DIVISION OF LOCAL GOVERNMENT AND SCHOOL ACCOUNTABILITY

REPORT OF EXAMINATION | 2018M-179

Monroe County

Financial Condition

DECEMBER 2018

OFFICE OF THE NEW YORK STATE COMPTROLLER
Thomas P. DiNapoli, State Comptroller

Contents

Report Highlights

Monroe County

Audit Objective

Determine whether the Legislature and County officials effectively managed the County's financial condition.

Key Findings

- The County's financial position has been strained for several years. Its combined funds'[1] available fund balance as of December 31, 2017 totaled only $1.9 million or .13 percent of gross expenditures, after $12.4 million in one-time increases that are unlikely to recur.
- The County relied on $65 million in revenue anticipation notes and $30.85 million in reported general fund interfund advances to cover deficit cash balances in 2017.
- The County does not have sufficient general fund balance to mitigate significant revenue shortages or unanticipated expenditures.

Key Recommendations

- Identify ways to increase recurring revenues or decrease recurring expenditures to improve the County's financial condition.
- Take measures to ensure the County generates and maintains adequate fund balance and cash flow in all funds.
- Develop a sustainable plan to phase out the general fund's subsidizing of the solid waste fund.

County officials generally disagreed with our findings and recommendations. Appendix B includes our comments on issues raised in the County's response (Appendix A).

Background

Monroe County (County) is located in the western portion of New York State along Lake Ontario's southern shore. The County is governed by its 29-member County Legislature (Legislature). The County Executive (Executive) is the Chief Executive Officer and is responsible for oversight of operations. The Director of Finance is the County's Chief Fiscal Officer and manages the County's financial affairs. Together, these County officials are responsible for making financial decisions that are in the best interest of the County and its taxpayers.

Quick Facts	
Population	Approximately 750,000
Square Miles	657.21
2018 Appropriations	Almost $1.2 billion

Audit Period

January 1, 2014 – September 11, 2018

1 Combined funds include the general and road funds and all enterprise funds.

Financial Condition

The County has five governmental funds that include the general, road, library and two special revenue funds. The County also maintains five enterprise funds − hospital, airport, solid waste, utility and sewer funds − and an internal service fund. In addition, County officials use a capital projects fund to account for ongoing projects and a debt service fund to reserve funds earmarked for paying off specific debt instruments and to make annual debt payments related to governmental funds. For the 2014 through 2018 fiscal years, the County structured its annual operating budget to maintain a flat real property tax rate and remained within the statutory tax cap.

What Factors Indicate Sound Financial Condition?

A county's financial condition determines its ability to finance services on a continuing basis, maintain adequate service levels and survive economic fluctuations. A county in sound financial condition can consistently generate sufficient recurring revenues to finance necessary services, and maintain sufficient cash flow to pay bills when they are due, without relying on one-time revenues, short-term borrowings or interfund advances. New York State General Municipal Law (GML)[2] allows Board-authorized temporary advances between funds, which must be repaid by the close of the year in which the advances are made.

A county's fund balance (the total accumulation of prior years' operating surpluses and deficits) is a key measure of financial condition. County officials should ensure that the level of available fund balance (assigned unappropriated and unassigned) maintained is sufficient to provide adequate cash flow and to help endure short-run fiscal pressures such as revenue shortfalls or unanticipated expenditures. To do so, county officials should develop a formal policy that establishes reasonable fund balance goals, and articulates a framework and process for how to increase or decrease fund balance to reach established goals over a period of time.

County officials need to adopt budgets based on historical trends and anticipated changes, and may include in the budget an appropriation for a general contingent fund to address unanticipated expenditures or budgetary shortfalls. Counties may also maintain reserves to mitigate the financial impact of major, nonrecurring or unforeseen expenditures. To monitor financial condition throughout the year, county officials need to periodically review financial reports of interim operating results.

2 New York State General Municipal Law (GML) Section 9-a

The County Continues to Experience Financial Condition Difficulties

The County's financial condition has been deficient for a number of years, including our audit period (fiscal years ending December 31, 2014 through 2017). We project that the County will end 2018 in a similar position based on the four-year trend and information available at the completion of our fieldwork. The County's financial condition has improved slightly over the audit period as evidenced by the gradual decreases in the amounts of annual short-term debt and interfund advances used to address cash flow shortages. However, this improvement was largely the result of one-time revenues or fund balance increases that are unlikely to recur. Without identifying ways to significantly reduce expenditures or increase recurring revenues, the County will continue to have significant cash flow concerns that necessitate the use of short-term debt and interfund advances, and limit its ability to restore fund balances to reasonable levels.

The County's combined funds'[3] available fund balance as of December 31, 2017 totaled only $1.9 million or .13 percent of gross expenditures. Figure 1 shows available fund balance for each of these funds, and the internal service fund, for fiscal years 2014 through 2017. The County's deficient financial condition primarily relates to the past operations of the general fund and the hospital and solid waste enterprise funds. In addition, the internal service fund had fund balance deficits in 2014 and 2015, a minimal positive fund balance in 2016,[4] and an increase to $20 million – despite a $4 million operating deficit in 2017 − due to a one-time increase.

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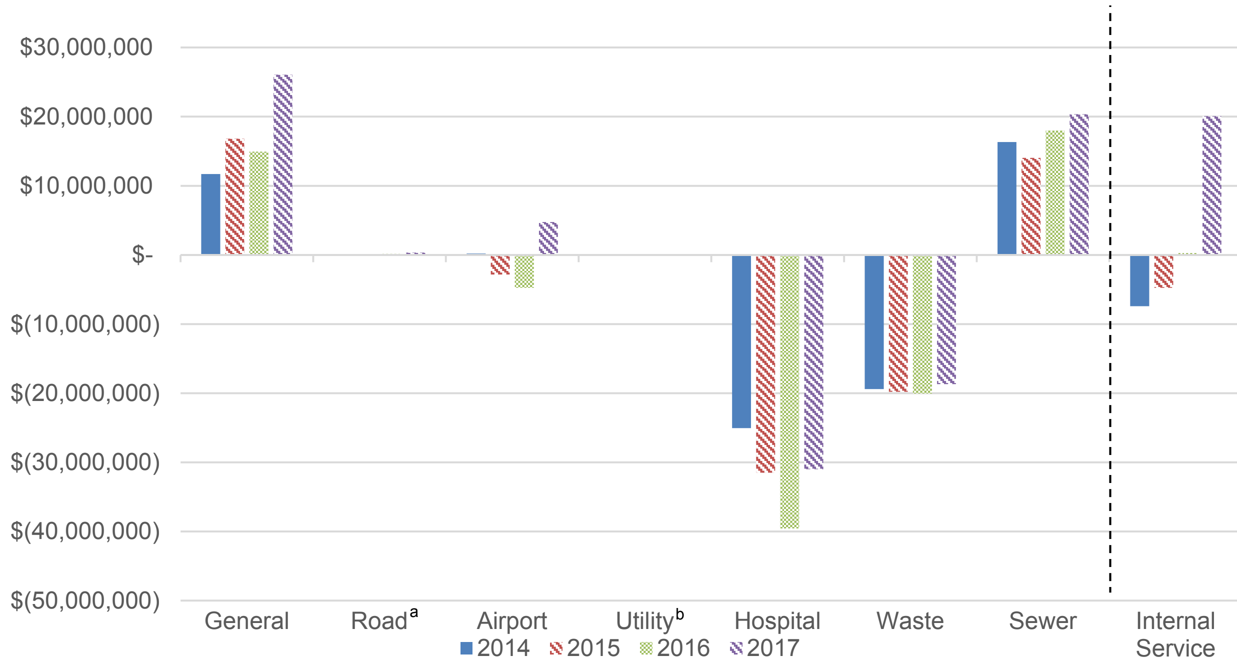
3 Combined funds include the general and road funds and all enterprise funds.

