



Village of Mill Neck Financial Management

Report of Examination

Period Covered:

June 1, 2011 — May 31, 2014

2014M-358



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

February 2015

Dear Village Officials:

A top priority of the Office of the State Comptroller is to help local government officials manage government resources efficiently and effectively and, by so doing, provide accountability for tax dollars spent to support government operations. The Comptroller oversees the fiscal affairs of local governments statewide, as well as compliance with relevant statutes and observance of good business practices. This fiscal oversight is accomplished, in part, through our audits, which identify opportunities for improving operations and Village 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 Village of Mill Neck, entitled Financial Management. This audit was conducted pursuant to Article V, Section 1 of the State Constitution and the State Comptroller's authority as set forth in Article 3 of the New York State General Municipal Law.

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

Respectfully submitted,

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

Introduction

Background

The Village of Mill Neck (Village) is located in Nassau County, is about three square miles and has a population of approximately 1,200 residents. The Village provides various services to its residents including police and fire protection, street maintenance, snow removal, sanitation and general government support. The Village's general fund budget for the 2014-15 fiscal year¹ is approximately \$2.6 million, funded primarily with property taxes.

The Village Board of Trustees (Board) comprises four elected Trustees and an elected Mayor, who serves as the Village's chief executive officer. The Board is the legislative body responsible for the general management and control of the Village's financial affairs, including developing and adopting the annual budget and establishing financial policies and procedures. The appointed Clerk/Treasurer is the Village's chief fiscal officer and is responsible for receiving, disbursing and maintaining custody of Village moneys and for preparing, maintaining and reporting all necessary financial information.

Objective

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

- Did the Board maintain the Village's general fund balance at a reasonable level and properly restrict funds intended for capital purposes?

Scope and Methodology

We examined the Village's financial condition for the period June 1, 2011 through May 31, 2014.

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

Comments of Local Officials and Corrective Action

The results of our audit and recommendations have been discussed with Village officials and their comments, which appear in Appendix A, have been considered in preparing this report. Village officials generally agreed with our findings and recommendations and indicated they plan to initiate corrective action.

The Board has the responsibility to initiate corrective action. A written corrective action plan (CAP) that addresses the findings and

¹ The Village's fiscal year is from June 1 through May 31.

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 Village Clerk's office.

Financial Management

An important part of budgeting for local governments is the prudent use of fund balance.² Village officials can legally set aside or restrict portions of fund balance to finance future costs for a specified purpose, designate a portion to help finance the next year's budget or retain a portion as a financial cushion for unforeseen financial circumstances. Each local government needs to assess what is reasonable for its particular situation considering various factors, such as timing of receipts and disbursements and volatility of revenues and expenditures. If fund balance is kept at excessively high levels, funds that could benefit the Village are not being used, thereby placing an unnecessary burden on the taxpayers. It is important that the Board adopt policies and procedures to govern the level of fund balance to be maintained in each fund. Therefore, the Board should adopt budgets that include realistic estimates of revenues and expenditures and use surplus fund balance as a funding source, when appropriate.

A multiyear financial or capital plan helps a local government assess expenditure commitments, revenue trends, financial risks and the affordability of new services and capital improvements. It allows Village officials to assess the impact and merits of alternative approaches to address financial issues, such as the use of unrestricted fund balance to finance operations and the accumulation of money in Board-authorized reserve funds. Establishing and funding reserves³ may help to avoid large increases in taxes resulting from unforeseen repairs or capital improvements and also increases transparency related to the intended use of revenues collected.

The Board has not established adequate policies and procedures or provided guidance on maintaining a reasonable level of fund balance. As a result, the Village has accumulated excessive fund balance in its general fund that resulted, at least in part, from unrealistic budget estimates. In addition, the Board has not developed a long-term financial or capital plan or established reserves to help address the Village's future needs.

Excessive Fund Balance – The Board has not adopted policies and procedures to govern the level of fund balance to be maintained and the Village has accumulated excessive fund balance in the general

² Fund balance represents resources remaining from prior fiscal years that can be used as funding sources in the next year's budget to reduce the amount of revenues needed to be raised from other sources.

