



# City of Saratoga Springs Financial Condition

## Report of Examination

Period Covered:

January 1, 2008 — December 31, 2011

2012M-201



Thomas P. DiNapoli

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# State of New York Office of the State Comptroller

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

February 2013

Dear City Officials:

A top priority of the Office of the State Comptroller is to help local government officials manage government resources efficiently and effectively and, by so doing, provide accountability for tax dollars spent to support government operations. The Comptroller oversees the fiscal affairs of local governments statewide, as well as compliance with relevant statutes and observance of good business practices. This fiscal oversight is accomplished, in part, through our audits, which identify opportunities for improving operations and City Council governance. Audits also can identify strategies to reduce costs and to strengthen controls intended to safeguard local government assets.

Following is a report of our audit of City of Saratoga Springs, entitled Financial Condition. This audit was conducted pursuant to Article V, Section 1 of the State Constitution and the State Comptroller's authority as set forth in Article 3 of the General Municipal Law.

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

Respectfully submitted,

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

# Introduction

## Background

The City of Saratoga Springs is located in Saratoga County and encompasses approximately 28 square miles. The City's population is approximately 28,000. The City provides police and fire protection, parks, recreation, snowplowing, water, sewer, and street maintenance services. The City's reported 2011 operating expenditures totaled \$35.4 million for the general fund, \$2.5 million for the water fund, and \$3.5 million for the sewer fund. The City's annual budget for the 2012 fiscal year was \$37.2 million for the general fund, \$2.9 million for the water fund, and \$3.7 million for the sewer fund. The City's expenditures were funded primarily with revenues from real property and sales taxes, water and sewer rents, and State aid.

The City is governed by its Charter and other general laws of the State of New York. The City Council (Council), consisting of five members, has overall responsibility for the City's operations. The Commissioner of Finance and other administrative staff are responsible for overseeing and managing the City's financial operations. The Finance Department provides the Council with quarterly financial reports, as required by the City Charter.

The Council is responsible for ensuring that sufficient resources are available to fund the cost of City operations. The annual budget for each operating fund is expected to provide a reasonable estimate of appropriations, revenues, and other financing sources. Periodic reporting and review of budgetary status and other interim and year-end reports are a means to ensure that appropriate fiscal and internal control monitoring frameworks are in place and operating effectively. The Council's ability to review such reports on a timely basis and promptly take actions warranted by the City's financial status are integral components impacting the City's overall fiscal success.

## Objective

The objective of our audit was to review the financial condition of the City's general, water and sewer funds. Our audit addressed the following related question:

- Does the Council adopt realistic budgets that are structurally balanced, routinely monitor financial operations and take appropriate action to maintain the City's financial stability?

## Scope and Methodology

We interviewed appropriate City officials, examined financial records and reviewed various procedures of the City for the period January 1, 2008, to December 31, 2011. Subsequent to our fieldwork, City officials provided us with a trial balance as of October 31, 2012 and the 2013 adopted budget.

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 City officials and their comments, which appear in Appendix A, have been considered in preparing this report. City officials generally agreed with our recommendations and indicated they planned to initiate corrective action.

The Council has the responsibility to initiate corrective action. A written corrective action plan (CAP) that addresses the findings and recommendations in this report should be prepared and forwarded to our office within 90 days, pursuant to Section 35 of the General Municipal Law. For more information on preparing and filing your CAP, please refer to our brochure, *Responding to an OSC Audit Report*, which you received with the draft audit report. We encourage the Council to make this plan available for public review in the City Clerk's office.

## Financial Condition

An essential component of the Council's duties and responsibilities is to make sound financial decisions that are in the best interest of the City and the taxpayers that fund its operations. This responsibility requires Council members to balance the level of services desired and expected by City residents with the ability and willingness of the residents to pay for such services. It is essential that the Council adopt structurally balanced budgets for all of its operating funds that provide recurring revenues to finance recurring expenditures. Also, effective management includes monitoring budgets during the course of the year and making any budgetary amendments that become necessary due to revenue shortfalls or from actual costs exceeding the appropriations provided for in the adopted budgets.

Since our last audit of the City's financial condition,<sup>1</sup> the general fund's unexpended surplus<sup>2</sup> has significantly increased from \$165,723 on December 31, 2006 to \$6.2 million on December 31, 2011. As of October 31, 2012, the fiscal year 2012 general fund budget of \$37.2 million appears on track with City officials not anticipating an operating deficit. Also, while the financial condition of the water and sewer funds has improved during our audit period, the water fund balance continues to remain in a deficit. As of October 31, 2012, the fiscal year 2012 water budget of \$2.97 million and sewer budget of \$3.67 million appear generally on track with City officials anticipating a small operating deficit in each fund.

