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VILLAGE OF PIKETON PERFORMANCE AUDIT

DECEMBER 27, 2001

Financial Forecast

Introduction

As a benefit to government entities in fiscal watch or emergency status, the Auditor of State's Office (AOS) has the ability to initiate performance audits. These performance audits are completed at no cost to the government entity and are designed to assist the government in making decisions with the objective of eliminating the conditions which brought about the declaration of fiscal watch or emergency. Another objective of the performance audit is to perform an independent assessment of the government's financial situation, including the development of a framework for the financial recovery plan. The recommendations contained within the performance audit provide one resource to a government entity in developing a financial recovery plan.

Scope and Methodology

This document, prepared as of October 2001, represents the performance audit of the Village of Piketon (Village) and consists of a specific financial forecast through 2005. In developing the financial forecast, a thorough analysis of each of the major revenue and expenditure line-items was conducted in an effort to develop detailed assumptions. The forecast focuses on an Enterprise Fund, specifically the Water Fund, and projects the Village's financial situation through 2005, assuming no major operational changes. To allow for a perspective of the Village's past financial situation, the financial forecast presents additional historical information from 1998 through 2000. Three other funds contributed to the Village's fiscal stress. These funds included the Street Fund, Litter Fund and Police Fund. In analyzing the future of these funds, there will be adequate funds available in the future to cover previous deficit balances.

Through the process of developing the financial forecast, a number of the Village's operational practices were also assessed for overall efficiency and effectiveness. Accordingly, the performance audit identifies detailed recommendations designed to assist the Village in enhancing its operational efficiency as well as in developing a financial recovery plan.

Background

As provided by Section 118.021 of the Ohio Revised Code (ORC), the Mayor of Piketon requested that a fiscal watch analysis be performed by the Auditor of State (AOS). On December 28, 2000, citing Section 118.03 of the ORC, the AOS placed the Village in fiscal watch as of the end of 1999. The Village of Piketon has remained in this condition since the AOS's original designation.

ORC § 118.022 specifies four fiscal watch conditions. The existence of any of these conditions constitutes grounds for the declaration of a fiscal watch. These conditions include assessments surrounding the following:

- General Fund accounts payable,
- General Fund and special revenue funds accounts payable,
- Deficit fund balances, and
- Treasury balance.

The Village was found to have deficit fund balances in excess of the provisions outlined in ORC § 118.022(A)(3) in the Water Fund, Police Fund, Street Fund and Litter Fund. Specifically, the treasury balance, less the positive fund balances, exceeded one-twelfth of the treasury receipts. Subsequently, the Police Fund, Street Fund and Litter Fund have all been rectified. The following are some of the major administrative problems contributing to the fiscal watch status:

- **Water Operations** - The Village provides water and sewer services to its residents. Piketon did not charge enough to cover the cost of providing water. The Village billed for approximately 130 million gallons of water in 2000 at an average cost of production of \$0.99 per thousand gallons. While expenditures totaled \$128,685, total revenues from water billings was \$100,384 or \$0.77 per thousand gallons. In September of 2000, the Village raised water rates from a usage rate of \$2.80 per month for the first 4,000 gallons, \$1.50 per thousand gallons for the next 8,000 gallons and \$1.40 per thousand over 12,000 gallons to a usage rate of \$6.00 for the first 4,000 gallons and \$2.00 for each additional 1,000 gallons used. In September of 2001 the Village passed a resolution to again increase water rates to \$6.00 for the first 2,500 gallons and \$2.00 for each additional 1,000 gallons.

Also, the water department funded five FTEs including, three water department employees, the village administrator and a billing clerk. The three water department employees often performed non-water related duties. In June of 2000, two of the water department employees retired. Due to the non-water related duties performed by the former employees, the Village intends to only fill one position.

- **Budgetary Process** - The Tax Budget, Certificates of Available Resources and the Annual Appropriation Ordinance routinely had not been prepared on a timely basis. The policies in place regarding the budget process were seemingly ineffective because time frames for the completion of tasks were not realized. The County withheld funds allocated to the Village due to the untimely preparation and filing of these documents. However, all funds in arrears have been collected from the County to date.

According to a representative from the Pike County Auditor's office, it appears that the Village has taken some steps to rectify past filing deficiencies; the Tax Budget for 2001 was filed within the appropriate time frames.

