



# Village of Hamilton

## Financial Management and Internal Controls Over Selected Financial Operations

### Report of Examination

Period Covered:

June 1, 2009 — September 30, 2010

2011M-219



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**

January 2012

Dear Village Officials:

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

Following is a report of our audit of the Village of Hamilton, entitled Financial Management and Internal Controls Over Selected Financial Operations. 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*



## State of New York Office of the State Comptroller

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# EXECUTIVE SUMMARY

The Village of Hamilton (Village) is located within the Towns of Hamilton, Madison, and Eaton in Madison County. The Village is governed by a Board of Trustees (Board) which comprises four elected Trustees and an elected Mayor. Operating expenditures for the fiscal year ended May 31, 2010, were approximately \$2.7 million in the general fund and \$460,000 in the water fund. These expenditures were funded primarily with revenues from real property taxes and water rents.

### **Scope and Objectives**

The objectives of our audit were to review the Village's financial management and internal controls over selected financial operations for the period June 1, 2009, to September 30, 2010. We extended the scope of our audit to review financial information for the fiscal years 2005-06 through 2008-09. Our audit addressed the following related questions:

- Did the Board provide adequate oversight of the Village's financial activities and records to ensure that Village resources are used effectively?
- Are internal controls over non-payroll cash disbursements appropriately designed and operating effectively to safeguard Village assets?
- Do the Village's bidding practices encourage competition to ensure goods and services are procured in the most economical manner without the influence of favoritism?

### **Audit Results**

The Village's budgeting practices in the general and water funds have resulted in the general fund having approximately \$1.3 million of unappropriated, unreserved fund balance and the water fund having approximately \$703,000. The Board and Village officials consistently overestimated expenditures and underestimated revenues over the last five years,<sup>1</sup> which resulted in annual operating surpluses and increases to fund balance totaling approximately \$718,000 in the general fund and \$275,000 in the water fund. Despite these surpluses, the Board increased the Village's real property tax levy by approximately \$200,000 during the past five years. The Board also increased the water rates in three of the last five years<sup>2</sup> by \$0.35 per cubic foot for Village residents and \$0.43 per cubic foot for properties outside of the Village limits. The \$1.3 million in unreserved, unappropriated fund balance in the general fund represented 96 percent of the Village's last year's tax levy.

<sup>1</sup> 2005-06 through 2009-10

<sup>2</sup> For usage above 200 cubic feet

In addition to the lax budgeting practices, the Board did not ensure that the Clerk-Treasurer maintained adequate accounting records or provided adequate monthly reports. Without appropriate and accurate information, the Board was unable to properly develop and monitor the Village's budgets. As a result, Village officials overspent 33 budget line items totaling approximately \$706,000 in the 2009-10 fiscal year and seven budget line items totaling approximately \$45,000 in the 2010-11 fiscal year.

The Board also did not ensure that the Clerk-Treasurer relieved delinquent water and sewer rents onto the account holders' property taxes. Instead, the Village pursued collection of unpaid water and sewer rents through the Court system, thereby violating Village Law and unnecessarily using Court resources. In addition, the Clerk-Treasurer was not reconciling the Village's bank account in a timely manner, and was not making appropriate corrections to the accounting records identified during the bank account reconciliation process. As a result, the Clerk-Treasurer was creating inaccurate financial records that did not provide an accurate picture of the Village's finances. These discrepancies were not identified because the Mayor was not performing an effective review of the Clerk-Treasurer's bank reconciliations.

The Board does not have non-payroll cash disbursement or claims processing policies in place. The Clerk-Treasurer performs incompatible duties, such as maintaining accounting records and performing disbursement transactions, without any supervisory or Board oversight. As a result, unauthorized or improper non-payroll cash disbursements could be made and not detected in a timely manner.

Also, because the Board has not established claims processing procedures, claims against the Village were not always audited. The claims that arrive after the Board meeting and before the date the checks are issued are not audited by the Board. In addition, Village officials used three debit cards to purchase items that were direct charges to the Village's checking account and circumvented the claims audit process. The Board's failure to ensure that all claims are audited and approved prior to payment increases the risk that the Village could erroneously pay for items that are not authorized or valid Village expenditures, make duplicate payments, or pay for goods and services that have not actually been received.

We also found that Village officials did not always comply with General Municipal Law when making purchases. We reviewed 10 purchases totaling approximately \$910,000 to determine whether Village officials advertised for bids or purchased from State or County contracts as required and found discrepancies with five of the 10 purchases. Village officials did not use competitive bidding for three of the 10 purchases totaling \$71,048 for two pickup trucks, a tractor, and a lawnmower. Additionally, for another purchase for a fire rescue truck totaling \$532,393, Village officials were unable to locate the bid documentation. Therefore, Village officials and taxpayers have no assurance that an appropriate competitive bidding process was used. Also, Village officials inappropriately restricted vendor competition when purchasing a garbage truck for \$129,450 by failing to adopt a standardizing resolution and by using bid advertisements that solely stipulated the product of a particular manufacturer. The Village could have saved \$1,178 had it purchased the truck from the lowest bidder.

