Comprehensive Municipal Financial Management

Disclosure on Materials – I
Sources of Ideas – to embrace & avoid

**Municipalities**
- Bristol Borough
- Hatboro Borough
- Horsham Twp.
- Upper Dublin Twp.
- Abington Twp.
- Montgomeryville Twp.
- Lower Gwynedd Twp.
- Plymouth Twp.
- Whitemarsh Twp.
- Doylestown Twp.
- MCATD

**Authorities/Utilities**
- BCWSA
- RTWA
- Chalfont New Britain
- Amicor
- Lamberton
- Quakertown
- Conshohocken
- City of Philadelphia
- Warwick
- Florida Water Svcs.
- Kentucky P&L

**Private Organizations**
- Air Products
- CONRAIL
- General Battery
- Lehigh Valley Hospital
- GHMH
- SBMC
- Reading Hospital
- LGH
- Brandywine Hospital
- Wood Company
- SPS Technologies

**OTHER**
- PICPA
- Personal Education
- PSATS

**DCED & Treasurer Reports from:**
- Plumstead Township
- Milford Township
- Morrisville Authority
- Lower Bucks Joint Authority
- New Britain Township
- Newtown Township
- Allen Township
- Lower Milford Township
- Lower Providence Township
- Williams Township
- Northampton County
- Bucks County
- City of Allentown
- Salisbury Township

Disclosure on Materials - II
Why Case Study Richland?
- Most client jobs were narrow niche specific task in scope; none had the comprehensive approach applied in Richland.
- Pulled **EVERY Idea & Experience** I could come up with and applied to my own township with the full & enthusiastic support of my co-Supervisors.
- Public Entities subject to “Open Record Laws”; none the less, I have a professional obligation to **NOT** advertise client projects.
- As an elected official, I have wide discretion over release of data from my own community, Richland Township. Virtually all of what you see today, is presented annually, with copies kept in our public meeting room.
- To sum it up, I have taken great pains to provide an insightful presentation without compromising principals of professional confidentiality.

What are your backgrounds?
What do you want from this workshop?
Today’s Outline

1. Philosophy & Concepts: Accounting & Finance and the Relationship with Operations
2. Reporting (Budget & Treasurers Reports, DCED vs. GAAP, Presentation Formats, Audits (Financial Statement, Liquid Fuels, Performance Audit, Speciality, Compliance, What they are and are not, how they can bring value), & Internal Control (Reasonable Controls with limited resources).)
3. Financial Specifics I (Revenue Streams, Fees & Fee Structures, Cable Franchise Fees, Build your Tax Base: Zoning, Codes, & Developer Management, Cash Management, Grants)
5. Financial Specifics III (Capital Planning & Investment, Asset Management, Credit Rating)
6. Interactive Exercises: Prepare a Budget, Read a Treasurers Report, Read a Performance Audit – these will be done throughout the presentation

Our Objectives Today:
- Present operating issues, then relate them to financial impacts
- Treasurers Report is nothing more than a score card; Operations drive finance more than the other way around. (But for money, there will be no operations.)
- Orient thinking to SUCCINCT FINANCIAL REPORTING on salient issues.
- Reports provide plenty of detail; BUT always have a Lead schedule that presents the “Big Picture”. Without an organized summary, it becomes eyewash and everyone zones out.
- Give YOU ideas on achieving the best practical Treasury Function.
- Most towns will not have a CFO, Payroll Manager, Billing Department etc.
- The takeaway?

Our Objective is NOT:
- To make you an accountant or teach you accounting

All this is aimed at one thing:
Informed Wise DECISIONS by users of financial information.

Comprehensive Municipal Financial Management – Part I

Philosophy and Concepts

Factoids on THE Problem:
- Less than 5% of all Americans balance their own checkbook once per year. - USA Today Statistic Box
- The Pennsylvania Institute of Certified Public Accountants, and most other State Societies, have undertaken projects at improving financial literacy. They wouldn’t devote valuable resources were it not true.
- A Pennsylvania township Treasurer’s Report (Complete):
  Fund Balance Beginning
  Add: Receipts
  Less: Disbursements
  Fund Balance Ending
- A Pennsylvania township produced NO Treasurer’s Report – just the year end audit report required by statute.