4 After consecutive operating surpluses from 2014 through 2016, resulting from a recent change to a self-insurance plan

FIGURE 1

Available Fund Balance by Fund



a The road fund's available fund balance was $89,731 in 2014; $78,415 in 2015; $147,874 in 2016; and $342,087 in 2017.

b The utility fund's available fund balance was $80,568 in 2014; $79,198 in 2015; $81,470 in 2016; and $79,660 in 2017.

Fund balances have remained similar over the last four years with minimal increases, with the exception of the sewer fund, which had planned operating deficits to reduce surplus fund balance. In addition, as discussed further, the general and internal service funds had significant one-time fund balance increases in 2017.

One-time Increases to Fund Balance Cannot Be Sustained

By definition, one-time increases (fund balance or revenues) are non-recurring and only temporarily defer the need to address structural budget imbalances. The County's limited improvement to its available fund balance as of December 31, 2017 was largely the result of one-time increases.

The County dissolved five local development companies (LDCs) and issued bonds in 2016 to take over the LDCs' $78 million outstanding debt. The State Supreme Court formally approved the LDCs' dissolution in 2017. The financial activities of three of the LDCs are now accounted for in the general fund[5] and

5 Greater Rochester Outdoor Sports Facility Corporation, Civic Center LDC, and Monroe Security and Safety Systems

the other two in the internal service fund.[6] The one-time addition of the LDCs' December 31, 2016 fund balances increased January 1, 2017 fund balance in the general fund by $11.4 million (representing 44 percent of available fund balance as of December 31, 2017).[7] The LDCs increased the internal service fund's total fund balance by $23.9 million (119 percent of December 31, 2017 available fund balance). However, future principal and interest payments for the LDCs' debt elimination will total $52 million for the general fund and $37.2 million for the internal service fund. While these funds show an increase in fund balance, those increases come with significantly higher debt service obligations that will affect future expenditures.

In addition, the solid waste fund had an operating surplus of $1.5 million in 2017.[8] The surplus resulted primarily from a one-time revenue. The County renegotiated the landfill operating lease effective January 1, 2016. The lease amendment provided for a $1 million one-time payment to the County, received in 2017, for a landfill expansion development fee.

While the one-time increases slightly improved financial condition in 2017, one-time increases only affect the current year. There is no indication that the recent improvement is sustainable.

The County Relies on Short-term Debt and Interfund Advances for Cash Flow

Another indicator of financial condition is whether the County has or generates enough cash to pay its bills. The County's combined funds' cash and investments of $96.8 million as of December 31, 2017 covered only 35 percent of its combined current liabilities of $276.5 million, down from 36.6 percent as of December 31, 2016. Figure 2 shows the inadequacy of the County's cash-to-liabilities ratio in comparison to those reported by other New York State (NYS) counties[9] as of December 31, 2017.

In addition, the County's 2017 gross expenditures, including transfers out, totaled $1.53 billion for the combined funds, and averaged $127.1 million per month. Available cash as of December 31, 2017 was sufficient to cover about 76.2 percent of one month of expenditures. Although this is a 12 percent improvement from 2016, it is inadequate, as shown by the comparison to other NYS counties (Figure 3).

6 Monroe Newpower Corporation and Upstate Telecommunications Corporation

7 While the LDCs' short-term assets and liabilities and resulting fund balance were reflected on the individual funds' balance sheets, the long term-debt obligations were recorded in the Non-Current Governmental Liabilities supplemental schedule.

8 Prior to an $816,475 operating surplus in 2016, the fund had consistent operating deficits for at least 12 years.

9 Includes all NYS counties except Cortland County which had not reported 2017 financial information as of the September 5, 2018 data analysis date. See Appendix C for a list of the Finger Lakes and large upstate counties.

FIGURE 2

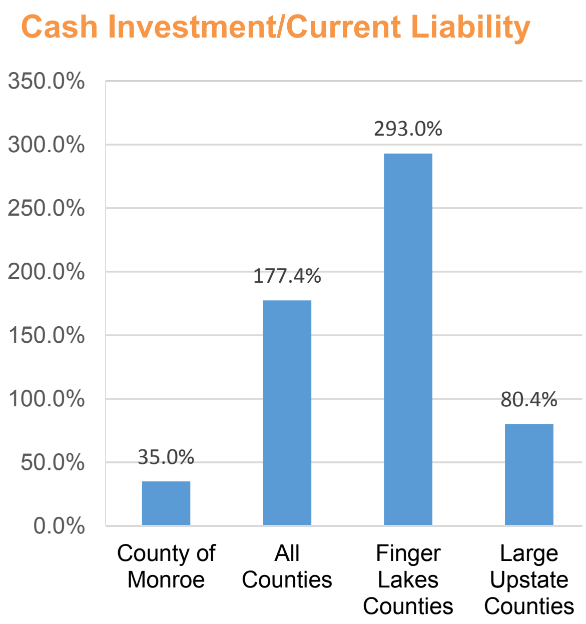
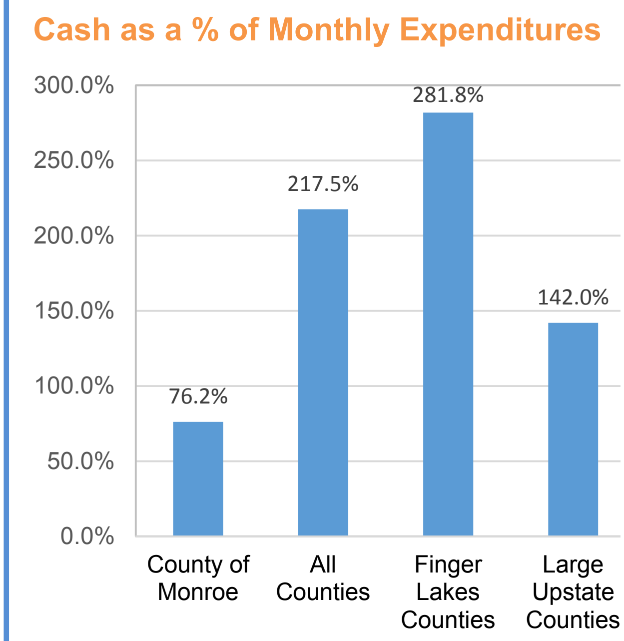


FIGURE 3



Because of the County's lack of liquid assets, it continues to rely on short-term debt and interfund advances to have sufficient cash to pay for operations.