### **Comments of Local Officials**

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

# Introduction

## Background

The Village of Hamilton (Village) is located within the Towns of Hamilton, Madison, and Eaton in Madison County, and has a population of about 4,200. The Village is governed by a Board of Trustees (Board) which comprises four elected Trustees and an elected Mayor. The Board is responsible for the general management and control of the Village's financial affairs. The Clerk-Treasurer is the Village's chief fiscal officer and is responsible for maintaining custody of the Village moneys, maintaining appropriate accounting records, and preparing monthly and annual financial reports.

The Village offers a variety of services to its residents, including street maintenance, snow removal, police, recreation, garbage pickup, water, sewer, electric, and general government support. Operating expenditures for the 2010 fiscal year were approximately \$2.7 million in the general fund and \$460,000 in the water fund. These expenditures were funded primarily with revenues from real property taxes and water rents.

## Objectives

The objectives of our audit were to review the Village's financial management and internal controls over selected financial operations for the period June 1, 2009, to September 30, 2010. Our audit addressed the following related questions:

- Did the Board provide adequate oversight of the Village's financial activities and records to ensure that Village resources are used effectively?
- Are internal controls over non-payroll cash disbursements appropriately designed and operating effectively to safeguard Village assets?
- Do the Village's bidding practices encourage competition to ensure goods and services are procured in the most economical manner without the influence of favoritism?

## Scope and Methodology

We examined the Village's financial condition and internal controls over selected financial operations for the period June 1, 2009, to September 30, 2010. We extended the scope of our audit to review financial information for the fiscal years 2005-06 through 2008-09.

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

**Comments of  
Local Officials and  
Corrective Action**

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

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

# Financial Management

One of the most important tools for managing a Village's financial condition is the budget process. Village officials must ensure that budgets are prepared, adopted and modified in a prudent manner, accurately depicting the Village's financial activity while also using available resources to benefit Village taxpayers.

The Village's budgeting practices in the general and water funds have resulted in the general fund having approximately \$1.3 million of unreserved, unappropriated fund balance and the water fund having approximately \$703,000. The Board and Village officials consistently overestimated expenditures and underestimated revenues over the last five years,<sup>3</sup> which resulted in annual operating surpluses and increases in fund balance totaling approximately \$718,000 in the general fund and \$275,000 in the water fund. Despite the surpluses, the Board increased the Village's real property tax levy by approximately \$200,000 during the past five years. The Board also increased the water rates in three of the last five years<sup>4</sup> by \$0.35 per cubic foot for Village residents and \$0.43 per cubic foot for properties outside of the Village limits.

## Budgeting and Use of Fund Balance

The Board is responsible for making sound financial decisions that are in the best interests of the Village and the taxpayers. This requires the Board to balance the level of services desired and expected by the Village's residents with the ability and willingness of the residents to pay for such services. The Board is allowed to retain a reasonable portion of fund balance, referred to as unreserved, unappropriated fund balance,<sup>5</sup> to be used as a financial cushion in the event of unforeseen circumstances. The Board also is allowed to establish and fund reserves to finance the future costs for a variety of purposes.<sup>6</sup> However, it is important that the Board follow proper budgeting practices to reduce the need to raise real property taxes. It also is important that the Board adopt long-term plans to ensure that the moneys accumulated in the operating funds and reserve funds are reasonable and used for appropriate purposes.

<sup>3</sup> 2005-06 through 2009-10

<sup>4</sup> For usage above 200 cubic feet

<sup>5</sup> Fund balance represents the resources remaining from prior fiscal years that can be appropriated as funding sources in the next year's budget to reduce the amount of revenues needed to be raised from other sources.

<sup>6</sup> The statutes under which reserve funds are established determine how they may be funded, expended, and discontinued. The Board is responsible for ensuring that reserve funds are maintained in accordance with statutory requirements and are in the best interest of the Village.

We compared the Village's general and water funds' budgeted revenues and expenditures with actual results of operations for the last five fiscal years. Village officials underestimated general fund revenues by approximately \$859,000 and overestimated expenditures by a total of \$93,000<sup>7</sup> for a total budget variance of \$952,000. In the water fund, Village officials overestimated expenses by \$351,000. Village officials were unable to provide justification for the following unrealistic budget estimates:

- Although annual interest on debt service is established per debt service schedules and is a fixed amount, Village officials budgeted for significantly more interest costs in the general and water funds for four of the last five years than they knew they were going to actually pay, by as much as 105 percent. The total amount of overestimated interest in the general fund for four of the last five years was \$170,927, and in the water fund it was \$178,617.
- Although debt principle payments are established per debt service schedules and are a fixed amount, Village officials budgeted for significantly more principle costs in the general fund than they knew they were going to actually pay for the last five years, by as much as 44 percent for a total of \$223,614.
- In the water fund, Village officials budgeted for a total of \$70,903 to be transferred into reserve funds in four of the last five years. However, officials actually transferred only \$10,000.

