hit; the staff losses in this area included a 39 year veteran in payroll. An unexpected major illness left the primary accounting position vacant for nearly 2 years and the support position for the accountant was eliminated. By 2011, the entire accounting staff consisted of new people or people in new positions. Clearly, impact of the loss of institutional knowledge was not anticipated. Because of these shortages, many of the supporting records for accounts were not in proper order, which made it difficult for new staff to bring records into the desired state. Additionally, during this transition period the City Treasurer was newly elected and in 2011 the City Budget Director retired. The Treasurer's Office encountered difficulty in generating financial statements as new staff did not have sufficient data available to know the history on some of the figures on the books, which resulted in inaccuracies noted by the State Comptroller.

OSC Recommendations and City of Lockport Responses:

- 1) **The Mayor and Council should adopt structurally balanced budgets that include realistic estimates of revenues and expenditures.**

In early 2013, the Mayor and Common Council hired CPA Firm Lumsden and McCormick to provide budget development services for the 2014 budget in an effort to have a more accurate budget. Lumsden and McCormick began with an analysis of previous years' finances and budgeting. The Treasurer's Office supported the work of Lumsden and McCormick by providing prior year history and explanation of some of the figures and also providing data on which figures were one-time instances. Lumsden and McCormick presented a thorough analysis of the city's finances and what steps would need to be taken to balance the 2014 budget. City officials believe that the analysis done in preparing the 2014 budget has created a budget that contains far more accurate revenue and expenditure projections. Further, the Mayor and Council realize that if these estimates fall short, changes need to be made immediately in an attempt to re-balance the budget. For 2014, some internal restructuring has been done to better categorize our expenses so that future analysis will be easier. We have also attempted to start building many budget figures from zero up, rather than assuming that a prior year's estimate should just be continued going forward. This has led to a decrease in authorized departmental discretionary spending. We believe our 2014 budget is very realistic and an important first step in improving our budget process and financial condition.

See
Note 1
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In a 10/15/13 meeting with City Officials and NYS OSC staff, some verbal recommendations were made by OSC staff to aid the City in putting forth a balanced 2014 budget. One recommendation was for the City to cut expenses and increase revenue. The message was consistent with recommendations by Lumsden and McCormick CPA. As a result, the 2014 budget has reductions of 16 positions, which is 15 actual employee layoffs. (The City's Accounts Payable Clerk left the City for a new position in September. This enabled a CSEA employee to transfer to this position.) This is a significant step towards having expenses match up with revenue. Additionally, while the Common Council was strongly against an increase in the property tax rate, the Council did ultimately raise the tax rate by 1.7% - to generate an additional \$178,000 in property tax revenue. Furthermore, the City was able to secure a \$1,050,000 one-time New York State grant. This combination of significant cost reductions and revenue increase aided greatly in the City's ability to put forth a balanced 2014 budget.

The OSC Report also included a review of the City's 2014 preliminary budget. Some concerns were noted regarding tax overlay for general fund real property tax revenues; police department overtime; rent revenue estimates in sewer and water; and water and sewer contingencies.

City officials conferred with Lumsden and McCormick regarding these concerns and also reviewed past years' actuals in these areas. Lumsden and McCormick advised the City that the budgeted revenues and expenses were accurate based on previous years' actuals. Regarding the concern that general fund real property tax revenues as estimated may not be realized – the City has reviewed

the past three years of tax revenue that are received in a given year but incurred in previous years. These annual amounts have been \$910,000 (2011), \$861,000 (2012), and \$880,000 (2013). These amounts are divided between the City and the Lockport School District. Therefore, the City expects to receive approximately \$442,000 per year in revenue in this category. Lumsden and McCormick indicated that when combined with the property tax revenue received for the actual year incurred, this number should be quite close. City officials will monitor this revenue closely. If it appears to be lower than estimated, City officials will decrease expenses elsewhere in the budget to balance the impact. Police Overtime is budgeted at \$354,302 for 2014, a significant increase over the 2013 budget. City officials are working with the Police Department to determine ways to reduce Overtime. If these plans do not result in the anticipated savings, the City will amend the budget accordingly by reducing an equivalent expense in another line. The budgeted rent revenue estimates in water and sewer are based on previous years' estimates. City officials will monitor these revenues as well and will consider cutting expenses or increasing rates mid-year as necessary to balance it. Lastly, the Sewer Fund has contingency funds available and a positive fund balance.

