

# Village of Gowanda

## Sewer Financial Operations

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DECEMBER 2019

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

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# Report Highlights

## Village of Gowanda

### Audit Objective

Determine whether the Board and Village officials properly accounted for and effectively managed the financial operations of the sewer fund.

### Key Findings

- The Board overestimated revenues by \$379,000 in fiscal years 2014-15 through 2018-19, resulting in net operating deficits in the sewer fund totaling \$144,000.
- The Board did not annually review contractual revenues, resulting in potential unrealized revenue totaling approximately \$295,000.
- The Board did not document a basis for, or adequately monitor, shared service costs, resulting in possible sewer fund inequities.

### Key Recommendations

- Adopt budgets that include realistic revenue estimates.
- Review rates and contractual revenues annually and revise them, as needed, to generate sufficient revenues to cover expenditures.
- Develop an equitable basis for shared service costs and adjust it, as needed, based on actual expenditures.

Village officials agreed with our recommendations and indicated they planned to initiate corrective action.

### Background

The Village (Village) of Gowanda is located in Erie and Cattaraugus Counties. The Board of Trustees (Board) is responsible for the overall management and oversight of the Village's financial operations. The Mayor serves as the Village's chief executive and budget officer.

The Village Treasurer (Treasurer) is the chief financial officer and is responsible for maintaining the Village's accounting records. The Chief Operator is responsible for oversight of the day-to-day sewer operations.

The Village provides sewer services to Village residents and a portion of the Town of Perrysburg. The Village also contracts with the New York State Department of Corrections and Community Supervision (DOCCS) for sewage disposal at the Collins and Gowanda facilities and allows bulk disposal from permitted entities.

#### Quick Facts

Population	2,700
2018-19 Sewer Fund Expenditures	\$744,064
2018-19 DOCCS Subsidy	\$506,250

### Audit Period

June 1, 2014 – September 12, 2019

# Sewer Financial Operations

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## What Is Effective Financial Condition Management?

A board is responsible for providing oversight of sewer fund operations. This includes adopting reasonably estimated budgets based on historical trends and other known factors to ensure that recurring revenues finance recurring expenditures and a reasonable fund balance<sup>1</sup> is maintained as a cushion for unforeseen expenditures and cash flow. To properly fund sewer operations, the board needs to determine the annual cost of operations and repairs of the sewage treatment facility and also perform an analysis of future repairs and improvements. Based on that review, the board should revise the sewer user rates as necessary to generate sufficient revenues to pay the total operation and maintenance costs for the facilities and service lines.

Boards can also legally set aside, or reserve, a portion of fund balance to finance future costs for specific purposes (e.g., repairs or vehicle replacements). Once reserved, expenditures should be made in accordance with applicable laws authorizing the reserves. A village with sound financial health can consistently maintain sufficient cash flow to pay bills and other obligations when they become due without relying on other resources, such as one-time revenues or fund balance, which can indicate a deteriorating financial condition.

The general fund is the principal operating fund and includes all operations not required to be recorded in a separate fund, such as water operations and sewer operations which are accounted for in the water and sewer funds, respectively. Sharing the cost of services between operating funds can be a cost-effective way to provide like services to multiple funds. It is important to identify all costs associated with a shared service and to use an allocation method that shares the total cost equitably. Using a formula or several methods (e.g., service usage, proportion of total personnel costs) can provide a reasonable basis to help ensure costs and benefits are equally shared. These methods should be reviewed in a timely manner and adjusted as needed based on actual experience.

## The Board Did Not Effectively Manage Revenues

The Board overestimated revenues and adopted sewer fund budgets with estimated revenues that exceeded actual revenues. For the cumulative five-year period of 2014-15 through 2018-19, total actual revenues fell short of total estimates by \$379,000. Although 2018-19 was more reasonably estimated, overall the Board's budgeting practices can be improved.

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<sup>1</sup> Fund balance is the difference between revenues and expenditures accumulated over time.