Tables 1 and 2 show how Village officials' budgeting practices have affected fund balance in the general fund and water fund, respectively.

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<sup>7</sup> The \$93,000 of overestimated expenditures is relatively low because Village officials also made unbudgeted expenditures from the general fund totaling over \$562,000. Village officials transferred more than \$433,000 to the sewer fund from the general fund and purchased a garbage truck for \$129,450 which they did not provide for in the budget in 2009-10. Refer to Table 1 for further information regarding the general fund's operating deficit.

<b>Table 1: General Fund</b>					
	<b>FY 2005-06</b>	<b>FY 2006-07</b>	<b>FY 2007-08</b>	<b>FY 2008-09</b>	<b>FY 2009-10</b>
Beginning Fund Balance	\$374,978	\$594,966	\$924,930	\$1,278,743	\$1,466,797
Actual Revenues	\$2,154,539	\$2,276,183	\$2,512,113	\$2,417,637	\$2,575,993
Actual Expenditures	\$1,927,009	\$1,946,229	\$2,158,300	\$2,256,053	\$2,697,050
<b>Operating Surplus/ (Deficit)</b>	<b>\$227,530</b>	<b>\$329,954</b>	<b>\$353,813</b>	<b>\$161,584</b>	<b>(\$121,057)</b>
Prior Period Adjustments <sup>a</sup>	(\$7,542)	\$10	\$0	\$26,470	\$21,160
Year-End Fund Balance	\$594,966	\$924,930	\$1,278,743	\$1,466,797	\$1,366,900
Less: Reserved Fund Balance	\$29,801	\$99,801	\$91,500	\$77,817	\$84,055
Unreserved, Unappropriated Fund Balance <sup>b</sup>	\$565,165	\$825,129	\$1,187,243	\$1,388,980	\$1,282,845

<sup>a</sup> The Clerk/Treasurer was unable to provide documentation to support the adjustments in 2005-06 and 2008-09.  
<sup>b</sup> The Village did not appropriate any fund balance over the last five years.

At the end of the 2009-10 fiscal year, the Village's general fund had an operating loss. This loss was the result of two large unbudgeted transactions. The first was for the purchase of a garbage truck for \$129,450 and the second was an interfund transfer of \$433,058 to the sewer fund. If Village officials had not incurred these unbudgeted expenses, the Village would have ended the year with another large operating surplus.

<b>Table 2: Water Fund</b>					
	<b>FY 2005-06</b>	<b>FY 2006-07</b>	<b>FY 2007-08</b>	<b>FY 2008-09</b>	<b>FY 2009-10</b>
Beginning Fund Balance	\$329,297	\$438,603	\$497,796	\$659,113	\$709,198
Actual Revenues	\$624,693	\$587,855	\$654,258	\$497,093	\$469,536
Actual Expenditures	\$511,377	\$528,662	\$492,941	\$484,658	\$459,389
<b>Operating Surplus</b>	<b>\$113,316</b>	<b>\$59,193</b>	<b>\$161,317</b>	<b>\$12,435</b>	<b>\$10,147</b>
Prior Period Adjustments	(\$4,010)	\$0	\$0	\$37,650	\$3,992
Year-End Fund Balance	\$438,603	\$497,796	\$659,113	\$709,198	\$723,337
Less: Reserved Fund Balance	\$10,000	\$20,000	\$20,000	\$20,002	\$20,315
Unreserved, Unappropriated Fund Balance <sup>a</sup>	\$428,603	\$477,796	\$639,113	\$689,196	\$703,022

<sup>a</sup> The Village did not appropriate any fund balance over the last five years.

As a result of the consistent use of unrealistic budget estimates over the last five years, the Village's unreserved, unappropriated fund balance in the general fund has grown by 127 percent and in the water fund by 64 percent. During this same time, the Board increased the tax levy by approximately \$200,000, or 18 percent, and increased water rates by \$0.35 per cubic foot for Village residents and \$0.43 per cubic foot for properties outside the Village, or 13 percent. Therefore, Village residents were being taxed during this time period to finance Village operations for which the Village already had moneys available.

## **Accounting Records and Reports**

The Clerk-Treasurer, as chief fiscal officer, is responsible for maintaining custody of all Village moneys, collecting and depositing cash received, performing basic accounting functions, including maintaining accounting records, signing checks, providing monthly financial reports to the Board, and filing the Village's annual financial reports with the Office of the State Comptroller on a timely basis. Accounting records and reports are essential tools that the Board should use to monitor Village financial operations. Their importance increases the need for them to be complete and accurate. It also is important that the Clerk-Treasurer perform monthly bank-to-book reconciliations of cash. Any differences must be promptly documented and resolved to ensure that financial activities are accounted for in a proper and timely manner.

The Village's records and reports are inadequate. The Clerk-Treasurer was not providing the Board with adequate monthly reports. The Village's bank account was not being reconciled in a timely manner, and the Village's delinquent water and sewer rents were not being relieved (added to the delinquent water and sewer users' property taxes).