- **Record-keeping** - The lack of financial records for the Village has been well documented. The Village uses the services of an Independent Public Accountant (IPA) to prepare cash basis reports for the Village based on information summarized and developed by the Village. However, Local Government Services (LGS) has had to reconstruct financial statements for 1998 and 1999 and is currently working on 2000 through July. Several account reclassifications were made to the annual reports for 1998 and 1999. In addition, the Village did not have a receipts or an appropriations ledger, nor was there a duplicate receipt book. The receipts appear to be posted to the proper fund, but several were not classified properly. Reclassifications for 2000 may also be required.

Nature and Purpose of Presentation

This financial projection represents the expected revenues, expenditures and fund balances of the Water Fund and of the Village of Piketon. The financial projection includes the calendar years 2001 through 2005, with historical information presented for 1998 through 2000.

Description of Village

The Village of Piketon (the Village) is located in the northeast portion of Pike County and consists of a 5.524 square kilometer area. The 1990 U.S. Census shows a population of 1,717, while the current U.S. Census estimate is 1,907, indicating an overall trend toward an increasing population.

The Village, incorporated in 1931, is directed by a publicly-elected six-member Council, a Mayor, a Clerk-Treasurer and an appointed Village Administrator. The Village of Piketon provides services to its residents that include water and sewer utilities. The water and sewer utilities department employs three full-time employees. The head of the department is salaried and oversees the purification and treatment processes, as well as sewer treatment. Any major repair and maintenance requirements are outsourced to private contractors.

Fund Accounting

The Village uses fund accounting to segregate cash in its enterprise funds which is restricted as to its use, and the following are the fund classifications:

- **Enterprise Funds** - These funds account for operations similar to private business enterprises where management intends that the significant costs of providing services will be recovered through user charges. The Enterprise Funds consist of the following specific funds:

- ▶ Water Fund - This fund receives charges for services from residents to cover the cost of providing this utility.
- ▶ Sewer Fund - This fund receives charges for services from residents to cover the cost of providing this utility.

Financial Forecast

The financial forecasts and assumptions presented in this section represent the Auditor of State’s projection of the Village of Piketon’s present and future financial condition in the absence of significant increases in revenues or reductions in expenditures. The projection, which is for the Water Fund, is accompanied by three years of comparable historical results, general assumptions and explanations.

Water Fund Forecast

The following information in **Table 1-1** represents actual and forecasted financial information in the Water Fund for the Village of Piketon.

Table 1-1: Water Fund

	Actual 1998 (audited)	Actual 1999 (audited)	Actual 2000 (unaudited)	Forecast 2001	Forecast 2002	Forecast 2003	Forecast 2004	Forecast 2005
Charges for Services	\$94,384	\$85,031	\$100,384	\$149,160	\$162,720	\$162,720	\$162,720	\$162,720
Total Operating Revenues	\$94,384	\$85,031	\$100,384	\$149,160	\$162,720	\$162,720	\$162,720	\$162,720
Personal Services	\$101,201	\$67,843	\$65,655	\$49,155	\$50,630	\$52,149	\$53,713	\$55,324
Contractual Services	33,683	40,190	25,736	26,508	27,303	28,122	28,966	29,835
Supplies and Materials	17,835	34,149	36,296	37,385	38,506	39,662	40,851	42,077
Capital Outlay	0	0	998	1,000	1,000	1,000	1,000	1,000
Total Operating Expenses	\$152,719	\$142,182	\$128,685	\$114,048	\$117,439	\$120,933	\$124,531	\$128,236
Excess of Operating Receipts Over/(Under) Operating Expenses	(\$58,335)	(\$57,151)	(\$28,301)	\$35,112	\$45,281	\$41,787	\$38,189	\$34,484
Other Sources	\$3,895	\$11	(\$1,707)	\$0	\$0	\$0	\$0	\$0
Excess of Receipts Over/(Under) Disbursements	(\$54,440)	(\$57,140)	(\$30,008)	\$35,112	\$45,281	\$41,787	\$38,189	\$34,484
Beginning Cash Fund Balance	\$41,657	(\$12,783)	(\$69,923)	(\$99,931)	(\$64,819)	(\$19,538)	\$22,249	\$60,438
End Cash Fund Balance	(\$12,783)	(\$69,923)	(\$99,931)	(\$64,819)	(\$19,538)	\$22,249	\$60,438	\$94,922

Source: 1998 - 1999 Financial Audits, 2000 cash journal and interviews with Village and County officials

The water ordinance passed in September of 2000, effective November of 2000, raised rates from \$2.80 for the first 4,000 gallons to \$6.00 and each additional 1,000 gallons from \$1.50 to \$2.00. The Village sends out 565 water bills monthly.