**Figure 1: Sewer Fund – Estimated Revenues to Actual Comparisons**

	2014-15	2015-16	2016-17	2017-18	2018-19	Totals
<b>Estimated Revenues</b>	\$693,784	\$802,829	\$934,694	\$895,079	\$821,105	\$4,147,491
<b>Actual Revenues<sup>a</sup></b>	\$639,322	\$757,930	\$698,523	\$835,440	\$837,222	\$3,768,437
<b>(Overestimated)/ Underestimated Revenues</b>	(\$54,462)	(\$44,899)	(\$236,171)	(\$59,639)	\$16,117	(\$379,054)

a Actual revenues were calculated using billed revenue for residential, DOCCS and septic haulers. The Village's reported revenues were \$17,750 less than total actual revenue over the five-year period.

The revenue variances were primarily caused by overestimated residential rents in four of the five years. Officials were unable to provide us with documentation to support their \$115,000 (58 percent)<sup>2</sup> increase in estimated residential rents – from \$200,000 to \$315,000 – between 2015-16 and 2016-17. The increase was most likely attributed to the anticipated installation of new water meters, approved in August 2016, which would more accurately reflect usage.<sup>3</sup> Officials planned to bill four quarters after the new meters were installed and then address the need for a rate increase, which eventually went into effect in July 2017. However, even with the new meters and rate increase, residential rents still averaged \$244,000 for the 2017-18 and 2018-19 fiscal years, significantly less than the \$315,000 estimate. Village officials subsequently reduced estimated residential rents to more reasonable levels: \$250,000 in the 2018-19 and 2019-20 budgets. Additionally, the Village charges \$60 per thousand gallons for bulk disposal and received annual revenues, averaging approximately \$34,000 over the past five years, from outside septic haulers. However, officials could not recall the last time the rate for these services had been adjusted.

Additionally, the Board did not effectively monitor or manage its sewage disposal contract with DOCCS. According to the contract, DOCCS pays 75 percent of the annual operating and maintenance costs of the Village's sewer fund<sup>4</sup> in exchange for sewage disposal services. The contract also indicates that the annual contribution amount should be adjusted "not less frequently than annually... and based upon actual experience for the preceding period..." However, Village officials have not reviewed the contribution amount on an annual basis. The Village last requested an increase from DOCCS in March 2015 which increased the total contribution amount from \$438,384 (effective since June 1, 2006) to

2 At this time the Department of Public Works Superintendent assisted in budget preparation. He separated from Village service in March 2018 and current officials did not find any records of discussions that provided details on the budgeted amount. There was also a turnover in the Treasurer and Mayoral positions with the current individuals starting in January 2017 and April 2017, respectively.

3 Sewer charges are based on the amount of water used.

4 This percentage is based on a formula involving the facilities' wastewater discharge. It is not our intent to comment on this calculation but to focus solely on billing procedures and operational and maintenance costs of the sewer fund.

\$506,250, or 15 percent. However, annual operation and maintenance costs over the past three years averaged approximately \$806,000 (Figure 2). Accordingly, at the contractual subsidy rate of 75 percent, the annual payment from DOCCS would be approximately \$605,000, or an additional amount of over \$98,000, but officials have not requested an increase. As a result, the Village did not realize potential revenues approximating \$295,000 over the three years.

**Figure 2: Sewer Fund – Comparison of Actual Expenditures to DOCCS Contribution**

	2016-17	2017-18	2018-19	Total
<b>Expenditures<sup>a</sup></b>	\$929,220	\$798,764	\$690,837	\$2,418,821
<b>75 percent of Expenditures</b>	\$696,915	\$599,073	\$518,128	\$1,814,116
<b>Less: DOCCS Annual Contribution</b>	\$506,250	\$506,250	\$506,250	\$1,518,750
<b>Difference</b>	\$190,665	\$92,823	\$11,878	\$295,366

a Total expenditures have been adjusted from reported expenditures to include \$35,754 in expenditures erroneously recorded in the capital projects fund in 2016-17; and to exclude debt-related principal and interest payments totaling \$53,227 in 2018-19.