Monthly Reports — Good management practices require the Clerk-Treasurer to provide monthly financial reports to the Board that include budget-versus-actual comparisons for total revenues and expenditures, individual revenue and expenditure accounts, and totals for balance sheet accounts.

The Clerk-Treasurer did not provide complete and accurate monthly financial reports to the Board. During the Board meetings, the Clerk-Treasurer did not provide any written reports to the Board, but verbally reported the percentage of budgeted revenues and expenditures that the Village had received or expended as of the last completed month. She did not provide any budget-versus-actual comparisons for total revenues and expenditures, total individual revenue and expenditure accounts, or totals for balance sheet accounts. Without appropriate and accurate information, the Board was unable to properly develop and monitor the Village's budgets.

Also, the Board did not have a comprehensive understanding of the Village's overall financial condition.<sup>8</sup> As a result, we found the following budget-related issues:

- During the 2009-10 fiscal year, Village officials overspent 33 budget lines items totaling approximately \$706,000.
- During the 2010-11 fiscal year, within three months of the beginning of the fiscal year, Village officials overspent seven budget line items totaling approximately \$45,000.
- By July 2009, one month into the Village's 2009-10 fiscal year, Village officials over expended the general fund's refuse collection and disposal account by \$129,450. The Village purchased a garbage truck that had not been included in the adopted budget. Because the Board was not monitoring the budget and did not know these budget items were overspent, it did not complete a budget transfer to cover the appropriation.
- By August 2010, two months into the Village's 2010-11 fiscal year, Village officials over expended the general fund's attorney fees account by approximately \$33,000. Because the Board was not monitoring the budget and did not know this budget item was overspent, it did not complete a budget transfer to cover the appropriation.

Without periodic, accurate reports, the Board is limited in its ability to effectively monitor and make informed decisions concerning the Village's financial activities.

Delinquent Water and Sewer Rents — Village Law requires the Clerk-Treasurer to provide the Board with an annual accounting of delinquent water and sewer rents. Also, the law requires the Board to certify the list of delinquent amounts and to ensure that the Clerk-Treasurer adds the delinquent amounts to the real property taxes of the water and sewer account holders who are delinquent.

The Clerk-Treasurer did not provide the Board with an annual list of the Village's delinquent water and sewer rents, and the Board did not ensure that the delinquent amounts were added to the account holders' real property taxes. Instead, the Village pursued collection of unpaid water and sewer rents through the Court system, thereby unnecessarily using Court resources. Village officials told us they knew they could relevel delinquent water rents, but they did not know they could relevel delinquent sewer rents. However, during our audit

<sup>8</sup> Refer to the Budgeting and Use of Fund Balance section for further information

period, none of the Village's delinquent water or sewer rents were added to the account holders' property taxes.

Because the Board did not ensure that delinquent water and sewer rents were relieved onto the account holders' property taxes, the Village did not collect approximately \$3,000 in delinquent payments by adding them to the delinquent account holders' property taxes for the 2009-10 fiscal year.

Bank Reconciliations — Monthly reconciliations between the bank statements and Village accounting records are important steps in maintaining control over cash and provide for verification of cash receipts and disbursements transactions. It is important that a Village official or staff member prepare and verify bank reconciliations, which compare bank balances to the general ledger, on a monthly basis, especially when the employee who prepares bank reconciliations has incompatible duties, such as signing checks. When book and bank balances do not agree, the Clerk-Treasurer must identify the source and nature of the differences and make appropriate corrections.

We requested the two most recent bank reconciliations, August and September 2010, and found that the Clerk-Treasurer had not yet completed these reconciliations. We also selected and reviewed a non-biased judgmental sample of two other bank reconciliations that were completed for December 2009 and March 2010 and found no exceptions.

Additionally, we found that the Clerk-Treasurer was not making the appropriate corrections to the accounting records as she found them during the bank account reconciliation process. Rather than making adjusting entries to the appropriate revenue or expense accounts, the Clerk-Treasurer recorded the majority of her corrections to an unidentified revenue account. Ultimately, the unidentified revenue account closed with a negative balance of approximately \$77,000; however, revenue accounts should never have a negative balance.<sup>9</sup> When the Clerk-Treasurer does not record adjusting entries to the appropriate accounts, she is creating inaccurate financial records that do not provide an accurate picture of the Village's finances. Although the Mayor began reviewing bank reconciliations in November 2009, she did not review the adjusting entries in the unidentified revenue account. Therefore, her review of the bank reconciliations was incomplete and ineffective.

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<sup>9</sup> The Village's certified public accountant recorded an adjusting entry at the end of the year to correct this negative account balance.

The Clerk-Treasurer's failure to provide the Board with monthly financial reports, an annual accounting of the delinquent water and sewer rents, and complete, up-to-date bank reconciliations diminishes the Board's ability to effectively monitor the Village's financial operations and make informed business decisions. As a result, there is an increased risk that errors and irregularities could occur without being detected.