Revenue Anticipation Notes – The County issued revenue anticipation notes (RANs)[10] annually to provide cash flow for the general and hospital funds. The general fund's RANs decreased from $58 million in 2014 to $50 million in 2017. The RANs issued on behalf of the hospital fund decreased from $17 million in 2014 to $15 million in 2017 (Figure 4).

Figure 4: RANs Due at Year End

Year End	General Fund	Hospital Fund	Total
2014	$58,000,000	$17,000,000	**$75,000,000**
2015	$58,000,000	$17,000,000	**$75,000,000**
2016	$55,000,000	$15,000,000	**$70,000,000**
2017	$50,000,000	$15,000,000	**$65,000,000**

The general fund had operating surpluses from 2014 through 2017 totaling $16 million, and the hospital fund had an $8 million operating surplus in 2017, allowing for the RAN decreases in 2016 and 2017. However, significant and consistent surpluses will be necessary to eliminate reliance on RANs and provide sufficient cash from operations.

10 In anticipation of receiving federal and State aid

Interfund Advances − The County pools cash from the governmental and enterprise funds and uses this cash pool to pay for expenditures for all funds. This process allows certain funds to maintain negative general ledger cash account balances throughout the year. At year end, the Controller's financial staff prepare reclassification entries for reporting purposes to cover cash deficits with interfund advances, and report positive cash balances in each fund.[11] At the end of 2017, the general fund reported $34.2 million due from other funds. The solid waste fund ($19.7 million) and road fund ($9.7 million) accounted for 95 percent of the $30.85 million advanced by the general fund to offset negative cash balances.

The solid waste fund[12] reported interfund advances[13] from the general fund of $19.7 million as of December 31, 2017.[14] The County has no formalized plan to generate surpluses needed to repay this interfund loan in the near future. We estimate that if the solid waste fund continues to have operating surpluses,[15] and reduce the interfund advance from the general fund at a similar rate,[16] it would take 35 years to eliminate the long-standing interfund advance from the general fund to cover cash deficits. Furthermore, without the solid waste fund loan, the potential to eliminate $19.7 million in RANs could have saved the general fund approximately $349,000 in interest from 2014 through 2017.

Although the road fund's reported interfund advances increased from $8.6 million in 2014 to $9.7 million in 2017, the fund reported sufficient current receivables[17] to cover the general fund advances, and thus did not have a significant financial concern.[18]

Without significant improvements in operations, the County will need to continue its reliance on short-term debt and interfund advances to provide needed cash flow and cover deficit cash balances in certain funds.

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11 GML Section 9-a requires that interfund advances be made with Board authorization and repaid within the fiscal year made.

12 Used to account primarily for the landfill, renewable energy power plant, residential recycling center and hazardous waste facility operated by a private company, as well as a resource recovery facility operated by another private company

13 Interfund advances began prior to 2004 when they totaled $3.3 million, and increased to $21.4 million (highest amount) in 2014.

14 The advance decreased by $1.4 million in 2017 primarily due to a $1 million one-time landfill expansion fee, along with reduced tipping fees and the County's decision to charge the sewer fund for the Mill Seat pump station debt and interest payments (starting in 2016).

15 Averaged $1.2 million over 2016 and 2017

16 Averaged $566,667 over three years; advance decreased $90,000 in 2015, $210,000 in 2016 and $1.4 million in 2017.

17 From local, federal and State governments for expenditures made for work performed but not paid for at year-end and advances to the capital projects fund.

18 Notwithstanding the lack of statutory authority to maintain interfund advances outside the fiscal year they were made.

Reported Available General Fund Balance Was Inadequate

The County has not retained a reasonable available fund balance in the general fund, appropriated a sufficient contingent account or established any reserves to mitigate the financial impact of major, nonrecurring or unforeseen expenditures.

County Law[19] allows retention of a reasonable amount of available fund balance, to be determined based on such factors as fund size, cash flow timing, contingency appropriations, revenue and expenditure volatility and availability of reserves. As of December 31, 2017, the general fund's reported available fund balance and total fund balance were 2 percent and 3 percent of 2017 gross expenditures, respectively. These fund balance levels are significantly lower than amounts reported by other NYS counties (Figures 5 and 6).

FIGURE 5

2017 General Fund Available Fund Balance as a % of Gross Expenditures

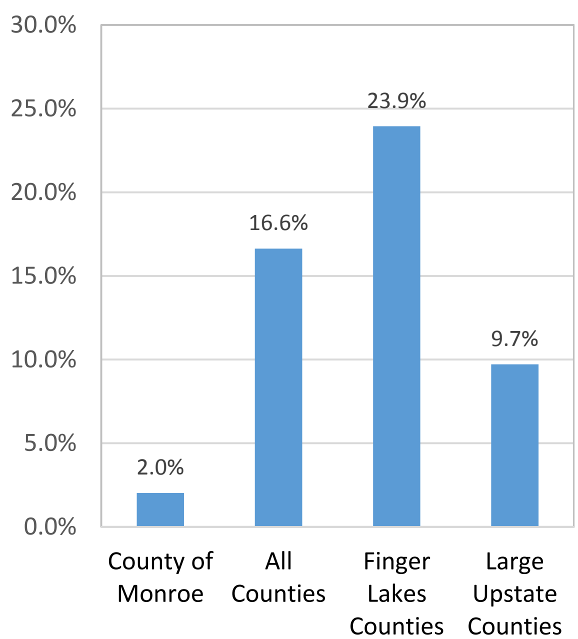
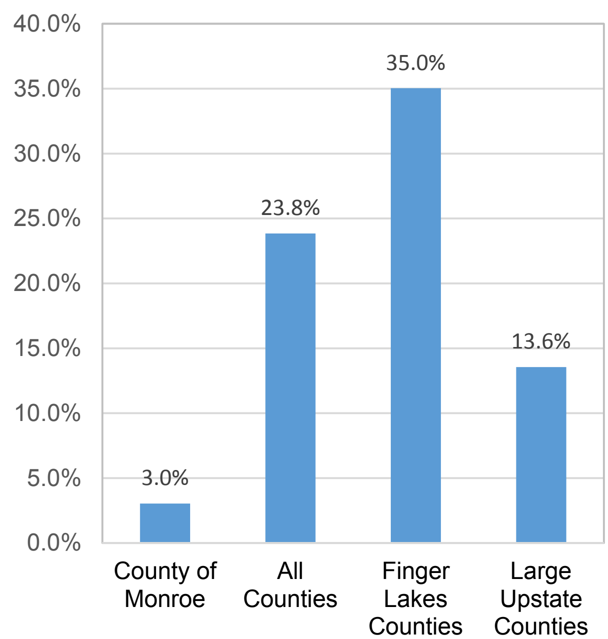