Current officials told us that they were not aware that the DOCCS contribution amount should be addressed annually and continued billing DOCCS based on past practice. Because officials were not monitoring these contractual revenues and were overestimating revenues in the annual budget, the sewer fund experienced financial condition problems.

### The Board Did Not Allocate Shared Service Costs Equitably

The Board did not ensure that the sewer fund paid its appropriate share for shared service costs or monitor actual expenditures to help ensure costs were allocated in an equitable manner. The Village’s three operating funds (general, water and sewer) share Department of Public Works (DPW) employees and certain other costs including payroll-related benefits (e.g., health insurance, retirement), insurance (e.g., general liability, workers’ compensation), vehicle replacements and administrative duties. Each fund includes its portion of the shared service costs in its operating budgets. For example, current payroll allocations are based on expected time spent by employees working in each department or vehicles purchased based on the amount of time used by each department.

For the fiscal years 2014-15 through 2018-19, we reviewed payroll costs and shared service expenditures totaling approximately \$1.18 million<sup>5</sup> to determine

5 This amount is the sewer fund share of the combined operating funds’ total expenditures of approximately \$3.19 million for 10 allocations. See Appendix B for the expenditures reviewed.

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whether the sewer fund's proportionate share was equitably allocated based on supporting documentation. In certain instances expenditures had no reasonable basis for the allocation percentages used. For example, the June 2015 Board minutes indicated that a highway employee was "moved to the sewer fund" and 100 percent of his \$44,662 earnings were charged to the sewer fund in 2015-16. However, according to his time sheets, only 220 hours should have been charged to the sewer fund (10 percent),<sup>6</sup> approximating \$4,446 in actual payroll costs during 2015-16.<sup>7</sup> This practice continued in 2016-17 through 2018-19. Additionally, in 2015-16 the Village's proportionate share of this individual's health insurance cost, totaling approximately \$4,500, was charged to the general fund.

The Treasurer told us that historically the annual retirement and workers' compensation costs were allocated based on budgeted personnel costs rather than actual expenditures or time worked by shared employees. However, if payroll costs are allocated based on budgetary expectations, rather than actual time worked, the sewer fund could be paying a disproportionate share of these costs. A Board member told us she was aware of the workers splitting time between departments and had assumed that shared costs were allocated based on actual time worked, not budgeted costs.

Additionally, we question whether shared service expenditures totaling approximately \$26,000 were allocated equitably. In January 2016, the Board approved a mileage reimbursement totaling \$4,420. Although Board minutes indicated this should be a water fund expenditure, the entire amount was charged to the sewer fund. Further, the sewer fund expended \$21,600 for building upgrades to accommodate moving the Water and Highway Departments into the Sewer Department building. We could not determine whether the Board's intent was to make this a sole cost of the sewer fund.

While it is appropriate to share costs, the basis for allocation should be clearly documented during the budget process. Budgets should be reviewed, and amended as needed, based on supported actual costs.

Without proper oversight officials cannot be sure the sewer fund is paying the appropriate share of the costs. Further, because the DOCCS contribution is based on total expenditures, it is critical that this amount includes actual, and all, sewer fund costs. After discussing with officials, they made a significant effort to provide more detailed information regarding cost allocations in the 2019-20 budget.

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6 Based on a 40-hour work week

7 This same individual only charged 56 hours totaling approximately \$1,100 to the sewer fund in 2014-15. Time clocks were used between October 2016 and February 2018 with no detailed time sheets and therefore we could not determine the amount charged during this time period.

## The Sewer Fund's Financial Condition Is Improving

The sewer fund experienced operating deficits in two of the last five fiscal years and used a portion of its reserves to fund operations. The largest operating deficit, totaling approximately \$231,000, occurred in 2016-17 and was caused, in part, by unanticipated equipment repairs totaling \$71,000.