## **Recommendations**

1. Village officials should use excess fund balance identified in this report in a manner that benefits Village taxpayers. Such uses could include, but are not limited to the following:
  - Financing one-time expenses
  - Increasing necessary reserves
  - Paying off debt
  - Reducing property taxes.
2. The Board should ensure that budget estimates are reasonable.
3. The Board should ensure that the Clerk-Treasurer prepares and submits necessary financial reports to the Board, so that it is able to monitor the Village's budget and financial condition.
4. The Clerk-Treasurer should provide the Board with a delinquent water and sewer rents report at the end of the fiscal year. The Board should ensure that the Clerk-Treasurer adds the delinquent water and sewer rents to the real property taxes of the delinquent water and sewer account holders.
5. The Clerk-Treasurer should accurately prepare the Village's bank account reconciliations in a timely manner and record all adjusting entries in the appropriate accounts. The Mayor should review the Clerk-Treasurer's adjusting entries during her review of the bank reconciliations.

## Non-Payroll Cash Disbursements

An effective internal control system over cash disbursements and claims auditing includes establishing policies and procedures to ensure that cash disbursements are appropriate Village expenditures and that cash is safeguarded to prevent loss or theft. The Board is required to audit all claims against the Village prior to the Clerk-Treasurer issuing checks to pay the claims. An appropriate segregation of financial duties ensures that no single person controls all phases of a transaction without proper oversight. If it is not practical to adequately segregate financial duties because of limited staff resources, the Board must establish compensating controls such as reviewing bank reconciliations. Because debit card charges are immediately deducted from the attached bank account, thus circumventing the claims audit process, debit cards are inappropriate for transacting the Village's business and purchasing goods and services for Village purposes.

Policies and Procedures — An effective system of internal controls consists of policies and procedures that enable local government officials to provide reasonable assurance that they are properly safeguarding and accounting for public resources. An important component of good internal controls is the development of written policies and procedures for cash receipts and disbursements and claims auditing. Key aspects of good policies and procedures include timely supervision of those charged with handling public moneys. Good internal controls provide assurance that cash receipts and disbursements are recorded and reported in a timely and accurate manner and that all disbursements are properly supported. Written policies and procedures over the claims audit process provide direction to the Board or a Board-appointed claims auditor as to what constitutes a proper audit of claims and explain how to communicate audit findings to the Board and taxpayers.

The Board does not have non-payroll cash disbursement or claims processing policies in place. Further, the Board has not established written procedures to address these functions. As a result, internal controls over non-payroll cash disbursements in the Clerk-Treasurer's office were inadequate, and claims against the Village were not always audited.

The lack of written policies and procedures over cash disbursements and the claims auditing process creates an increased risk that cash transactions are not adequately controlled. As a result, the Village is vulnerable to the possibility of inappropriate transactions occurring and not being detected in a timely manner.

Segregation of Duties — Concentrating key duties with one individual with little or no oversight weakens internal controls and significantly increases the risk that errors and/or irregularities might occur and go undetected. A major weakness in internal control exists when the same individual maintains the accounting records, has cash custody, and performs bank reconciliations. The lack of appropriate oversight increases the risk that errors and/or irregularities may not be prevented or detected.

Village officials have not adequately segregated non-payroll cash disbursement duties. The Clerk-Treasurer can perform cash recordkeeping and disbursement transactions with little effective oversight. The Clerk-Treasurer also is a designated check signer, routinely posts journal entries, and reconciles the bank accounts without any supervisory or Board oversight.

We selected a non-biased judgmental sample of two months of transactions (December 2009 and March 2010) and reviewed all of the non-payroll check disbursements made during those months, totaling approximately \$1.4 million. We verified that payees and amounts agreed with the abstracts,<sup>10</sup> accounts payable registers<sup>11</sup> and supporting documentation, and we examined the associated canceled check copies and the endorsements. All of these payments agreed with the supporting documentation and appear to be legitimate Village expenditures. We also examined all 22 bank transfers totaling \$63,000 made during the selected months that were listed on the bank statements, and verified that these transfers were made to valid payees such as the Internal Revenue Service and the New York State and Local Retirement System. Although we did not find any indications of improper payments, the failure to segregate duties and the lack of management oversight increases the risk that unauthorized transactions can be initiated and not be detected.

Claims Audit — The Board is required to audit all claims against the Village prior to the Clerk-Treasurer making payments for the claims. All claims must be submitted to the Board and specific claims audited by the Board must be documented in the minutes of the Board's proceedings. It is important that the Board's minutes identify which claims the Board audited and approved. After claims have been audited and approved, the Mayor must sign an abstract of audited claims directing the Clerk-Treasurer to pay the claimants the allowed amounts.

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<sup>10</sup> An abstract is a list of claims provided to the Board, or to a Board-appointed claims auditor, so that the claims can be reviewed and approved for payment.

<sup>11</sup> The accounts payable register is the report that is provided to the Board members prior to the audit and approval of the claims.