According to the Village Administrator, the Village Council has voted to raise water rates again in September of 2001 to cover costs in mid-summer. The rate increase will raise rates to \$6.00 for the initial 2,500 gallons and \$2.00 for each additional 1,000 gallons. For the purpose of this forecast, it is assumed the rate increase will take place in January of 2002. **Table 1-2** provides an estimate of revenues based on the projected usage for 2001 of 11,400 gallons of water usage per account billed. Accounts billed include both commercial and residential accounts.

Table 1-2: Water Fund Revenue Forecast

	2001	2002	2003	2004	2005
Base level of water usage ¹	\$6	\$6	\$6	\$6	\$6
Remainder of water usage	\$16	\$18	\$18	\$18	\$18
Average monthly billing per account	\$22	\$24	\$24	\$24	\$24
Average yearly billing per account	\$264	\$288	\$288	\$288	\$288
Estimated annual revenue	\$149,160	\$162,720	\$162,720	\$162,720	\$162,720

Source: Interviews

¹ For 2001, the base level of water usage is 4,000 gallons per month. In years 2002 through 2005, the base level is 2,500 gallons.

As indicated in the example of **Table 1-2**, the Village’s water rates will increase revenue significantly.

In 1998, the Village’s personal services expense was higher due to required updating work on the water treatment facility. The Village will experience an additional decrease in personal services for 2001 because two of the three full-time water department employees retired in 2000. The Village plans to fill only one of the vacant positions with a part-time employee of the water and sewer department. For the purpose of this forecast, it is assumed the Village will set the employee’s new salary at \$15,000 plus 25 percent for benefits, which, when compared with the current part-time employee’s salary, will be an overall increase of \$8,000 towards personal services. However, the Village will save approximately \$28,000 in salary and benefits by not filling the one vacancy in the water department.

The other full-time water department employee, who recently became certified in water operations, will receive a \$3,000 increase in pay. This employee will perform all daily activities associated with

the water department, including reading meters and overseeing the water facility. For the purpose of this audit, a three percent increase is included for personal services during the forecast years.

Supplies and materials was significantly lower in 1998. According to the village administrator, there were fewer water breaks and less repairs needed in 1998. For the purposes of this report, supplies and materials are forecasted to increase at a three percent rate and are based on year 2000 expenditures.

Contracted services includes professional services and utilities. In 1998, the Village had emergency repairs completed on three wells, totaling \$20,000. The repair cost were incurred in 1998 and 1999 and are not assumed to be recurring during the forecast period. For the purposes of this forecast, contracted services are forecasted to increase at a three percent rate and are based on the three year average less the \$20,000 emergency repair cost in 1998 and 1999.

Capital outlay increased in 2000 to provide for necessary meter and pipe upgrades. For the purposes of this report, capital outlay is forecasted to remain comparable to 2000 levels.

Litter Fund

The Litter Fund started as a grant to promote litter control within the Village. It was a short term fund which provided litter control services. The fund showed a deficit of \$331 for several years and was closed by the Village. Therefore, no assessment of the Litter Fund was conducted.

Police Fund

The Police Fund accumulated a deficit of \$101,679. The cause identified in previous financial audits was that the Police Department was not generating enough revenue to meet its operational expenditures. In an ordinance passed on November 20, 2000, the Village transferred funds from the General Fund and Revolving Loan Fund to cover the deficit balance of the Police Fund. The Department enhanced its patrol services and added the Law Enforcement Automated Data System (LEADS), which has allowed the Village to increase its revenues for the Police Fund. Currently, the Police Chief is assessing other funding measures to help support the department. An assessment of the Police Fund was performed and it indicated that the fund should maintain a positive balance through 2005. Therefore, a detailed forecast of the fund was not performed.

Street Fund

The Street Fund deficit was caused by not allocating labor costs to other appropriate funds.. The Street Fund had a \$53,351 deficit fund balance. The ordinance passed on November 20, 2000 also transferred funds to cover this deficit balance. An assessment of this fund was also performed and

indicated that the Street Fund should maintain a positive fund balance through 2005 barring unanticipated expenditure increases in the fund. Therefore, a detailed forecast of the fund was not performed.