See
Note 2
Page 19

See
Note 3
Page 19

2) The Mayor and Council should monitor actual revenues and expenditures against budgeted amounts and amend the budget, as necessary, when significant variances become known.

The Mayor and Common Council agree that heightened monitoring of the budget is necessary in the coming year to ensure fiscal soundness. Greater scrutiny and budget modifications will need to occur throughout the year as unexpected events/expenses arise. The Mayor and Common Council are in the process of establishing a new process, which will ensure greater monitoring over the year's actual expenses and revenues. Beginning in January 2014, the Mayor, Treasurer, and Common Council will have a monthly finance meeting in which Department Heads will be required to attend. This will give City Officials the opportunity to monitor the budget with Department Heads, in a timely manner. Increased involvement of the City's Department Heads will assist the Mayor and Common Council in understanding variances in revenues and expenditures and aid in monitoring the budget and implementing cost reduction strategies on an ongoing basis.

3) The Mayor and Council should develop and implement a plan to eliminate the fund deficits.

The Mayor and the Common Council are in the process of considering plans to eliminate the fund deficits and rebuild the City's fund balance. In tightening up the 2014 budget, a much larger amount has been budgeted in contingency so that budget shortfalls can be funded when necessary, but the money is not available for discretionary spending at the departmental level. The Council will need to authorize spending of these funds by resolution and is hopeful that all of it will not

be needed so that excess in this area will help to rebuild Fund Balance. We are attempting to implement long-term planning to rebuild our Fund Balance. We anticipate a 3-5 year window to pay off our existing RAN and eliminate the need to borrow to fund current operations.

- 4) **The Mayor and Council should consider all appropriate options available to speed the receipt and delay the disbursement of cash.**

In 2013, the City established a Financial Management Group and has charged this group with analyzing problem areas and researching resolutions to identified problems and suggesting viable alternatives. One of the areas already addressed this year was the area of Ambulance billing. Currently we are utilizing the services of an outside billing firm which has already resulted in more timely receipt of the revenue. We are also starting to research the timing related to payment of claims. We are aware of the importance of group and will continue to meet to problem-solve.

- 5) **City officials should ensure that the proceeds of BANS are used in accordance with Local Finance Law provisions and not used to support operations.**

City officials shall adhere to the strict restrictions on BANS and Bonds proceeds. We are in the process of more closely monitoring cash flow and review of available funds for operating purposes to prevent this from occurring again. City officials understand that BANS may not be used to support city operations and will not utilize the proceeds of BANS for city operations going forward.

- 6) **The Treasurer's Office should routinely update its cash flow projections for 2014 and present them to the Council for consideration.**

While the Treasurer's office has provided cash flow projections and related reports to the Mayor and the Council, the frequency and details of such reports will be provided monthly.

- 7) **The Treasurer should correct the accounting records and remove any unsupported balances to ensure that reports provided to the Council members and other City officials provide a realistic representation of the City's financial condition.**

The Treasurer and his staff are formulating a plan to correct the accounting records. In the past year, the Treasurer's Department has spent a great deal of time responding to previous recommendations by the Comptroller's office relative to the Internal Control Audit that was done in 2012. The City updated and implemented a new procurement policy and the enforcement of this policy has been assumed by the Treasurer's office. The Treasurer's office was also the

lead department in implementing the billing for the new refuse program. In 2012, the City upgraded its accounting software package and this project was lead by the Treasurer's staff and was very time consuming. The City also implemented the acceptance of credit cards for the payment of some revenues and has been instrumental in working the third party billing agent for Ambulance billing. Additionally, many procedures have been documented, as suggested as part of the internal control audit that was done. As a result of past cost-cutting measures, previous support staff from this area were eliminated and necessary routine tasks are now performed by senior staff. The Treasurer's office is also now prepared for succession planning and getting staff in place to work with current staff to address any transitions of staff due to illness or retirement. The Treasurer's office has recommended to the Mayor and Council a plan to hire an experienced outside consultant. There is a great deal of work that needs to be done to make corrections that will result in more accurate statements of financial condition for y/e 2013. In light of our current financial situation, the Treasurer's Office feels the most economical way to accomplish what needs to be done timely is with an experienced, knowledgeable consultant who will require minimal training from senior staff. This plan includes a time-line of projects that need to be completed and would far less expensive than increasing internal staff. This consultant, after completing this initial project, would be a very good person to consider as budget consultant for next year. In discussion the Lumsden and McCormick, this year's budget consultant, there was consensus that this would be an excellent way to accomplish the necessary tasks. The Mayor and Council have been informed of the Treasurer's request for a consultant and will be considering this request.