FIGURE 6

2017 Total General Fund Balance as a % of Gross Expenditures



The general fund's revenue consists primarily of real property and sales tax, federal and State grants and aid, department fees and intergovernmental agreements or chargebacks. For the 2014-2017 fiscal years, actual revenues were less than budget estimates by a total of \$56.7 million (1.5 percent) and actual expenditures were less than appropriations by \$74.8 million (1.9 percent), resulting in a net budget variance totaling \$18.1 million. Also, appropriated fund

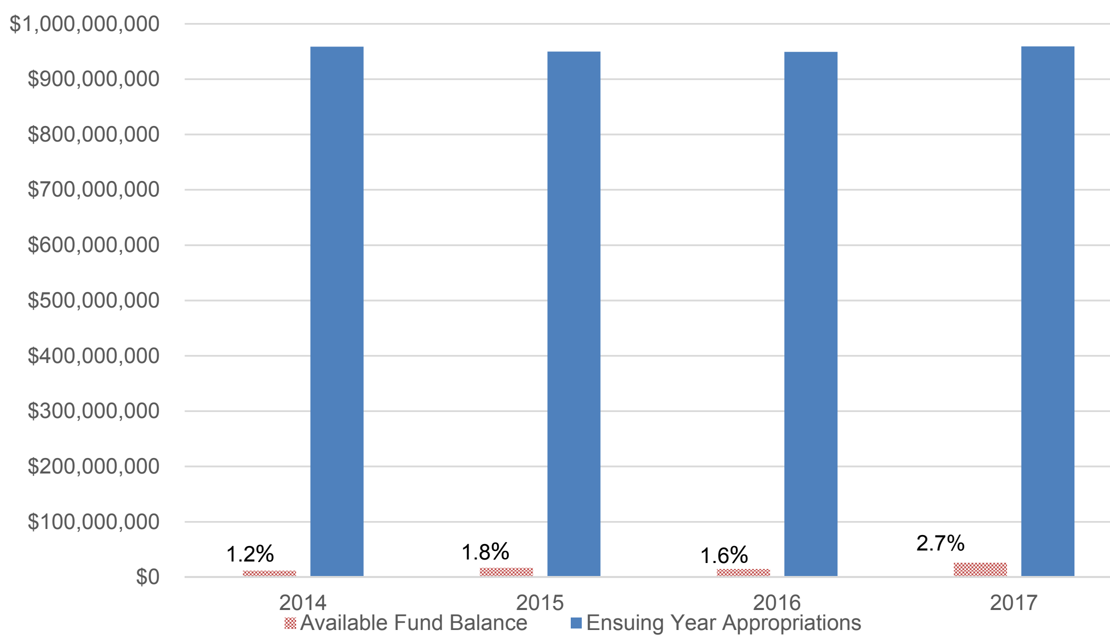
19 County Law Section 355(1)(g)

balance of $1.6 million as of December 31, 2015 went unused in 2016, resulting in total operating surpluses of $16.5 million over four years, which increased total fund balance by 146 percent from January 1, 2014 through December 31, 2017.

The increased available and total fund balances also resulted from the absorption of fund balance of three dissolved LDCs. The general fund's reported available fund balance increased from $11.7 million at the end of 2014 to $26.1 million at the end of 2017, or from 1.2 percent to 2.7 percent of the ensuing year's appropriations. Despite the increases, these fund balance levels were still inadequate to provide sufficient cash flow for the 2018 fiscal year or to cover unexpected expenditures or revenue shortfalls. Figure 7 compares the available fund balance to the ensuing year's appropriations during our audit period.

FIGURE 7

Available General Fund Balance vs. Ensuing Year Appropriations



The County's fund balance policy establishes a lower ($25 million) and upper ($35 million) threshold for the general fund's unassigned and assigned fund balance, needed to provide fund balance stability. The thresholds represent 2.6 to 3.7 percent of the general fund's average annual appropriations of about $950 million during the audit period, which is far less than the level maintained by other counties (Figure 5). The County achieved meeting the fund balance policy's lower threshold in 2017 with about $26.1 million in available fund balance. However, with such insufficient available fund balance, the general fund still must rely on short-term debt to manage cash flow for operations and is vulnerable to unexpected occurrences.

In addition, the County does not have any established reserve funds to mitigate the financial impact of major nonrecurring or unforeseen expenditures, making it more vulnerable to increasing financial instability. County Law[20] also allows for the appropriation of funds in a contingent account up to approximately $27.4 million, based on the $950 million average annual budget. However, the County consistently budgets only $100,000 for the contingent fund.

Without reserves or contingent funds, even minor budgeting variances can have a significant impact when there is inadequate available fund balance.

Questionable Reporting May Further Affect General Fund Balance

The majority of the County's reported fund balance is made up of various assets and liabilities, which must be properly calculated and supported to provide an accurate financial representation. We reviewed available support for the December 31, 2017 significant[21] balance sheet amounts and found the following two material amounts that were improperly reported.

The County incorrectly reported an $18 million current liability for payments it made in February 2018 to prepay amortized retirement costs due between 2019 and 2023. County officials told us the current liability was appropriate because they made the payment with available 2017 surplus funds, primarily the one-time increases that resulted from the dissolution of the LDCs. Because the payments were not made until 2018 and were for retirement costs due after 2018, the County should not have reported the current liability as of December 31, 2017.[22] By doing so, the County overstated 2017 general fund liabilities and expenditures, which reduced the reported year-end operating surplus and fund balance by $18 million.

The general fund also reported a $19.7 million interfund advance to the solid waste fund that originated at least 14 years ago and should not be considered and reported as a current asset. Furthermore, the County does not have statutory authority to provide interfund advances on a long-term basis, but must repay all advances within the fiscal year the advances are made. This amount should be reported as nonspendable, rather than available, fund balance.

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20 County Law Section 365 (1) allows a contingent account up to $35,000 plus 3 percent of budgeted appropriations before debt payments, less $500,000.

21 Any asset, liability or fund balance component over $500,000

22 The County should have reported the $18 million in 2018 by either recording the entire prepayment as an expenditure in 2018 (purchases method) or deferring recognition of the expenditure until the years that these amounts actually come due (consumption method).

The net effect of these two errors on the 2017 general fund balance sheet, if properly reported, would be a $1.7 million reduction in available fund balance. However, while the first error is just a timing difference, if the County properly ceased reporting the $19.7 million general fund loan to the solid waste fund as a current asset, the effect on the general fund would be a permanent reduction in available fund balance.

We also determined that $18.1 million in unpaid accrued receivables for State and federal aid and $4.4 million in due to other governments lacked adequate supporting documentation − after multiple requests to the finance department − to determine whether they were accurate and reasonable.

Without adequate supporting documentation, the County lacks assurance that assets and liabilities were accurately reported. The effect of this is magnified given the limited fund balance reported. Without assurance that the County's assets, liabilities and fund balance were accurately reported, the Executive and Legislature are not in a position to adequately monitor and take action to improve the County's financial condition.