Want proof?
- Federal Government - $14.2 Trillion Debt
- California, New Jersey, New York, Illinois, Massachusetts, Rhode Island ------and Pennsylvania – Multi Billion deficits AND bankrupt pension funds – top 15 states with unfunded liabilities over a trillion dollars.
- Millions of homeowners upside down
- Ask Ma & Pa
Macro Economic Effect

- If each Pennsylvania municipality created capital reserves of only $1 million, that would amount to a $2.5 BILLION capital formation, and have a leveraged economic effect in local municipalities and in the statewide economy.
- Accounting & Financial Reporting are the tools to make that happen.

How Do You Build Reserves?

- Certainly Macro Economic Factors Helped
  - Example: Recalibrating Personal Energy Usage
- Best Management Practices:
  - A “Strategic Vision” for the community
    - Sustainable Communities Concept – COP, Ben Franklin Parkway, Fairmount Park
  - Relevant Accounting Format
  - Value Emphasized Spending
  - Operations Improvement
  - Non Tax Revenue Enhancements
  - Individual Best Management Practices

Start with a Case Study:

Applied Concepts to Build Fund Balance

- Use of Investment Income vs. Real Estate Tax
- Establish 14 Employee Police Service, in operation for 10 years without new taxes, 19 years in total between tax increases
- Compensation Policy: Below the top, but above market midpoint
- Comfortably managed OPS with ~ 32 employees; presently 3 less with no layoffs
- Have elements of bonus and incentive pay
- Funded $12-15 million in Capital Projects; borrowed ~ $4 million
- Net Reserves: December 1998 = $400k; December 2010 = $2.8mm
- Reduced Tax Payer Funded Professional Fees
- Wide use of volunteers, ancillary events funding

The Center Piece or “Tool” that made it happen: Multi Year Budgeting coupled with a GAAP formatted Treasurer’s Report

Revenue, Expense & Fund Balance Structure

Richland Township 1998-2004

(In 000)

The Center Piece or “Tool” that made it happen: Multi Year Budgeting coupled with a GAAP formatted Treasurer’s Report
Revenue, Expense & Fund Balance Structure
Richland Township 2005-2010
(In 000)

- Revenue
- Expenses
- Surplus/Deficit
- Fund Balance
- Investment Income

Revenue, Expense & Fund Balance Structure
A Montgomery County Borough 2004 & 2005

With about 30% less in population, core cost structure was almost 3 times core cost structure of case study. Larger PD was “A” major reason.

The actual results of the past 12 years were nearly all (though not all - there were some surprises) planned. This has occurred in Authorities, Hospitals, a Private Utility, and an outfitter.

Most business units can achieve the results they desire, IF they plan. Two Municipalities about 30 miles apart, totally different cost structures. The high cost town enjoyed greater per capita income.

Key Terms: Accounting & Finance
Important to apply & use standard language/terminology

- Capital Expenditure & Revenue (Slides 21 & 22)
- Operating Expenditure & Revenue (Slides 23 & 24)
- Capital Intensive — Slide 25
- Labor Intensive — Slide 25
- Value Analysis (Slides 26, 27, & 28)
- Cash vs. Accrual (Slide 29)
- Asset — what are township assets?
- Liability — what are township liabilities?
- Equity (Fund Balance or Reserves)
- Treasurer’s Report vs. Budget

Important that everyone in an organization use the same language.

What are Capital Revenues?

- One Time or Non Recurring:
  - Grants
  - Dedications
  - Developer Contributions
  - Sale of a Business Unit

What are Capital Expenditures?

- One Time or Non Recurring
  - Major Equipment
  - Building Projects
  - Police Cars
What are Operating Revenues?
- Revenues that are constant, that you can count on recurring every year. They may go up or down, but they will likely be recurring.
- Examples: EIT, EST, Real Estate Tax, Transfer Tax, Permit Fees. These may increase or decrease, sometimes widely, but they are fairly reliable.