Each month, one Trustee is assigned to audit the claims before the Board meeting. The entire Board then approves the claims during the monthly Board meeting based on the recommendations of the Trustee who completed the audit. The Mayor signs the abstracts after the Board meetings. We reviewed a non-biased judgmental sample of three abstracts from December 2009 and March 2010<sup>12</sup> and compared the cash balance totals on the abstracts to the cash balance totals listed on the accounts payable registers.<sup>13</sup> We found that it is virtually impossible to identify which claims were actually audited and approved by the Board. The Village's Board minutes do not identify the dollar amount or the voucher numbers of the claims approved for payment.

Also, the abstract totals did not agree with the cash balance totals listed on the accounts payable registers. The cash balance total on the abstract dated December 15, 2009, was approximately \$32,000 more than the cash balance total on the accounts payable register for the same period. The abstract dated March 11, 2010, was approximately \$11,600 more than the accounts payable register for that period, and the abstract dated March 25, 2010, was \$3,735 more than the accounts payable register for the same period. The Clerk-Treasurer told us that the accounts payable clerk adds claims to the abstracts that come in after the Board meeting and before the date the checks are cut to pay the claims. The Mayor was unaware that the accounts payable clerk was adding claims to the abstracts that were not audited. She also was unaware that she was signing abstracts that had cash balance totals that did not match the abstracts used by the Board to audit the claims. Because these additional claims are added to the abstracts after the Board meetings and paid before the following Board meetings, they are not audited by the Board before or after they are paid. In addition, the Mayor did not sign the abstract dated March 25, 2010, before the checks were mailed.

The Board's failure to ensure that all claims are audited and approved prior to payment increases the risk that the Village could erroneously pay for items that are not authorized or valid Village expenditures, make duplicate payments, or pay for goods and services that have not actually been received.

Debit Cards — The use of debit cards represents significant risks because, unlike credit card usage, for which a statement is received

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<sup>12</sup> Due to the holidays, there was only one abstract in December 2009, dated December 15, 2009. There were two abstracts in March 2010, dated March 11 and 25, 2010.

<sup>13</sup> Each month, the Clerk-Treasurer provides an accounts payable register to all the Board members prior to the Board meeting. While the Trustees have the accounts payable register, they do not compare it to the claims presented at the Board meeting.

and the purchase can be examined, the card holder may have no opportunity to determine the legitimacy of the expense before it is paid. Also, unlike credit cards, debit cards offer less protection against identity theft and may not limit the monetary amount the card holder will be responsible for paying. Because the charges are immediately deducted from the bank account, an unauthorized individual who obtains a card holder's account information may empty the card holder's bank account before the card holder realizes it and is able to react to it. Therefore, debit cards are not legally authorized for transacting a village's business in New York State.

Village officials used three Village debit cards to purchase items including lodging, meals, conference registration fees, used books for the Village library through an on-line bookseller, and various items at local vendors. These transactions were direct charges to the Village's checking account and circumvented the claims audit process. During our audit period, the three debit cards were assigned to the Clerk-Treasurer, clerk/typist, and the Director of Utilities and Public Works. These in turn were shared with other Village employees.

We reviewed all 100 debit card transactions made during our audit period, totaling approximately \$20,000. We also reviewed the supporting documentation for each selected payment to verify that it was a proper expenditure. Our review identified the following exceptions:

- Ten transactions totaling \$2,703 did not appear on an abstract, which indicated that they had not been audited by the Board. Nine of these purchases totaling \$2,566 lacked supporting documentation. At our request, Village officials were able to obtain documentation from the vendors for six of these purchases totaling \$2,417. However, Village officials were unable to provide us with documentation for the other three purchases.
- Forty-three transactions totaling \$945 did not have properly itemized receipts.
- All of the purchases were paid prior to audit by the Board.

Because the use of debit cards circumvents the purchasing process, their use could lead to over-expenditures of appropriations or the purchase of goods and services that are not necessary or reasonable for Village operations. The risks include inappropriate or even fraudulent use of the cards.

## Recommendations

6. The Board should establish and adopt comprehensive policies and procedures for cash disbursements and claims auditing.
7. The Board should segregate the duties of the Clerk-Treasurer so that this individual does not control all aspects of any financial transaction. If it is not feasible to adequately segregate the Clerk-Treasurer's duties, the Board should establish compensating controls to routinely monitor and review the work of the Clerk-Treasurer.
8. The Board should ensure that all claims against the Village are submitted to the Board for audit before they are paid.
9. The Board should document its audit of specific claims in the minutes of its proceedings. Also, the Board should ensure that the minutes identify which claims have been audited and approved. After claims have been audited and approved, the Board must ensure that the Mayor signs an abstract of audited claims directing the Clerk-Treasurer to pay the claimants the allowed amounts.
10. Village officials should discontinue the use of debit cards.

## Bidding Practices

The objectives of a public procurement process are to obtain services, materials, supplies and equipment of a desired quality and appropriate quantity at the lowest cost, in accordance with applicable Board and legal requirements. The effective use of competition in the procurement process helps Village officials achieve these goals and provides assurances that public purchase decisions are not influenced by favoritism, extravagance, fraud, or corruption.