The Legislature Rarely Monitors Monthly Financial Reports

The County charter requires the Executive to provide a monthly report to the Legislature. The Chief Financial Officer (CFO) manages the financial departments including the County Controller (Controller), responsible for preparing the monthly report for the Executive.

The Controller delivers the monthly report to the Executive and CFO, and the Executive delivers a copy to the Clerk of the Legislature (Clerk). The Clerk includes the monthly report on a list she prepares, and provides to the Legislators, of documents that are available to them, upon their request. The monthly report includes the adopted and modified budget, actual, committed and uncommitted expenditures by department and revenue by source.

However, both the minority and majority leaders did not include this report when asked what financial information they received and reviewed. The Clerk informed us that she received only two requests for the monthly report during 2017.[23]

Without frequent and thorough analysis of detailed financial information, the Executive and Legislature are not in a position to adequately monitor and work with the CFO to manage County finances and improve the County's financial condition.

23 Both requests were made by a minority party staff person.

What Do We Recommend?

The Executive and Legislature should:

1. Identify ways to increase recurring revenues or decrease recurring expenditures to provide for recurring operating surpluses.
2. Take measures to ensure the County generates and maintains adequate fund balance and cash flow in all funds.
3. Develop a sustainable plan to phase out the general fund's subsidizing of the solid waste fund or reduce the long-term receivable.
4. Develop a more adequate and comprehensive fund balance policy that allows retention of a reasonable amount of fund balance.
5. Review and monitor all County financial reports to discuss and address budgetary trends and the County's financial condition in a routine and informed manner.

County officials should:

6. Ensure compliance with GML when using interfund advances for cash flow purposes.
7. Develop a better system for obtaining and maintaining documentation to support year-end balances reported on the County's annual financial report.
8. Provide the charter-required monthly reports directly to the Legislature, instead of waiting for Legislators to request them.

Appendix A: Response From County Officials

Department of Finance

Monroe County, New York

Cheryl Dinolfo
County Executive

Robert Franklin
Chief Financial Officer

November 5, 2018

Mr. Edward Grant, Chief Examiner
NYS Office of the State Comptroller
Rochester Regional Office
16 W. Main Street, Suite 522
Rochester, NY 14614-1608

RE: Monroe County Financial Condition
Report of Examination, 2018M-179

Dear Chief Examiner Grant:

This correspondence is to provide your office with Monroe County's position concerning the draft report's findings and recommendations. As you know, county governments are not statutorily required to submit a Corrective Action Plan (CAP). However, as a courtesy, we have responded to your recommendations in sufficient detail so that this correspondence may serve as an informal CAP.

Audit Introduction: What Factors Indicate Sound Financial Condition?

To be blunt, the report's introduction of what indicates sound financial condition is an unsophisticated, one-size-fits-all evaluation reminiscent of accounting practices last popularized in the 18th and 19th centuries. Most concerning, however, is that many of the report's "findings" and "recommendations" presuppose that local governments must tax their way to fiscal strength by hoarding cash at the expense of local taxpayers. Monroe County disagrees strongly with this misguided "tax and stash" approach to budgeting.

See Note 1 Page 21

See Note 2 Page 21

As public officials charged with the responsible stewardship of local taxpayer dollars, Monroe County measures the strength of our financial condition by accessing our ability to provide vital services to residents at the lowest possible cost for taxpayers, while ensuring the sustainability of our fiscal management for future years. By every objective measure, Monroe County is succeeding in these endeavors. The County's property tax rate has been stable for over ten years, the County Budget produced a $12 million surplus for Fiscal Year 2018, and the County's credit rating is ranked at "A" status by all three major bond rating agencies for the first time in a decade.

See Note 3 Page 21

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We find it unfortunate that your office seems to find itself at-odds with S&P, Moody's, Fitch, and local residents and taxpayers, all of whom have reaffirmed Monroe County's fiscally-responsible approach governing.

See Note 4 Page 21

Beyond your office's repeated recommendations that Monroe County should stockpile cash on the backs of local taxpayers, the primary failing of the report is that it equates indicators with the whole story, rather than using indicators as a guide to learning the rest of the story. Stripped of context, numbers can be used to demonstrate almost anything. Comptroller DiNapoli seemingly acknowledged as much recently himself, when he responded to a critic's attacks on his management of the State Pension Fund by retorting, "*The reality is he's very selective in what numbers he uses, what years he looks at.*" We agree that context is important in the assessment of any financial condition. It is unfortunate that this report fails to live up to the same standard.

See Note 1 Page 21

Within the proper context, however, numbers can and should be used as a guide for sound financial decision-making. Indicators such as fund balance and cash balance are more useful when they are evaluated within the context of other indicators to form *ratios*. The relationships between financial statement accounts and categories help investors, creditors, and internal financial managers to better understand how the County is performing and what areas may need improving.

However, to narrowly focus on cash and fund balance is neither a modern nor a particularly savvy way to approach assessing financial condition. Frankly, it is disappointing that four auditors from your office spent over nine months pouring through thousands of routine financial transactions, likely costing taxpayers over $300,000, and yet the only real recommendation the report offers is that the County should tax its way to fatter bank accounts. Respectfully, Monroe County rejects this recommendation and its underlying premise.

See Note 5 Page 21

See Note 2 Page 21

Audit Finding: The County Continues to Experience Financial Condition Difficulties
County Position: Disagree

We disagree with your conclusion based on the limited context and criteria used.

See Note 6 Page 21

1. The report states that recent improvements were the result of one-time revenues or fund balance increases that are unlikely to recur, but completely ignores the one-time expenses *that also will not recur*. The reality is that the County's recurring expenses are supported by recurring revenues, such that year-end surpluses are the result of one-time revenues – as they should be.

See Note 7 Page 22

   Through monthly budget monitoring, the Finance Department continually projects revenues and expenses to anticipate year-end financial results. For the past several years, those projections have been favorable and have allowed us to strategically incur one-time expenses, such as paying down prior year pension liabilities. Because the report focuses only on the limited context of generating an abundant cash and fund balance on the backs of local taxpayers, the County otherwise receives no credit for making financial decisions that *actually save money for local taxpayers*. In fact, the only comment in the report regarding the one-time pension payment was to wrongly criticize the County's accounting treatment. The report made no comments about how the County saved $2.3 million in future interest expense that would have otherwise been payable to the State Comptroller.

See Note 2 Page 21

See Note 8 Page 22

2. The report cites the use of short-term borrowing and interfund advances as evidence of difficult financial conditions. Given your office's clear belief that local governments should hoard cash at the expense of local taxpayers, it is understandable that the report would find fault with this practice commonly used in both local governance and business management. However, maintaining financial silos within a single County government does not benefit the taxpayers. Forty years ago, when accountants were still using paper ledgers, keeping track of cash flow was more difficult, unless it was well segregated. For the last thirty years, however, financial managers in the public and private sectors have benefitted from the advent of computers to do that work for us. As such, Monroe County is able to utilize sophisticated financial software that allows us to break down those silos for more effective cash management, while still maintaining accounting integrity.