What are Operating Expenses?
- Expenses that are constant, that you can count on recurring every year. They may go up or down, but they will likely be recurring.
- Examples: Payroll, Road Materials, Utilities, Vehicle Operating Expenses, Printing & Advertising etc. These may increase or decrease, sometimes widely, but they are fairly constant – and if you are doing your job well, on the expense side, there should not be that much fluctuation.

Understanding Capital vs. Operating
- Labor costs are $3 million (an immediate cash outlays in the next year) and Depreciation (or annual debt service) is $7 million, is this a capital or operating intensive business?
- Debt service (or depreciation) is $4 million, Labor is $30 million, is this a capital intensive business?
- Are municipalities typically labor or capital intensive? Note GASB 34.

Operations Improvement –Based on Value:
  Philosophy & Concept
- If and when to charge vs. not
- If and when to inspect vs. not
- If and when to service vs. not
- When to plow, build, measure, etc. vs. not
- Operating Improvement that yields returns
  - Returns to Fund Balance
  - Returns in Improved Public Service

Value Oriented Spending:
  Philosophy & Concept – Ask Jack Benny
- Good vs. Bad Spending
- Don’t major on the minors
- Conscious and Analytical Look at Tradeoffs
- Spending that yields returns
  - Returns to Fund Balance
  - Returns in Improved Public Service

Your Philosophy & Concepts
Within the enumerated powers of the Second Class Code, trade waivers for community benefit. In 1999, applied strict adherence to a buffering/berm requirement. We buffered one industrial site from another. Had we been more flexible, the owner likely would have made a $25,000 to $35,000 park contribution, and saved himself a similar amount. The buffer is there and useless. Blind adherence to “by the book philosophy” made this a “lose lose” code compliance. The township, developer, and community all lost.

Accounting & Finance (and related operations) are not always exact “right vs. wrong”, but more often are bad, not so bad, ok, decent, better, best or perfect judgment calls. YOUR Governing & management philosophy, & knowledge of concepts will drive decisions.
Cash vs. Accrual Basis

- **Cash Basis**: Transactions are only recorded once cash is received or disbursed.
- **Accrual Basis**: Transactions are recorded once a liability is incurred, or revenue is earned.
- **Modified Accrual Basis**: Expenses are recorded when incurred; Revenue is recorded when received.

Enterprise Funds (Utilities for example) are always Accrual; Governments will either be cash or modified accrual. Most of the governments I have worked on used Modified Accrual or Modified Cash on a limited basis (applied to Payroll, benefits, and limited Payables).

Operating Improvement Example: Zoning Hearing Board

- Annual ZHB Solicitor Costs - $50K
- Annual ZHB Costs - $7K
- Total Cost might be $57
- Residential Ancillary Hearing Charge - $300 - Cost is $400; Municipality loses $100 per hearing
- Commercial/Industrial/Subdivision Charge - $1,500 – Cost is $400
- One Commercial offsets 11 Residential
- Total Charges exceed Total Cost in most years
- ZHB Solicitor Costs is also attendant with Revenue.
- Challenge for Municipality is to analyze these with Breakeven Analysis

Breakeven Analysis

<table>
<thead>
<tr>
<th>Fixed Cost</th>
<th>Unit Revenue – Unit Cost = No. Units</th>
</tr>
</thead>
</table>

\[
\text{Fixed Cost} = \frac{\text{Unit Revenue} - \text{Unit Cost}}{\text{No. Units}} = \text{Unit Margin}
\]

Comprehensive Municipal Financial Management – Part II

**Reporting, Audits, & Internal Control**

Our Objective: To Assist Financial Users

- Financial Reports by necessity need to be **SIMPLE** and above all else **TRANSPARENT** to governing officials who have little or no financial acumen.

Users of Financial statements should **NOT** have to be trained accountants. The report should make it easy for readers to discern their financial position AND DIRECTION for sound decision making within financial means.