³ Reserve funds provide a mechanism for legally saving money to finance all or part of future infrastructure, equipment and other allowable purposes. Reserve funds are classified as restricted fund balance.

fund. While our audit period covered the Village's financial condition from the 2011-12 through 2013-14 fiscal years, we found that the Village has maintained excessive fund balance for several more years. Specifically, over the past eight years, the Village's fund balance has ranged from approximately 25 percent to 52 percent of the next year's budgeted appropriations. For example, the general fund's unrestricted, unappropriated fund balance is more than half of the 2014-15 fiscal year's budgeted appropriations (see Figure 1). This has resulted in the Village levying taxes that were not needed and taxpayer funds lying idle instead of being used to benefit taxpayers.

Figure 1: Operating Results and Fund Balance

	FY 2011-12	FY 2012-13	FY 2013-14
Revenues	\$2,577,254	\$2,517,490	\$2,696,402
Expenditures	\$2,344,869	\$2,365,541	\$2,400,880
Operating Surplus	\$232,385	\$151,949	\$295,522
Beginning Fund Balance	\$646,509	\$878,894	\$1,030,843
Operating Surplus	\$232,385	\$151,949	\$295,522
Ending Fund Balance	\$878,894	\$1,030,843	\$1,326,365
Less: Fund Balance Appropriated to Finance Next Year's Operations	\$58,500	\$0	\$0
Unrestricted, unappropriated Fund Balance	\$820,394	\$1,030,843	\$1,326,365
Next Year's Budgeted Appropriations	\$2,477,370	\$2,506,051	\$2,560,301
Unrestricted, unappropriated Fund Balance as a Percentage of Next Year's Budgeted Appropriations	33%	41%	52%

Due to the excessive fund balance, we examined the budgets and operating results for the 2011-12 through 2013-14 fiscal years, and found that the Board had underestimated revenues and overestimated expenditures in each of these three years (see Figure 2). General fund revenues were underestimated by a total of \$500,456 (7 percent) and appropriations were overestimated by a total of \$237,900 (3 percent) over the last three years. For example, over the last three years, the Village underestimated departmental income by as much as \$50,826 (65 percent), and revenue from licenses and permits by as much as \$43,750 (64 percent), while it also overestimated its transportation expenditures by as much as \$65,223 (45 percent). Furthermore, the Board also planned for an operating deficit in the 2012-13 fiscal year and appropriated \$58,500 to fund the ensuing year's operations. However, in the 2012-13 fiscal year, the general fund generated an operating surplus of \$151,949 and the Village did not use any appropriated fund balance. The general fund had operating surpluses in 2011-12, 2012-13 and 2013-14), which has caused an already excessive level of fund balance to become even larger.

Figure 2: Budget-to-Actual Comparison

	2011-12	2012-13	2013-14	Total
Estimated Revenues	\$2,365,769	\$2,418,870	\$2,506,051	\$7,290,690
Actual Revenues	\$2,577,254	\$2,517,490	\$2,696,402	\$7,791,146
Variance	\$211,485	\$98,620	\$190,351	\$500,456
Variance Percentage	9%	4%	8%	7%
Budgeted Appropriations	\$2,365,769	\$2,477,370	\$2,506,051	\$7,349,190
Actual Expenditures	\$2,344,869	\$2,365,541	\$2,400,880	\$7,111,290
Variance	\$20,900	\$111,829	\$105,171	\$237,900
Variance Percentage	1%	5%	4%	3%

While it is prudent to budget conservatively or to maintain adequate fund balance to protect against unforeseen circumstances, retaining a substantial fund balance in addition to adopting a conservative budget, as the Village has been doing, results in taxes being higher than necessary.

Long-Term Planning – Village officials have not developed a comprehensive, written multiyear financial or capital plan. Such plans would be a useful tool for the Board to address its plans for using fund balance. Rather than establishing and funding reserves, the Board underestimated revenues and overestimated expenditures in the general fund which resulted in an increase in fund balance. The Board explained that it has identified potential future expenditures that could reduce fund balance, such as highway repairs, Village hall upgrades and the purchase of a sanitation truck. However, it did not establish reserves, but instead assigned fund balance for its intended projects, since it was not certain of the total amounts needed. When fund balance is assigned, these moneys can still be used for any purpose; alternatively, establishing reserves would legally restrict the use of these moneys to a specific purpose. It would be appropriate for the Board to include these types of potential uses in a long-term financial or capital plan. Without formal long-term capital plans, it is difficult to provide transparency of the Village's financial position and its long-term capital needs.