8) The Treasurer's Office should analyze interfund loan balances and make recommendations to the Council for consideration and authorization for action.

The Treasurer's office plans to analyze inter-fund loan balances and to make a recommendation to the Council for consideration and authorization for action. The Treasurer's office feels that a consultant would also be helpful in this analysis.

9) City officials should consider modifying revenue and expenditure estimates in the 2014 preliminary budget prior to adoption.

Recent years' collection of tax certificates has been analyzed and discussed with Lumsden & McCormick, our budget consultant. In recent years the collection of prior years' taxes has exceeded the amount of uncollected current year taxes and the figure for city tax revenue has been unchanged in the 2014. We expect that the revenue collected in 2014 will meet or slightly exceed the budgeted amount.

Summary

The Mayor, Common Council, and Treasurer agree that improvements to budgeting and budget monitoring need to occur. Several steps have already been taken to improve the budgeting and monitoring process. City officials remain committed to making the changes discussed herein and while the next few years will be challenging – improvements to the city's financial status can and will be made. We are appreciative of the analysis and recommendations that have been made by the State Comptroller's Office and will work diligently to implement necessary changes. Thank you for your assistance in this matter.

Sincerely,

Michael Tucker, Mayor

Anne McCaffrey, Council President

Michael White, Treasurer

APPENDIX B

OSC COMMENTS ON THE CITY'S RESPONSE

Note 1

The estimated rent revenue in the water and sewer funds is overestimated in the 2014 budget. The budgeted revenue for 2014 is greater than the projected rent revenues for 2013 for both funds. The projected sewer rent revenue for 2013 is estimated at \$2.9 million and 2014 budgeted revenue is \$3.5 million. Projected water rent revenue for 2013 is estimated at \$3.2 million and 2014 budgeted revenue is \$3.9 million.

Note 2

We note that police overtime costs were vastly understated in the 2013 adopted budget. While the 2014 budget is an improvement, overtime expenditures for 2013 are projected to significantly exceed the amount appropriated for police overtime in the 2014 budget.

Note 3

It is important to note that 2012 actual revenue from water and sewer rents included 13 months of collections due to a change in the City's billing and collection procedures. City officials acknowledged this anomaly. However, it does not appear they considered this fact when they estimated revenue from water and sewer rents in the 2014 budget.

APPENDIX C

AUDIT METHODOLOGY AND STANDARDS

The Office of the State Comptroller's Fiscal Stress Monitoring System evaluates local governments based on financial and environmental indicators. These indicators are calculated using the local government's annual update document (AUD)¹¹ and information from the United States Census Bureau, New York State Department of Labor and the New York State Education Department, among other sources. The City has demonstrated signs of fiscal stress in several areas. Due in part to these fiscal stress indicators, we selected the City for audit.

Our overall goal was to review the City's financial condition. To accomplish this, our initial assessment included a comprehensive review of the City's financial condition. To obtain valid audit evidence, we performed the following audit procedures:

- We reviewed the City's charter, code, and policies and procedures for developing and reporting information relevant to financial and budgeting activities, including the fiscal responsibilities of City officials.
- We interviewed City officials to determine what budget development processes were in place and gain an understanding of the City's financial condition.
- We reviewed and analyzed the City's financial records and reports for all funds, including balance sheets, budget reports and statements of revenues and expenditures. We evaluated the City's December 31, 2012 financial statements, prepared by the City's external auditor, to determine if they were reliable. We asked City officials and the external auditor to provide us with support for many of the City's assets and liabilities reported as of December 31, 2012.
- We determined the reasonableness of budget estimates by comparing the adopted budgets to actual revenues and expenditures.
- We projected revenues and expenditures for the remainder of the 2013 fiscal year, using operating results from 2012 and prior fiscal years when needed.
- We reviewed the 2014 preliminary budget.

We conducted this performance audit in accordance with generally accepted government auditing standards (GAGAS). Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

¹¹ Required to be submitted annually by the City to the Office of the State Comptroller

APPENDIX D

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