Competitive Bidding — General Municipal Law (GML) requires Village officials to follow competitive bidding requirements when purchasing goods and commodities that exceed \$20,000 and public work contracts that exceed \$35,000,<sup>14</sup> annually. Advertising for bids encourages competition among vendors and provides taxpayers with reasonable assurance that those goods and services are procured in a prudent and economical manner.

Village officials did not always adhere to GML when making purchases. We examined approximately \$910,000 in payments that were made to seven vendors for 10 purchases to determine whether Village officials advertised for bids or purchased from State or County contracts as required. Village officials did not use competitive bidding for three of the 10 purchases totaling \$71,048 for two pickup trucks, a tractor, and a lawnmower. Village officials told us that they did not competitively bid these purchases because they preferred to buy from local vendors when possible. Additionally, for another purchase included in the 10 that we reviewed for a fire rescue truck totaling \$532,393, Village officials were unable to locate the bid documentation. Therefore, Village officials and taxpayers have no assurance that an appropriate competitive bidding process was used.

Restrictive Bid Specifications — According to GML, when a municipality advertises for bids it may specify a particular article or object which it regards as an industry-wide standard. But, it must either specify that any other manufacturer of a similar article or object may meet the specifications – if such a product is reasonably equivalent to that mentioned as the standard – or it must be prepared to justify, by appropriate documentation, that no other product provides substantially equivalent or similar benefits. In addition, particular makes or models may be specified to the exclusion of others only if the municipality has passed a resolution standardizing that particular product.

<sup>14</sup> Effective November 12, 2009, the public works contract threshold was increased to \$35,000 from \$20,000. Effective June 22, 2010, the purchase contract threshold was increased to \$20,000 from \$10,000.

The Village purchased a new garbage truck for \$129,450 using bid specifications that referred to specific brand names of parts. The Village also required that the representative bidder have a minimum of 40 years of experience in manufacturing this type of truck. The bid specifications made no provision for the purchase of equivalent parts or experience. Also, the Village had not passed a standardization resolution.

The Village inappropriately restricted vendor competition when purchasing this truck by failing to adopt a standardizing resolution and by using bid advertisements that solely stipulated the product of a particular manufacturer. The Village could have saved \$1,178 had it purchased the truck from the lowest bidder.

## **Recommendations**

11. The Board should closely monitor the purchasing process to ensure that purchases are made in accordance with GML.
12. Village officials should maintain their purchasing documentation for six years after the final payment is made, as required by law.
13. The Board should take an active role in reviewing equipment specifications prior to advertising for bids, especially when using specifications based on a specific product, to avoid using unduly restrictive language in the specifications and stifling competition.

## **APPENDIX A**

### **RESPONSE FROM LOCAL OFFICIALS**

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

VILLAGE OF HAMILTON  
PO Box 119  
3 Broad Street  
Hamilton, NY 13346  
Telephone: 315-824-1111  
Fax: 315-824-0922

Mayor:

Margaret Miller

Trustees:

Anne R. Clauss

Samuel L. Cooper

Deborah S. Kliman, Ph.D.

Russell Lura

Village Clerk:

Alana Scheckler

Village Treasurer:

Mary Ann Henderson

Village Administrator:

Sean Graham

January 11, 2012

Office of the State Comptroller  
Division of Local Government & School Accountability  
PSU CAP Submission  
110 State Street, 12th Floor  
Albany, NY 12236

Dear Sir/Madam:

Please accept this document as our response to the preliminary draft findings received on December 13, 2012 from the New York State Division of Local Government and School Accountability of the recent examination of the Village of Hamilton. The Village of Hamilton Board of Trustees is in agreement with the findings of the audit team. This response will also serve as our Corrective Action Plan.

Recommendation 1: Village officials should use excess fund balance identified in this report in a manner that benefits Village taxpayers.

Response 1: Village officials have discussed the use of fund balance for one time expenses, increasing capital reserves, and have considered the use to offset property taxes for future budgets.

Recommendation 2: The Board should ensure that budget estimates are reasonable.

Response 2: The Board is now projecting expenses by tracking revenue and expenses more closely.

- Recommendation 3: The Board should ensure that the Clerk-Treasurer prepares and submits necessary financial reports to the Board, so that it is able to monitor the Village's budget and financial condition.
- Response 3: The Treasurer will provide monthly financial reports to the Board at their monthly meeting.
- Recommendation 4: The Clerk-Treasurer should provide the Board with a delinquent water and sewer rents report at the end of the fiscal year. The Board should ensure that the Clerk-Treasurer adds the delinquent water and sewer rents to the real property taxes of the delinquent water and sewer account holders.
- Response 4: The report will be given to the Board and the delinquent water and sewer rents will be relieved by a resolution from the Board.
- Recommendation 5: The Clerk-Treasurer should accurately prepare the Village's bank account reconciliation's in a timely manner and record all adjusting entries in the appropriate accounts. The Mayor should review the Clerk-Treasurer's adjusting entries during her review of the bank reconciliation's.
- Response 5: The bank accounts are reconciled up-to-date. The Administrator now opens and reviews the bank statements, including returned checks. The Mayor will review journal entries.
- Recommendation 6: The Board should establish and adopt comprehensive policies and procedures for cash disbursements and claims auditing.
- Response 6: The Board and Administration will develop policies and procedures and will adopt by resolution as soon as possible.
- Recommendation 7: The Board should segregate the duties of the Clerk-Treasurer so that this individual does not control all aspects of any financial transaction. If it is not feasible to adequately segregate the Clerk-Treasurer's duties, the Board should establish compensating controls to routinely monitor and review the work of the Clerk-Treasurer.
- Response 7: Reorganization of staff was done by resolutions. Duties have been segregated; one individual does not have control over financial transactions.
- Recommendation 8: The Board should ensure that all claims against the Village are submitted to the Board for audit before they are paid.
- Response 8: No claims will be paid unless audited; passed by resolution.