Since the Board has not formally documented any of these plans or set aside funds in reserves for these purposes, these funds remain as excess fund balance, causing tax increases to appear unnecessary. Furthermore, the lack of policies and procedures governing the level of fund balance to be maintained, and the inclusion of unrealistic revenue and expenditure estimates in Village budgets, limits the Board's ability to effectively manage financial operations.

Recommendations

The Board should:

1. Adopt a fund balance policy that establishes reasonable levels of fund balance to be maintained to meet the Village's financial needs.
2. Formulate a plan for the use of excess unrestricted, unappropriated fund balance in the general fund in a manner that benefits taxpayers. Such uses include, but are not limited to, reducing property taxes, paying off debt, establishing necessary reserves or financing one-time expenditures.
3. Adopt budgets that include realistic estimates for revenues and expenditures.
4. Develop and adopt a comprehensive multiyear financial and capital plan to establish the goals and objectives for funding long-term operating and capital needs. This plan should address the use of unrestricted, unappropriated fund balance and the necessity and funding of reserves and should be monitored and updated on an ongoing basis.
5. Formally establish authorized reserves to finance certain anticipated future expenditures and adopt a policy to establish funding and use of the reserves.

APPENDIX A

RESPONSE FROM LOCAL OFFICIALS

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

Incorporated Village of Mill Neck

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February 12, 2015

Mr. Ira McCracken, Chief Examiner
NYS Office Building, Room 3A10
250 Veterans Memorial Hwy
Hauppauge, NY 11788-5533

RE: Village of Mill Neck Draft Financial Management Report of Examination

Dear Mr. McCracken,

The Board of Trustees would like to thank the Comptroller's Office and their audit team for their professionalism and their recommendations. Please consider this our letter in response to the Draft Financial Management Report for the examination period of June 1, 2011 through May 31, 2014.

During the years under examination the Village of Mill Neck experienced Hurricane Irene and Tropical Storm Sandy which caused unexpected expenditures which were eventually partially reimbursed by FEMA. As a result of Hurricane Sandy, West Shore Road partially collapsed into Oyster Bay and has caused detours onto Village roads. The Board felt it was prudent to hold off on road maintenance projects to see how the detour roads would be affected. There was \$579,000 designated in 2012-2013 for equipment, building maintenance and highway repairs, but not reserved as recommended to us by your office.

The village was very fortunate during these years to experience an unexpected surge in film permits which added over \$200,000 to revenues. This year in contrast filming revenues to date are \$29,600 vs a budget of \$26,000 a sharp contrast to the previous year's permit revenues that were at \$78,000 this time last year. We have also been the recipient during the three years of \$74,000 in Grants and funding from New York State. Budgeting as we know is not an exact science. The Board has already begun implementation of Reserve Accounts for the Village's Projects as recommended by your office. This will result in a reduction of the Village's current Fund Balance.

It was a pleasure working with your staff.

Sincerely,

Peter Quick
Mayor

Cc: Board of Trustees
Village Attorney

APPENDIX B

AUDIT METHODOLOGY AND STANDARDS

We interviewed appropriate Village officials to obtain an understanding of the organization and the accounting system. We reviewed pertinent documents, such as Village policies and procedures manuals, financial records and reports and Board minutes. Further, we reviewed the Village's internal controls and procedures over the computerized financial databases to ensure that the information produced by such systems was reliable.

After reviewing the information gathered during our initial assessment, we evaluated the Village's internal controls for the risk of potential fraud, theft or professional misconduct. We then decided on the reported objective and scope by selecting for audit the area most at risk. We selected the Village's financial management for further audit testing. To accomplish the objective of this audit and obtain valid audit evidence, procedures included the following:

- We reviewed Board minutes, policies and procedures and made inquiries of Village officials.
- We interviewed Village officials to gain an understanding of the organization, budgeting practices, establishment and use of reserve funds and planned use of unrestricted, unappropriated fund balance.
- We reviewed the Village's financial records and reports, including budgets and annual reports, and completed an analysis of fund balance.
- We analyzed the changes in fund balance and variances between budgeted and actual revenues and expenditures to determine whether budget estimates and fund balance levels were reasonable. We also calculated operating deficits and surpluses.

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

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