Conclusions

Based on the Water Fund forecast presented in **Table 1-1**, it appears that the Village has the capability to stabilize the financial position of the Water Fund. The forecast reflects positive significant fund balances in the water fund by 2003. The major contributing factor for the positive fund balances is the water rate increase. However, for Piketon to achieve the results projected in **Table 1-1**, certain aspects of the Village's operations need to be improved. More specifically, the Village should focus on improving its budgetary practices, begin maintaining accurate financial and water billing records, and begin fostering proper accounting practices. The detailed operational changes that Piketon should implement are outlined in the **General Recommendations** section of this report.

In developing the Water Fund forecasts presented in **Table 1-1**, the projections for the Village's water services were based upon the following general assumptions:

- The Village's implemented rate will be constant, based on the new rates authorized in September 2001.
- The Village will only fill one of the vacant positions within the water department; and
- Revenues will be used to cover previous deficits and current expenses.

Should the water department change the conditions of the assumptions, the results projected in the Water Fund forecast could be significantly impacted.

General Recommendations

1. *The Village should formalize the budgetary process*

In the past, the Village has not filed its Tax Budget and its appropriation resolutions with the County Auditor within the prescribed time frames. As a result, the County Auditor has withheld tax revenues that were due to the Village. Because the Village is currently in Fiscal Watch, it cannot afford to forego any revenues which it is owed. Accordingly, the Village should develop a formal timetable and instructions for preparing the tax budget and the appropriations resolution. By having detailed budget preparation instructions and a formal timetable, the Village can ensure it is meeting the County Auditor's filing deadlines. The Village should consider forming a finance committee to ensure the Village's work meets guidelines set forth by the Ohio Revised Code. Embracing a sound budgeting methodology and preparing budgets under written guidelines will help ensure that the Village meets filing deadlines and further enables smooth transitions associated with employee and elected official turnovers.

2. The Village should utilize the Uniform Accounting Network

Although the Village has used the services of an Independent Public Accountant (IPA), the Village's financial records have not been effectively maintained as evidenced by a number of citations during financial audits. More specifically, the Village has failed to adequately maintain cash journals, receipt ledgers, appropriation ledgers and has not properly used the encumbrance method of accounting. As a result, LGS has had to reconstruct past financial records. The Village cannot operate effectively or efficiently without accurate financial records and sound accounting practices.

To rectify these record keeping and accounting deficiencies, the Village should consider discontinuing use of the IPA firm and take advantage of the Uniform Accounting Network (UAN) services offered by the Auditor of State's office. The UAN not only provides computer training for Clerk/Treasurers, but also provides general fund accounting training that would be helpful in establishing financial reporting procedures for the Village. The Village cannot operate effectively or efficiently without accurate financial records and sound accounting practices.

In August 2001, the Auditor of State began offering an online training course based upon the Government Finance Officers Association's (GFOA) Elected Officials Guide series. The Clerk/Treasurer and all other public officials for the Village should enroll immediately to enhance their knowledge of government finance. There are ten chapters to the course. The topics include, but are not limited to, introduction into government finance, multi-year budgeting, procurement, and internal controls. Completion of the course will result in the participant receiving an Ohio Financial Accountability Certificate. More importantly, however, is the greater benefit derived from the enhancement of knowledge in government finance of those who participate.

Financial Implication: By discontinuing use of the IPA firm, the Village can save approximately \$1,600 annually in professional fees.

3. The Village should periodically monitor the water usage fee

On September 5, 2000, the Village passed an ordinance that increased water rates from \$2.80 for the first 4,000 gallons to \$6.00 for the first 4,000 gallons. A fee for usage greater than 4,000 gallons was implemented at \$2.00 per every 1,000 gallons. The future rate, will charge \$6.00 for the initial 2,500 gallons and \$2.00 per every additional 1,000 gallons. Village officials should periodically monitor the current rates to ensure that they provide adequate revenue to meet the costs of production and equipment replacement. The village should consider establishing a Water and Sewer Committee to review sewer and water rates. This entity could increase public participation and provide an independent, objective view and provide information to the Village council, who are responsible for setting the water and sewer rates for the Village.

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