You hire a skilled Carpenter to install your kitchen, but you should **NOT** have to be a skilled carpenter to cook, clean and otherwise use the kitchen. Likewise, you hire a skilled accountant to develop your accounting & reporting process, but you should **NOT** have to be a CPA to use the statements.
Relevant Accounting:
The Tool Used by Most Municipalities: "DCED" Formatted Accounting Structure

The Tool Suggested to Manage Fiscal Policies: "Operating Income" Formatted Accounting Structure

DCED: Department Of Community & Educational Development
GAAP: Generally Accepted Accounting Principals

The Information Tools Compared

DCED
- By Dept or Function of Government
- Multiple Pages
- Similar Costs – Split
- Immaterial Account Reporting
- Capital & Operating Are Mixed
- Recurring vs. Non Recurring are Mixed
- DCED not always reconciled to Annual CPA Audit

Operating Income
- Organized by Manageable Cost
- Concise – Single Page; can include supporting schedules
- Similar Costs – Grouped
- Material Account Grouping
- Capital & Operating Are Separate
- Recurring vs. Non Recurring are Separate

Aims to apply a common format to all municipalities to ensure they capture similar costs in a consistent manner, allowing for comparisons. How much do townships spend on public works?

The Information Tools Compared

Two Issues:

- Discernment of Revenue/Cost Structures
- Mixing Capital & Extraordinary with Operating

Discernment of Revenue-Cost Structure

<table>
<thead>
<tr>
<th>Natural Class</th>
<th>Utilities</th>
<th>Legal</th>
<th>Engineering</th>
<th>Supplies</th>
<th>Reported Per DCED Format</th>
</tr>
</thead>
<tbody>
<tr>
<td>General Govt.</td>
<td>$475</td>
<td>$90,000</td>
<td>$700,000</td>
<td>$30,000</td>
<td>$600,457</td>
</tr>
<tr>
<td>Public Safety</td>
<td>$1,204</td>
<td>$15,000</td>
<td></td>
<td>$136,294</td>
<td></td>
</tr>
<tr>
<td>Legislature</td>
<td>$55</td>
<td>$20,000</td>
<td></td>
<td>$22,058</td>
<td></td>
</tr>
<tr>
<td>Public Works</td>
<td>$2,827</td>
<td>$35,000</td>
<td>$500,000</td>
<td>$687,827</td>
<td></td>
</tr>
<tr>
<td>Total For G.A.A.P or Managerial Format for Treasurer's Report</td>
<td>$6,656</td>
<td>$130,000</td>
<td>$800,000</td>
<td>$312,000</td>
<td>$1,200,654</td>
</tr>
</tbody>
</table>

Note that total of the two formats MUST agree.

Mixing Capital with Operating, and Routine with Extraordinary

<table>
<thead>
<tr>
<th>Year</th>
<th>Income</th>
<th>Expenditure</th>
<th>Net Surplus (Deficit)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Year 1</td>
<td>$2,000,000</td>
<td>$1,700,000</td>
<td>$300,000</td>
</tr>
<tr>
<td>Year 2</td>
<td>$2,050,000</td>
<td>$1,993,000</td>
<td>$57,000</td>
</tr>
<tr>
<td>Year 3</td>
<td>$2,550,000</td>
<td>$3,586,000</td>
<td>($1,036,000)</td>
</tr>
<tr>
<td>Year 4</td>
<td>$2,060,000</td>
<td>$2,110,000</td>
<td>($50,000)</td>
</tr>
<tr>
<td>Year 5</td>
<td>$2,215,000</td>
<td>$1,765,000</td>
<td>$450,000</td>
</tr>
</tbody>
</table>

Without which, a Municipality cannot:
- Acquire Capital Equipment
- Undertake projects, or new services
The point is to present in a format where Operating Income – or Loss – is OBVIOUS to Policy Makers.