**Figure 3: Sewer Fund – Results of Operations**

	2014-15	2015-16	2016-17	2017-18	2018-19	Totals
<b>Actual Revenues</b>	\$639,322	\$757,930	\$698,523	\$835,440	\$837,222	\$3,768,437
<b>Actual Expenditures<sup>a</sup></b>	\$688,989	\$751,423	\$929,220	\$798,764	\$744,064	\$3,912,460
<b>Operating Surplus/(Deficit)</b>	(\$49,667)	\$6,507	(\$230,697)	\$36,676	\$93,158	(\$144,023)

**a We increased the 2014-15 expenditures by \$13,214 and reduced the 2015-16 expenditures by \$11,492 to account for recording errors. We also increased expenditures in 2016-17 by \$35,754 as noted previously.**

A key measure of the Village's financial condition is its level of fund balance. The sewer fund had a total fund balance of approximately \$514,000 as of June 1, 2014, which decreased by \$144,000 (28 percent) over a five-year period to approximately \$370,000 because of the operating deficits. The majority of total fund balance, more than \$230,000 (62 percent), has been restricted in reserves for capital improvements and equipment.

Board minutes indicated that the sewer fund's financial condition has fluctuated. For example, in October 2015, the prior Treasurer indicated that because of DOCCS payments the sewer fund was "healthy" while the October 2016 minutes stated the sewer fund was spending more than it was taking in. In February 2017 a member of the finance committee stated the sewer fund was struggling financially. The Village issued revenue anticipation notes (RAN) in February 2015 (\$500,000) and March 2016 (\$350,000) to alleviate cash flow issues in the general, water and sewer funds.<sup>8</sup> However, the sewer fund still did not have enough operating cash to pay its obligations.

As of February 24, 2016, the sewer fund's operating bank accounts were nearly depleted and cash balances had dwindled to \$894. To cover documented outstanding expenditures as of this date, which totaled approximately \$16,100, the prior Treasurer transferred \$25,000 from the capital reserve account. Capital reserve funds<sup>9</sup> are statutorily restricted and typically cannot be used in this manner. We found no indication that the Board approved this transfer and the funds have not been returned to the reserve. In April 2017, the Board approved

<sup>8</sup> Proceeds were deposited into a combined operating bank account with \$25,000 of RAN proceeds recorded as transferred to the sewer operating account in April 2016.

<sup>9</sup> New York State General Municipal Law Sections 6-c and 6-g stipulate how capital reserves can be established, funded and used. Capital reserves are used to finance all or part of the cost of construction, reconstruction, or acquisition of a capital improvement or the acquisition of equipment.



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a \$10,000 transfer from the same reserve account to again be used toward operating expenditures. Without this transfer the sewer fund would not have been able to meet its May 2017 obligations totaling approximately \$24,000.

Because the Board did not adopt realistic budgets, the sewer fund incurred operating deficits and a decline in its overall financial health. However, with rate increases in effect and the adoption of more realistic revenue estimates in 2018-19 and 2019-20, there has been marked improvement. To sustain the gains in fund balance levels over the last two years, the Board should continue to monitor the operations of the sewer fund by annually reviewing the need for rate increases and revising cost allocations based on historical trends.

### **What Do We Recommend?**

The Board should:

1. Continue to adopt budgets that include reasonable revenue estimates.
2. Review rates and contractual revenues annually and revise as necessary to generate sufficient revenue to cover expenditures.
3. Document its rationale for shared service cost percentages and periodically evaluate these calculations to accurately reflect actual costs and ensure that all funds are paying their proportionate share.
4. Consult with legal counsel as needed and investigate all transfers from reserves and return any funds used improperly.

# Appendix A: Response From Village Officials

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## VILLAGE OF GOWANDA

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December 10, 2019

Jeffrey D. Mazula  
Office of the State Comptroller  
Division of Local Government and School Accountability  
295 Main Street, Suite 1032  
Buffalo, NY 14203-2510

Re: Local Official Response (LOR)  
Village of Gowanda - 2019M-199

To the Office of the Comptroller

The Village of Gowanda has received the above referenced audit report of our Sewer Financial Operations for fiscal year 2014-2015 through 2018-2019. We appreciate the diligence and professionalism of the auditors during this process to help us improve our operating and financial management.