See Note 9 Page 22

See Note 2 Page 21

See Note 10 Page 22

Audit Finding: One-time Increases to Fund Balance Cannot Be Sustained
County Position: Disagree

One-time increases, in a very generic sense, can be sustained. The report, however, focuses on very *specific* one-time increases, and of course, *specific* one-time increases are just that – one-time. Because the County conservatively budgets in a manner such that recurring expenses are supported by recurring revenues, every year the County's finances benefit from some type of one-time increase. Said another way, the County does not budget one-shots. Rather, the County's philosophy is to allow one-time revenue increases and one-time expense reductions to drive year-end surpluses. With that philosophy, property owners are not over-taxed and the County benefits from slow, but steady growth to its fund balance.

Audit Finding: The County Relies on Short-term Debt and Interfund Advances for Cash Flow
County Position: Disagree

Again, this section of the report falsely equates financial condition with cash on hand, reflective of your Office's flawed opinion that municipalities should "tax and stash" to such an extreme extent that that responsible bonding would simply become unnecessary.

See
Note 2 and 11
Page 21 and 22

Conversely, Monroe County's perspective is that short-term borrowing is a tool, not a crutch. With sound knowledge of banking, credit, economics and financial markets, Monroe County is able to utilize bonding with expedience and integrity to smooth out the peaks and valleys of cash flow. A robust accounting system, solid internal controls, and established management practices ensure that all short-term borrowing is authorized, approved, tracked and accounted for, and conducted in the best interests of taxpayers.

The historical criticism over borrowing has been that borrowing comes with a cost – interest. While it is true that interest expense is a cost, Monroe County's cost of borrowing has been incredibly low. Ignored by the report is the fact that Monroe County's RANs were issued for the shortest duration in the State, approximately five months, and carried interest rates as low as 0.69% (2014) resulting in an interest cost of $215,000 on $75 million borrowed. Avoiding the interest cost would have saved local taxpayers *less than one-half of a penny of the County tax rate*. However, accumulating $75 million in a piggy bank to avoid borrowing, as your Office recommends, would have *added another $1.70 to the tax rate.* To that, Monroe County taxpayers respectfully respond: no thank you.

Audit Finding: Reported Available General Fund Balance Was Inadequate
County Position: Disagree

See
Note 2
Page 21

Again, this finding is rooted in your Office's apparent blind devotion to "tax and stash" budgeting. As evidence of a so-called inadequacy, the report simplistically compares Monroe County's fund balance to the fund balances maintained by other counties. The report offers no objective base of reference. Relative comparisons are subjective, not evidentiary. As referenced above, after four State auditors spent nine months pouring through financial records at an approximate cost exceeding $300,000, taxpayers should have expected a more thorough analysis of the local economy – and an explanation of why, given local conditions, Monroe County's fund balance is allegedly inadequate.

See
Note 12
Page 23

See
Note 5
Page 21

What allows Monroe County to have a lower fund balance relative to other New York Counties is our somewhat unique revenue structure. The revenue structure is unique because Monroe County is statutorily required to share roughly 70% (the highest in NYS) of its county-wide sales tax revenue with other municipalities and school districts. Because of that requirement, net sales tax – a volatile revenue source due to its economic sensitivity – represents only 15% of budgeted general fund revenues. That's the lowest percentage in New York State, and less than half of the statewide average of 32%.

Property tax revenue, on the other hand, is a stable revenue source. Monroe County's property tax revenue is particularly stable because the local real estate market has not historically experienced the boom and bust periods faced by housing markets in other counties. As such, Monroe County's property tax revenue consistently comprises 40% of budgeted general fund revenues, which is almost twice the statewide average of 21%. Furthermore, Monroe County consistently collects 98% of property taxes.

Lastly, federal and state aid comprise roughly 34% of budgeted general fund revenues. One can debate whether 34% of revenues being attributable to federal and state aid is too high or too low, but what is given is that those revenues are collected, making them a stable revenue source.

Taken together, the above structure led Moody's Investor Service to conclude, *"Revenues for the county are more reliable than for other New York counties."*

Audit Finding: Questionable Reporting May Further Affect General Fund Balance
County Position: Disagree

The entire section of the report that corresponds with this finding is borderline libel. A skeptic would be well within his rights to question the true motivations behind it, given that none of the State auditors have provided the County with any authoritative GASB, GAAP or AICPA statements or pronouncements supporting this false conclusion. This finding is, in short, utter nonsense.

See Note 8 Page 22

Throughout the report period, Monroe County has had an independent audit of its financial statements conducted by NYS licensed Certified Public Accountants, and has received unmodified opinions (colloquially known as clean opinions) that its financial statements, in all material respects, fairly represents the financial conditions of the County and the results of its operations. Furthermore, our independent auditors provided to the Legislature each year a letter of required communications, each of which expressed that no significant audit findings were noted, nor any findings related to accounting policies, estimates, disagreements with management, or material financial misstatements.

In addition, Monroe County has annually filed its Annual Update Document with the State Comptroller's Office. Each of those Annual Update Documents have been reviewed and approved by the OSC Division of Local Government and School Accountability.

See Note 13 Page 23

The only "questionable reporting" at play here is your Office's complete abandonment of commonly accepted accounting principles in making such nonsensical and misinformed allegations.

Audit Finding: The Legislature Rarely Monitors Monthly Financial Reports
County Position: Disagree

Numerous Legislators routinely request financial information directly from the County Administration, and routinely request from the Clerk of the Legislature the monthly reports prepared by the Controller.

See Note 14 Page 23

The report states that the Clerk of the Legislature only received two such requests for monthly financial statements, but the Auditor would only document written requests. Verbal, telephone, and in-person requests were not acceptable to the Auditors.

See Note 15 Page 23

Furthermore, to be clear, the Monroe County Administration already transmits financial information directly to the Clerk of the Legislature each month, as required by Charter.

See Note 14 Page 23

Audit Recommendations:

The Executive and Legislature should:

1. **Identify ways to increase recurring revenues or decrease recurring expenditures to provide for recurring operating surpluses.**

   What the auditors stated multiple times, and what is written in the draft report, is an expectation that the County will increase its budgeted appropriations for a Contingency Account. In black-and-white, the report calls upon Monroe County hoard cash at the expense of local taxpayers. Monroe County rejects this recommendation and the underlying premise.

   See Note 2 and 16 Page 21 and 23

   The County will continue conservative budgeting, such that recurring revenues will support recurring expenses, and will allow one-time items to generate additional fund balance.

2. **Take measures to ensure the County generates and maintains adequate fund balance and cash flow in all funds.**

   With a firm understanding of financial markets and economics, and utilizing sophisticated financial and accounting management software, Monroe County will break through government silos to manage the County's finances *holistically*, while continuing to maintain accounting integrity.

   See Note 10 Page 22

3. **Develop a sustainable plan to phase out the general fund's subsidizing of the solid waste fund or reduce the long-term receivable.**

   The Director of Environmental Services and the Chief Financial Officer agreed to a plan for the solid waste fund in 2014, with eight financial and operational adjustments to be implemented over a four-year period, 2015-2018.