### Operating Income (GAAP Like) Format

**Same Data Recast into Operating Income Format**

<table>
<thead>
<tr>
<th>Year 1</th>
<th>Year 2</th>
<th>Year 3</th>
<th>Year 4</th>
<th>Year 5</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Routine Revenue</strong></td>
<td>$2,000,000</td>
<td>$1,990,000</td>
<td>$2,060,000</td>
<td>$2,065,000</td>
</tr>
<tr>
<td><strong>Routine Expenses</strong></td>
<td>$1,700,000</td>
<td>$1,743,000</td>
<td>$1,760,000</td>
<td>$1,765,000</td>
</tr>
<tr>
<td><strong>Operating Income</strong></td>
<td>$300,000</td>
<td>$247,000</td>
<td>$300,000</td>
<td>$300,000</td>
</tr>
<tr>
<td><strong>Capital &amp; Extraordinary Items</strong></td>
<td><strong>Revenue (Expense):</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Recover Prior Years EIT</strong></td>
<td>$250,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Receive Grant Match</strong></td>
<td></td>
<td>$75,000</td>
<td></td>
<td>$150,000</td>
</tr>
<tr>
<td><strong>Start Internal EIT Collection</strong></td>
<td></td>
<td></td>
<td>$500,000</td>
<td></td>
</tr>
<tr>
<td><strong>Purchase Grader</strong></td>
<td></td>
<td></td>
<td>($250,000)</td>
<td></td>
</tr>
<tr>
<td><strong>Rebuild Street Light</strong></td>
<td></td>
<td></td>
<td></td>
<td>($150,000)</td>
</tr>
<tr>
<td><strong>Legal Settlement</strong></td>
<td></td>
<td></td>
<td></td>
<td>($200,000)</td>
</tr>
<tr>
<td><strong>New Township Building</strong></td>
<td></td>
<td></td>
<td>($1,800,000)</td>
<td></td>
</tr>
<tr>
<td><strong>Net of Capital Exp.</strong></td>
<td>$75,000</td>
<td>$300,000</td>
<td>($350,000)</td>
<td>$150,000</td>
</tr>
<tr>
<td><strong>Net Surplus (Deficit)</strong></td>
<td>$75,000</td>
<td>$247,000</td>
<td>($1,036,000)</td>
<td>$450,000</td>
</tr>
</tbody>
</table>

### Operating Income Exercises

1. **Routine Revenue**: $2,000,000
   - Year 1: $2,000,000
   - Year 2: $2,150,000
   - Year 3: $2,250,000
   - Year 4: $2,460,000
   - Year 5: $2,465,000
   - Operating Income: $300,000
2. **Routine Revenue**: $2,000,000
   - Year 1: $2,000,000
   - Year 2: $1,990,000
   - Year 3: $1,850,000
   - Year 4: $1,825,000
   - Year 5: $1,820,000
   - Operating Income: $300,000
3. **Routine Revenue**: $2,000,000
   - Year 1: $2,000,000
   - Year 2: $1,990,000
   - Year 3: $1,820,000
   - Year 4: $1,825,000
   - Year 5: $1,820,000
   - Operating Income: $300,000

DCED can be a VERY good format in larger entities with multiple departments that have an “economy of scale. It is a format not well applied where costs would have to be allocated in small towns.

### Designing A “GAAP Like” Report:

- **Establishing the Baseline Year**
  - Identify Recurring Revenue & Expense
  - Develop Chart of Accounts – Account Groupings
  - Set Up Various Municipal Funds
  - Separate High Activity (e.g. General) from Low Activity (e.g. Fire) funds
  - Keep Developer Escrow Funds Separate
  - Do NOT run transactions through General Fund
Operating Income Formatted Reporting:
Takes about 3 years to develop and mature before rewards for the effort become evident:

- 1-2 years to format – you will likely have iterations before you settle on your standard format
- Third year establishes the trend
- Most likely, you will be able to anticipate certain revenues and expense beforehand; but having the ACTUAL three year result adds certainty and precision to your policy decisions.

Other Tools
- Multi Year Operating Budgets
- Developer Escrow Fund
- Professional Fees Management
- Minor Funds other than General Fund
  - Example – Police
  - Example – Fire
  - Inspections
  - Code Enforcement
  - Capital Plan – *Cause we are a Capital Intensive Business*

Reporting – Your Treasurer’s Report

- Current Year Activity: Summary on 1 or 2 pages for each of two major funds including General
- 2 Pages for ALL of 7 low activity minor funds
- Total Pages – 95: Includes supporting schedules that tie to Summaries. We require it on a Quarterly basis. That said, you can grasp what is need in 2-4 pages, then “drill down” if needed.
- Comparatives: Prior Year & Budget

Reporting – Your Treasurer’s Report

- Avoid “Fund Creep” – adding new separate minor funds, when a specific ledger account will do.
- Separate all Police Costs from General Fund into separate distinct fund. This is very useful for Labor negotiations and right sizing your department. This is contradictory to GASB, but a solid Management Accounting principal. Arbitrators like this. Auditors at year end will consolidate with General Fund.