During the period reviewed, the Council did not address cash flow problems in the water and sewer funds. Instead, the Council routinely relied on increasing amounts of inter-fund loans from the general fund to finance operations in the water and sewer funds. The combined balance of outstanding inter-fund loans from the general fund to the water and sewer funds has increased from approximately \$1.4 million

<sup>1</sup> We last audited the City's financial condition for the period January 1, 2003 – December 31, 2006. The results of this audit were documented in our report entitled *Financial Condition*, which was issued in March 2008.

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

on January 1, 2008 to \$1.8 million on December 31, 2011, with no plan for repayment.

**General Fund** — Since 2008, the City's general fund unexpended surplus has increased by about \$2.4 million, from \$3.8 million in 2008 to \$6.2 million in 2011. The increase is primarily due to conservative budgeting and adequate monitoring during the year of actual revenues and expenditures in comparison to the budgeted amounts. These practices have, in part, resulted in operating surpluses in three of the last four years and placed less reliance on appropriating unexpended surplus funds to finance general fund operations. These operating surpluses have also helped eliminate the need to issue tax anticipation notes (TAN)<sup>3</sup> which have been issued in three of the last four years to finance current operations in the general fund. In 2012, the City had sufficient general fund cash balances and did not need to issue a TAN to meet current obligations while waiting for real property tax revenues. As of October 31, 2012, the fiscal year 2012 general fund budget of \$37.2 million appears on track with \$31.8 million in revenues recognized and \$27.5 million in expenditures incurred. City officials do not anticipate an operating deficit for 2012.

<b>Table 1: General Fund</b>				
	<b>2008</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>
Beginning Fund Balance	\$6,887,126	\$7,716,611 <sup>a</sup>	\$5,905,246 <sup>a</sup>	\$6,984,857 <sup>a</sup>
Operating Surplus/(Deficit)	\$832,504	(\$1,809,265)	\$1,106,611	\$3,513,917
Ending Fund Balance	\$7,719,630	\$5,907,346	\$7,011,857	\$10,498,774
Less: Restricted Fund Balance	\$2,954,321	\$2,992,489	\$2,809,809	\$4,312,953
Less: Appropriated Unexpended Surplus	\$928,535	\$62,313	\$0	\$0
Unexpended Surplus Funds	\$3,836,774	\$2,852,544	\$4,202,048	\$6,185,821

<sup>a</sup> Differences between the beginning and prior year ending fund balances are due to prior year adjustments.

**Water Fund** — The water fund has shown little sign of improvement since our last audit<sup>4</sup> and continues to report fund balance deficits and periodic operating deficits. During the period reviewed, the water fund experienced two annual operating surpluses and two operating deficits. The operating surpluses were not sufficient to significantly reduce the trend of fund balance deficits. From the end of 2008 through the end of 2011, fund balance deficits decreased from \$197,425 to \$129,005. As of October 31, 2012, the fiscal year 2012 water fund budget of \$2.97 million appears on track with \$2.3 million in revenues recognized and \$2 million in expenditures incurred. City officials said that they anticipate a minor operating deficit for 2012.

<sup>3</sup> Tax anticipation notes are short-term debt issued when cash balances are not sufficient to finance operations. These loans are paid back to the lending institutions when the related tax revenue is received.

<sup>4</sup> For the year ending 2006, the water fund reported an unexpended surplus fund balance of negative \$39,895.



<b>Table 2: Water Fund</b>				
	<b>2008</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>
Beginning Fund Balance	\$463,029	\$342,395	\$440,520	\$712,897
Operating Surplus/(Deficit)	(\$120,634)	\$98,125	\$272,377	(\$86,849)
Ending Fund Balance	\$342,395	\$440,520	\$712,897	\$626,048
Less: Restricted Fund Balance <sup>a</sup>	\$539,820	\$648,281	\$764,506	\$755,053
Less: Appropriated Unexpended Surplus	\$0	\$0	\$0	\$0
Unexpended Surplus/(Deficit) Funds	(\$197,425)	(\$207,761)	(\$51,609)	(\$129,005)
<sup>a</sup> Per the annual Board-approved water rate schedule, a portion of the water fees are dedicated to capital improvements and are recorded in a capital reserve. The Board uses the reserve moneys to pay down the capital debt and to make improvements to the water system's infrastructure.				