The Village of Gowanda accepts the report and documented past practice errors and issues. This audit has validated that the Village is now moving in the right direction with new staff and budget monitoring procedures in place to provide the board with more accurate and detailed information and data needed to make appropriate financial and operating decisions.

Your report identifies (3) key findings within the Sewer financial operations that have been addressed and improved during the audit process. To date, revenues were realistically reduced and approved by the board for the current 2019-2020 budget year reflecting accurate anticipated revenue. Shared services and staff allocations have also been adjusted to reflect actual expenditures by fund. In addition, we are in the process of reviewing annual bulk disposal agreements and fees and updating the 1981 Department of Corrections Bulk Sewer Agreement for the Collins Correctional Facility.

The Village of Gowanda will provide a Corrective Action Plan (CAP) within 90 days of the official release of the final report to identify our progress. This audit was valuable to new staff and board members and we appreciate the feedback for our continuous improvement efforts.

Thank you

David Smith, Mayor  
Village of Gowanda

## Appendix B: Audit Methodology and Standards

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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 interviewed Village officials, employees and members of the finance committee and reviewed Board meeting minutes, resolutions and financial documents to gain an understanding of sewer operations and officials' oversight responsibilities regarding budgetary and fiscal control.
- We prepared budget-to-actual comparisons for revenues and appropriations to determine whether adopted budgets were reasonable and whether specific revenues were consistently and significantly overestimated.
- We analyzed the Village's financial records for fiscal years 2014-15 through 2018-19 to determine the results of operations.
- We reviewed sewer rate increases to determine their impact on revenues and whether they were sufficient to meet related expenditures.
- We reviewed the DOCCS contract language to determine the basis for the annual contribution.
- We reviewed the adopted 2019-20 budget to determine whether revenue and appropriation estimates were reasonable.
- We recalculated material annual revenues (residential, DOCCS and outside haulers) using actual billings, compared them with reported revenues and discussed any large variances with officials.
- We reviewed certain accounting entries affecting revenues and expenditures to verify whether they were supported. We discussed erroneous or missing entries with officials and modified our estimated revenues and expenditures based on this review.
- We identified and discussed with officials shared service cost procedures and percentage allocations that occurred during the 2014-15 through 2019-20 fiscal years. We reviewed the actual costs for shared service expenditures including health insurance, workers' compensation insurance, retirement, Social Security, unallocated insurance (e.g., general liability), administrative (meter reading and bookkeeping), vehicle replacements, building upgrades, a consulting service agreement and one mileage reimbursement (due to the material amount). We recalculated allocations to the sewer fund using adopted budgets and actual expenditures to determine whether the Village's allocation methods were reasonable.
- We used available timekeeping records including time sheets, calendars and monthly reports to the New York State Department of Environmental Conservation to determine the number of recorded hours of sewer

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department personnel. We compared recorded hours against payroll registers and the accounting records to determine whether amounts charged to the Sewer Department were supported.

- We reviewed accounting records and Board minutes to determine whether payments made from reserve funds were authorized and for appropriate purposes.

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.

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 Village Clerk's office.

## Appendix C: Resources and Services

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### **Regional Office Directory**

[www.osc.state.ny.us/localgov/regional\\_directory.pdf](http://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](http://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](http://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#lmgm](http://www.osc.state.ny.us/localgov/pubs/listacctg.htm#lmgm)

### **Planning and Budgeting Guides** – Resources for developing multiyear financial, capital, strategic and other plans

[www.osc.state.ny.us/localgov/planbudget/index.htm](http://www.osc.state.ny.us/localgov/planbudget/index.htm)

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[www.osc.state.ny.us/localgov/pubs/cyber-security-guide.pdf](http://www.osc.state.ny.us/localgov/pubs/cyber-security-guide.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](http://www.osc.state.ny.us/localgov/finreporting/index.htm)

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