Recommendation 9: The Board should document its audit of specific claims in the minutes of its proceedings. Also, the Board should ensure that the minutes identify which claims have been audited and approved. After claims have been audited and approved, the Board must ensure that the Mayor signs an abstract of audited claims directing the Clerk-Treasurer to pay the claimants the allowed amounts.

Response 9: The minutes will reflect a numeric/alpha combination with the dollar amounts listed, that will correlate with the same numeric/alpha combination identified on each month's abstracts. The Mayor will sign the abstracts of audited claims each month.

Recommendation 10: Village officials should discontinue the use of debit card

Response 10: The debit cards have been destroyed.

Recommendation 11: The Board should closely monitor the purchasing process to ensure that purchases are made in accordance with GML.

Response 11: The Board will monitor the purchasing process more closely. The Board has also reviewed the current adopted procurement policy.

Recommendation 12: Village officials should maintain their purchasing documentation for six years after the final payment is made, as required by law.

Response 12: The Board adopted Records Retention and Disposition Schedule MU-1 and will follow those regulations.

Recommendation 13: The Board should take an active role on reviewing equipment specifications prior to advertising for bids, especially when using specifications based on a specific product, to avoid using unduly restrictive language in the specifications and stifling competition.

Response 13: The Board will review equipment specifications and avoid using restrictive language.

We thank the OSC staff for their professionalism of this audit.

Sincerely,



Margaret Miller  
Mayor, Village of Hamilton

## APPENDIX B

### AUDIT METHODOLOGY AND STANDARDS

The objectives of this audit were to review the Village's financial management and internal controls over non-payroll cash disbursements and bidding practices. To achieve our audit objective and obtain valid audit evidence, we performed the following audit procedures.

#### Financial Management

- We interviewed Village officials to obtain an understanding of the organization and the accounting system.
- We analyzed financial data for the general and water funds from the Village's annual financial reports for the 2005-06 through 2009-10 fiscal years to determine trends in the Village's financial activity.
- We obtained and reviewed the minutes of the proceedings of the Board, pertinent Board resolutions, relevant policies and procedures, and financial and budgetary information related to our audit objective. We reviewed financial information provided to the Board and interviewed the appropriate Village officials and Trustees.
- We analyzed the Village's tax levy for the last five years and compared it to the Village's unappropriated unreserved fund balance.
- We reviewed and analyzed available accounting records and reports and interviewed appropriate Village officials and Trustees.
- We interviewed Village officials and Trustees to obtain information about the Village's process for collecting delinquent water and sewer rents at the end of the fiscal year. We reviewed the Village's accounts receivable report for May 31, 2010.
- We tested bank reconciliations for the months of December 2009 and March 2010.

#### Non-Payroll Cash Disbursements

- We evaluated internal controls over non-payroll cash disbursements by interviewing Village employees and Trustees. We also reviewed applicable policies, procedures, and Board resolutions.
- We traced all bank statement disbursements for December 2009 and March 2010 totaling \$1.4 million to canceled check images, abstracts, accounts payable registers, and certified payrolls.
- We traced all check disbursements for December 2009 and March 2010 to supporting documentation.

- We scanned all bank statements during the audit period for debit card purchases and traced these purchases to supporting documentation.
- We reviewed journal entries during the audit period for unusual credits to cash.

### Bidding Practices

- We interviewed appropriate Village officials and employees to gain an understanding of the Village's purchasing process.
- We assessed compliance with GML competitive bidding requirements by selecting a non-biased judgmental sample of 10 purchases totaling approximately \$910,000. We examined the contracts and other supporting documentation for these purchases to determine if the Village complied with competitive bidding laws.
- We used an accounts payable disbursement report for the period June 1, 2009, to September 30, 2010, that was downloaded from the Village's financial system and scanned it for vendor payment totals over competitive bid limits. After scanning the data, we had the accounts payable clerk print a detailed vendor history of some of the vendors with payment totals over the limits so that we could see if any individual or aggregate purchases from the vendor were over competitive bidding thresholds.
- When selecting our non-biased judgmental sample of 10 purchases, we focused our examination on payments to vendors that would likely require Village officials to take action to solicit competition or purchase from a State contract to comply with competitive bidding requirements.

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 objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

## APPENDIX C

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