**Sewer Fund** — The sewer fund operations have shown little overall improvement since our last audit.<sup>5</sup> Following two years of operating deficits, the sewer fund experienced two years of operating surpluses in 2010 and 2011 that have helped to increase the level of unexpended surplus funds. The operating deficits in 2008 and 2009 were primarily due to an over estimation of revenues. Since 2008, the total unexpended surplus reported has increased \$105,000 from \$140,163 in 2008 to \$245,585 in 2011. As of October 31, 2012, the fiscal year 2012 sewer fund budget of \$3.67 million appears on track with \$2.8 million in revenues recognized and \$2.7 in expenditures incurred. City officials said that they anticipate a minor operating deficit for 2012.

<b>Table 3: Sewer Fund</b>				
	<b>2008</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>
Beginning Fund Balance	\$281,206	\$157,272	\$1,254	\$216,122
Operating Surplus/(Deficit)	(\$123,934)	(\$156,018)	\$214,868	\$51,151
Ending Fund Balance	\$157,272	\$1,254	\$216,122	\$267,273
Less: Restricted Fund Balance	\$17,109	\$21,313	\$17,752	\$21,688
Less: Appropriated Unexpended Surplus	\$0	\$0	\$0	\$0
Unexpended Surplus (Deficit) Funds	\$140,163	(\$20,059)	\$198,370	\$245,585

While the general fund and the sewer fund have experienced increases in their unexpended surpluses by generating periodic annual operating surpluses, the water fund has not had consistent and adequate levels of annual operating surpluses to significantly reduce its fund balance deficit. Annually, the Council authorizes increases in water and sewer

<sup>5</sup> For the year ending 2006, the sewer fund reported an unexpended surplus fund balance of \$227,022.



rents; however, these increases were not sufficient to address the water fund's fund balance deficit. Furthermore, the Council lacks a formal long-term plan to improve the financial condition of the water fund and is instead relying on inter-fund borrowings to meet the water funds cash flow needs.

Inter-fund Loans — The Council may authorize inter-fund loans between funds. Inter-fund loans are intended to meet periodic, short-term cash flow needs and are to be paid back by the end of the fiscal year in which the loans are made. We found that inter-fund loans were not paid back timely. Specifically, the water and sewer funds have annually borrowed from the general fund and these loans remain unpaid with no apparent plan to repay them. From the beginning of 2008 through the end of 2011, inter-fund loans to the water fund have increased by \$117,213, from \$692,537 to \$809,750. During this same period, inter-fund loans to the sewer fund have increased by \$273,882, from \$728,571 to over \$1 million. We reviewed the City's water and sewer fund trial balances as October 31, 2012 and found these inter-fund loans continue in 2012.

The water and sewer funds have been unable to repay these inter-fund loans and there was no indication of a Council plan or solution to address the repayment of these loans. With no plan to address the repayment of the inter-fund loans, the insufficient cash flow of the water and sewer funds places a burden on the general fund's cash liquidity and this burden could increase should the financial condition of the water and sewer funds decline. In addition, property taxpayers are subsidizing water and sewer system users because the user fees are not sufficient to pay the cost for the services used. As such, it is critical for the Council to take a more active role in monitoring the fiscal condition and cash flows of the water and sewer funds and establish a plan for the water and sewer funds to pay back the money borrowed from the general fund.

Budget Estimates — It is important for the Council to adopt realistic budgets and monitor the actual results and budgeted estimates of each fund regularly throughout the year. The annual budget is a plan, subject to modifications when appropriate, that provides City officials with the information necessary to control its spending and ensure revenue projections are being met during the year. Based on its observations and future expectations, the Council must make revisions to its budgetary estimates to ensure the City meets its revenue projections and does not expend moneys beyond the level of appropriations.

The City's practice of conservative budgeting and budget monitoring has generally resulted in actual expenditures falling below estimates to compensate for revenues falling below projected levels. For

example, general fund expenditures fell below estimates in all of the last four fiscal years with the variance ranging from a high of \$1.9 million in fiscal year 2009 to a low of \$600,000 in fiscal year 2011.