Whereas prior to 2015 the solid waste fund incurred operating losses of $2M-$3M per year, the phased-in improvement plan resulted in operating income in 2015, 2016, and 2017, and resulted in increases to fund balance in 2016 and 2017. Reductions to the interfund receivable were achieved in each of the three years of the improvement plan, 2015, 2016, 2017.

See Note 17 Page 24

The plan is working as envisioned.

4. **Develop a more adequate and comprehensive fund balance policy that allows retention of a reasonable amount of fund balance.**

   Given the economic base of Monroe County and the nature of County revenues, the current fund balance policy is reasonable. Each year the policy is reviewed for reasonableness, and will be adjusted if, and when, local conditions warrant change.

5. **Review and monitor all County financial reports to discuss and address budgetary trends and the County's financial condition in a routine and informed manner.**

   The Executive and Legislature routinely engage in financial and budgetary discussions. Such discussions stem from regularly scheduled and ad hoc meetings, regularly produced reports, legislative committee meetings, etc, etc.

See Note 14 and 15 Page 23

County officials should:

6. **Ensure compliance with GML when using interfund advances for cash flow purposes.**

   Monroe County manages interfund advances in compliance with GML.

See Note 18 Page 24

7. **Develop a better system for obtaining and maintaining documentation to support year-end balances reported on the County's annual financial report.**

   What your Office really means by this recommendation is that the County should develop a brand new system simply for the purpose of making such documentation easier to understand for your Auditors. While it is abundantly clear that your Office is more comfortable using antiquated paper ledgers in lieu of modern financial software, Monroe County's obligation is to our taxpayers, not your Auditors. We do not intend to set our financial tracking systems back thirty years or more.

See Note 19 Page 24

8. **Provide the charter-required monthly reports directly to the Legislature, instead of waiting for Legislators to request them.**

The Monroe County Administration already transmits financial information directly to the Clerk of the Legislature each month, as required by Charter.

Respectfully submitted,

Robert Franklin, MPA
Director of Finance – Chief Financial Officer

cc: Hon. Cheryl Dinolfo
Hon. Dr. Joe Carbone
Hon. Brian Marianetti
Hon. Cindy Kaleh

Appendix B: OSC Comments on the County's Response

Note 1

OSC completes all audits in accordance with generally accepted government auditing standards (GAGAS). We believe our audit, including its findings and recommendations, is factually correct and stands on its own merits. We have limited our comments to address factual inaccuracies regarding our audit results and/or report.

Note 2

Our report does not recommend taxing as a means of retaining excess funds. The report recommends eliminating questionable reporting, developing a plan to eliminate long-standing interfund advances (loans), and generating sufficient resources to reduce short-term cash flow borrowings. These are all steps that will improve the County's financial position and bring increased transparency to the County's operations.

Note 3

The budget did not produce a $12 million surplus. The general fund balance increase of $12 million in 2017 consisted of a $553,776 operating surplus and a one-time unbudgeted fund balance increase of $11,441,543 from the dissolution of LDCs.

Note 4

Bond rating agencies analyze the risk to investors of an entity's indebtedness. Our audit analyzed the County's finances on behalf of the taxpayers. Under OSC's Fiscal Stress Monitoring System, the County has been rated as being in Significant Fiscal Stress for fiscal years 2015, 2016 and 2017 with scores of 82.1, 78.8 and 69.2, respectively.

Note 5

The County lacked readily available documentation to support significant amounts included in its annual reports, and was unable to generate common financial reports (including payroll reports and accounts receivable and payable subsidiary ledger reports) from its accounting system. These deficiencies, combined with the County's decision to make our information requests a low priority, contributed significantly to the time needed to complete our audit.

Note 6

We did recognize that the County reported one-time expenses to offset the one-time increases and reduce the reported operating surplus. However, our recommendation is to make structural budgetary changes to generate operating surpluses and a reasonable fund balance to eliminate the need for regular short-term borrowing and long term interfund loans.

Note 7

We concur with the County's recent decisions to prepay small portions of the amortized retirement costs (except for the improper accounting method). The 2018 pre-payment followed a $5 million prepayment in 2017 that also was incorrectly reported as of December 31, 2016.

Note 8

As discussed with County officials at various meetings, OSC accounting bulletins[24] provide detailed and updated information on pension accounting and reporting, including references to the underlying Governmental Accounting Standards Board (GASB) statements and New York State laws. The bulletins provide that, for governmental fund expenditure and liability recognition, only the amount due and payable on the retirement systems' bills should be recognized. Authorized deferred (amortized) retirement costs would be reported in the Schedule of non-current government liabilities, not as a current liability. Furthermore, during our October 11, 2018 exit conference, the Chief Financial Officer (CFO) stated that County officials chose an accounting treatment that allowed them to report a reduced operating surplus and fund balance, "because large surpluses get noticed."

Note 9

The County's use of reported (but not recorded) interfund advances to cover long-term cash deficiencies in the solid waste fund fails to address the structural problems in the solid waste fund. It also is not statutorily authorized.

Note 10

Deficient records do not further an effective cash management process. The County could not provide records that detailed commingled bank account balances with amounts belonging to each fund, or that reconciled bank account balances to totals of general ledger cash account balances of contributing funds. In addition, as noted previously, long-term advances between funds are not authorized by General Municipal Law and have allowed deficient cash balances of certain funds to be hidden and covered by surplus cash from other funds.

Note 11

We do not recommend bonding to finance general operating expenses. Bonding is generally reserved for long-term capital assets. Operating expenditures should

24 Issued in September 2011, May 2015 (superseded September 2011 bulletin) and May 2017. Resources for Local Officials can be found on OSC's website: https://osc.state.ny.us/localgov/resources/index.htm

be financed with operating revenues. We have not suggested limiting responsible borrowing.

Note 12

Other counties manage similar programs, fiscal concerns and cash flow fluctuations. Monroe County reported available fund balance of $26.1 million, or 2 percent of annual expenditures, as of December 31, 2017, but it included a $19.7 million interfund advance to the solid waste fund that has existed for at least 14 years and is not collectible in the near-term. Thus, more realistic annual reporting would show the general fund with available fund balance of $6.4 million, or .5 percent of expenditures, far below the average levels (9.7 percent) reported by other large upstate counties.

Note 13

The general fund advance to the solid waste fund is improperly reported and uncollectible in the short-term. Our Office reviews, but has no approval role for filed annual update documents (AUDs). Both the County CFO and OSC Division of Local Government and School Accountability's Data Management Unit[25] (DMU) staff informed us that – during the review of the 2017 AUD − they discussed that if the amount is truly a long-term receivable, it should be reported as non-spendable, rather than available fund balance in the general fund. County officials had told DMU staff that reported advances were short-term when, in fact, the receivable from the solid waste fund had been annually reported for over 14 years.

Note 14

Providing the financial reports to the Clerk of the Legislature was not an effective method to share the reports with the Legislators, because the Legislators were unfamiliar with the report or its availability.