The Finance Department monitors the day-to-day financial operations and monitors those operations against the budget, prepares period financial reports for the Council,<sup>6</sup> and proposes budget adjustments. The monitoring procedures and conservative budgeting have resulted in a significant increase in the general fund balance and a modest increase in the sewer fund balance. However, this has not resulted in any significant improvement in the water fund balance. Specifically, the Council has consistently overestimated water revenues from year-to-year. Because water revenues can fluctuate from year-to-year depending on customer usage and result in operating deficits, a plan to conservatively estimate revenues may help offset the water fund deficit.

City officials are aware of the negative financial trends that have been affecting the City's water and sewer operating funds, including lack of sufficient cash flows to finance current operations, and have indicated that they will develop a plan of corrective action. We reviewed the 2013 general fund budget of \$39.86 million, water fund budget of \$3 million and sewer budget of \$3.8 million and did not identify any significant concerns. City officials said that they plan to increase water and sewer user fees in 2013 to support the budget increases in these respective funds. Because the City has experienced a pattern of actual water and sewer revenues falling short of budgeted collections, officials should ensure that any future increases in water and sewer rates are sufficient to meet the funds operating needs.

## **Recommendations**

1. The Council should monitor whether recurring revenue sources are sufficient to finance operations in the water and sewer funds and take appropriate action as necessary to improve the funds' financial condition. This may include the review of monthly cash flows, re-evaluating the sufficiency of the current water and sewer rate structures and monitoring fluctuations in fund balance to evaluate the results of any corrective action taken.
2. The Council should establish a plan to repay the inter-fund loans between the general, water and sewer funds.

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<sup>6</sup>These reports include a quarterly budget-to-actual report.

## **APPENDIX A**

### **RESPONSE FROM LOCAL OFFICIALS**

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



**City of Saratoga Springs**  
**OFFICE OF COMMISSIONER OF FINANCE**

**MICHELE D. CLARK-MADIGAN**  
COMMISSIONER OF FINANCE

474 Broadway - City Hall  
Saratoga Springs, New York 12866-2296  
518-587-3550  
Fax 518-580-0781

M. LYNN BACHNER  
Deputy Commissioner

CHRISTINE A. GILLMETT-BROWN  
Director of Finance

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KAMERON D. KLIPPEL  
Benefits Administrator

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Payroll Administrator

February 8, 2013

Office of the State Comptroller  
Division of Local Government and School Accountability  
One Broad Street  
Glens Falls, NY 12801

To whom it may concern:

The City has received the Financial Condition Report of Examination for the period January 1, 2008 – December 31, 2011. Recommendations were made for the City Council to continue to monitor whether recurring revenue sources are sufficient to finance operations of the water and sewer funds and to establish a plan to repay inter-fund loans between the general, water and sewer funds.

In the past few years the City Council has been working diligently to enact proper budgeting practices to improve the financial condition of the City's water and sewer funds, as well as for all funds. This involved moderately increasing water and sewer rates over a number of years. It also included the presentation of periodic financial reports by the Commissioner of Finance at regularly scheduled City Council meetings.

More recently, the Commissioner of Finance has consulted with the City's independent auditors to develop a multi year plan that will incorporate not only rate increases but also budget analysis, and cash flow evaluation. The purpose of the plan would be to improve the financial condition in both funds and to repay the inter-fund loans. In addition, the Commissioner of Finance plans to have a fund balance policy drafted for the water and sewer funds and presented to Council, once the financial condition of the funds have improved, in order to maintain a positive financial position.

The City Council will continue its discussions and will take action to ensure proper budgeting of all revenues and expenses for all City funds. The Commissioner of Finance

will continue to bring to the Council's attention any significant budget variances, positive and negative, and to make periodic reports on the City's financial condition.

Respectfully submitted,

**Michele D. Clark-Madigan**  
Commissioner of Finance

Cc: Saratoga Springs City Council

## **APPENDIX B**

### **AUDIT METHODOLOGY AND STANDARDS**

To accomplish our objective, we interviewed appropriate City officials and employees, tested selected records, and examined pertinent documents for the period January 1, 2008, through December 31, 2011. Our procedures included the following:

- We obtained an understanding of the internal controls related to the City's records and reports, budget development and monitoring process.
- We reviewed the minutes of Council meetings from January 2011 through December 2011 to obtain information related to the Council's financial oversight.
- We analyzed revenues and expenditure trends, inter-fund loans and the changes in fund balance of the general, water and sewer funds for the 2008 through 2011 fiscal years, as reported in the City's annual update document.
- We analyzed the cash flows of the water and sewer fund for the 2011 fiscal year and the ability of the funds to pay off existing inter-fund loans.

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

## **APPENDIX C**

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