Note 15

The Clerk of the Legislature did not provide us any information or documentation about verbal or other forms of Legislator requests for the monthly reports.

Note 16

The audit report does not recommend retaining excess funds. The referenced recommendation offers two options, increasing recurring revenues or decreasing recurring expenditures, to improve cash flow without incurring short-term borrowing and related interest expense or requiring long-term interfund loans.

25 The Data Management Unit reviews submitted annual update documents (AUDs).

Note 17

The first operating surplus occurred in 2016. The operating surpluses for 2016 and 2017 totaled $2.4 million, of which $1 million was from a 2017 one-time revenue that will not recur.

Note 18

The County consistently violated GML by reporting an ongoing general fund advance to the solid waste fund at year-end for over 14 years, and not recording it in the accounting records. The County lacks statutory authority to provide interfund advances on a long-term basis and just started very gradually reducing the long-term loan in 2015.

Note 19

A basic premise of internal controls is to have adequate supporting documentation for financial transactions − stored electronically or in hard copy − at the County's discretion. The County's system did not provide that. We expected this information to be available following reviews by County officials and external auditors in preparing and auditing annual financial reports. We did not anticipate the need for, or expect, the County to attempt to create records or reports for our use.

Appendix C: Audit Methodology and Standards

We conducted this audit 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. To achieve the audit objective and obtain valid audit evidence, our audit procedures included the following:

- We reviewed the County charter and any policies and procedures for information relevant to financial and budget activities and fund balance management, including a determination of County officials' fiscal responsibilities.
- We interviewed County officials to gain an understanding of the County's financial condition and to determine whether processes were in place for fiscal monitoring, budgeting, managing fund balance and providing financial oversight.
- We reviewed the County's general fund accounting records to assess whether they were accurate by determining whether balance sheet accounts as of December 31, 2017 (significant current assets and liabilities) were properly recorded, supported and currently collectible in accordance with the modified accrual basis of accounting.
- We compared the 2017 general fund accounts receivable ledger totaling $147.2 million to 2018 State payments and recorded receipts made through April 30, 2018 to determine whether they were paid.
- We compared the 2017 general fund accounts payable ledgers, totaling $43.9 million, to January, February and March 2018 check, electronic transfer and credit card registers. For 1,252 transactions, totaling $18.1 million, that did not have the same document number on both the ledgers and the registers, we judgmentally selected, based upon materiality, all 57 liabilities that were $50,000 or more, totaling $14.3 million. We randomly selected an additional 50 liabilities, totaling approximately $278,000, and compared them utilizing a purchase order and disbursement report to determine whether accounts payable were accurately stated.
- We used auditor professional judgment to determine that January was at most risk of including disbursements that should have been included in prior year liabilities. We judgmentally selected all 19 transactions of $50,000 or more from the January check, electronic transfer and credit card registers and compared them to vouchers, vendor invoices and 2017 accounts payable ledgers. We randomly selected an additional 30 disbursements, totaling $119,975 from the January, February and March 2018 registers to perform the same testing. On July 9, 2018, we discovered that the Controller's office had not provided two electronic transfers registers. As a result, we expanded our sample to include all 10 January disbursements that totaled $50,000 or more (consistent with the previous sample selection) and an additional five disbursements randomly selected. This resulted in a

sample of 64 disbursements totaling nearly $5.9 million (6.2 percent of the $94.7 million population).

- We compared 2017 general fund contractual and grant encumbrances totaling $3.2 million to invoices as of May 17, 2018 and $1.3 million of departmental encumbrances to invoices as of May 23, 2018.
- We reviewed all 22 liabilities, totaling approximately $24 million, reported as due to other governments on December 31, 2017 and compared them to 2018 check registers, invoices and County prepared schedules to determine whether they were accurately stated.
- We reviewed all 1,137 deferred revenues, totaling $2.4 million as of December 31, 2017, and compared them to grants and grant resolutions to determine whether they were recorded in the correct period.
- We reviewed support for real property tax and sales tax accruals.
- We analyzed changes in combined and general total and available fund balance.
- We compared Monroe County's 2017 general fund available and total fund balance, and combined funds' cash position, to amounts reported by all 56 NYS counties that had filed 2017 financial reports as of September 5, 2018 (excludes Cortland County). For additional perspective, we provided comparisons to the nine Finger Lakes Counties (Genesee, Livingston, Monroe, Ontario, Orleans, Seneca, Wayne, Wyoming and Yates Counties) and 14 large upstate Counties (Albany, Rensselaer, Saratoga, Schenectady, Onondaga, Oswego, Monroe, Oneida, Jefferson, St. Lawrence, Broome, Chautauqua, Erie, and Niagara Counties).
- We analyzed interfund advances for the ability of the borrowing fund to repay the short-term financing with available current assets and RANs to determine whether they were increasing or decreasing.
- We compared budget estimates to actual results for 2014 through May 2018. We reviewed the 2018 budget to determine whether revenue and appropriation estimates were reasonable.
- We analyzed the effect of absorbing the LDCs into the general and internal service funds.
- We reviewed the monthly, quarterly and annual reports available to the Legislature and inquired about the frequency of legislative requests for copies of the monthly report.

We conducted this performance audit in accordance with GAGAS (generally accepted government auditing standards). 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.

Unless otherwise indicated in this report, samples for testing were selected based on professional judgment, as it was not the intent to project the results onto the entire population. Where applicable, information is presented concerning the value and/or size of the relevant population and the sample selected for examination.

A written corrective action plan (CAP) that addresses the findings and recommendations in this report should be prepared and provided to our office within 90 days, pursuant to Section 35 of 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 the CAP available for public review in the Clerk's office.

Appendix D: Resources and Services

Regional Office Directory
www.osc.state.ny.us/localgov/regional_directory.pdf

Cost-Saving Ideas – Resources, advice and assistance on cost-saving ideas
www.osc.state.ny.us/localgov/costsavings/index.htm

Fiscal Stress Monitoring – Resources for local government officials experiencing fiscal problems
www.osc.state.ny.us/localgov/fiscalmonitoring/index.htm

Local Government Management Guides – Series of publications that include technical information and suggested practices for local government management
www.osc.state.ny.us/localgov/pubs/listacctg.htm#lgmg

Planning and Budgeting Guides – Resources for developing multiyear financial, capital, strategic and other plans
www.osc.state.ny.us/localgov/planbudget/index.htm

Protecting Sensitive Data and Other Local Government Assets – A non-technical cybersecurity guide for local government leaders
www.osc.state.ny.us/localgov/lgli/pdf/cybersecurityguide.pdf

Required Reporting – Information and resources for reports and forms that are filed with the Office of the State Comptroller
www.osc.state.ny.us/localgov/finreporting/index.htm

Research Reports/Publications – Reports on major policy issues facing local governments and State policy-makers
www.osc.state.ny.us/localgov/researchpubs/index.htm

Training – Resources for local government officials on in-person and online training opportunities on a wide range of topics
www.osc.state.ny.us/localgov/academy/index.htm

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