Remember the emphasis of this presentation is an accounting format that aids in MANAGEMENT, not regulatory/statutory/standards reporting.

Multi Year Operating Budgets

- Municipalities have more static than dynamic microeconomic structures
- Four Back, Current Year, & Five Forward
- Estimates where the Fund Balance will be at the end of three and five years
  *Decisions become deliberate, not reactive!*

Reporting – Your Budget

- Generally, it should almost mirror the Treasurer’s Report in format.
- Big difference is Treasurer’s Report is a score card of the past, Budget looks forward.
- Our Budget seeks to project Fund Balance 5 years out; which is a prognosis of when we might have to increase taxes. That said, the 5 year look forward has most assuredly helped us push those events further into the future.
Let's Build a Budget

Operating Revenue
- Real Estate Tax
- EIT
- Transfer Tax
- Fees

Operating Expenses
- Payroll – Budgetary Goals
  - FICA/Medicare
  - Staff Listing
  - Rates
  - Projections (COLA, steps, etc.)
  - Overtime
- Professional Fees – Budgetary Goals
  - Legal
  - Engineering
  - Other (Audit, stenographer, etc.)

Let's Build a Budget

Operating Expenses Cont'

Road Materials

<table>
<thead>
<tr>
<th>Materials</th>
<th>Baseline</th>
<th>Year 1</th>
<th>Year 2</th>
<th>Year 3</th>
</tr>
</thead>
<tbody>
<tr>
<td>None</td>
<td>$120,000</td>
<td>$130,000</td>
<td>$128,000</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Materials</th>
<th>Baseline</th>
<th>Year 2</th>
<th>Year 3</th>
<th>Year 4</th>
</tr>
</thead>
<tbody>
<tr>
<td>$80,000</td>
<td>$120,000</td>
<td>$130,000</td>
<td>$128,000</td>
<td></td>
</tr>
</tbody>
</table>

Reporting – Supporting Schedules & Detail
- Staff Narratives explaining significant deviations from budget
- Make sure Treasurer’s Report includes Balance Sheets
- Operating Statistics (Issued Permits, Snow Storm Report, Police Stats, etc.)
- EIT Report – Management Issue: Non Resident EIT, Penalties, EIT Stats
- Cash & Investment Report: rates, amounts, locations of funds.
- Developer Escrow – always best that this NOT – repeat - Not be co-mingled with Township Funds. Allowed to charge fees for processing to Developers.
- Professional Fee Summary: By Fund, By Profession, By Project. We want as little charged to meetings or miscellaneous as possible.
- Summary of the Combined Fund Balances
- “Project Receivable” schedule of expected Capital Inflow from Developers. In the present climate, collectability is at risk

Audits

Audits – What they are & what they are not
- They are (typically) narrow scope tests, with an attestation by the auditor on the results of said tests, and a statement affirming (or not), THE RELIABILITY OF THE FINANCIAL STATEMENTS.
- They are NOT a guarantor against fraud, inefficiency, mismanagement or any sort of malfeasance.

Audits – Routine Audits in Municipal Government
- Annual Financial Statement Audit
  - Attestation on the results of operations, and the financial position of the local government
- Annual Liquid Fuels Audit (3rd Party Statutory)
  - Attestation on the compliance of the municipality regarding its conformity to the rules on the use of Liquid Fuel Funds
- Annual EIT Audit (Going away as we have known it)
  - Not always done by the municipality, and of little value
- Periodic Worker Comp (3rd Party Statutory)
  - Affects Workers Comp Premiums
Audits – Discretionary

- Performance Audits
  - An assessment on the effectiveness (meeting mission) and/or efficiency of a given operating task, department or function of a Business Unit.

- Forensic Analysis/Audits
  - Testing and compilation of detail transactions into a coherent and succinct picture

- Compliance Audits
  - More or less checklist or yes/no verification that the entity is in compliance to the rules, laws, policies, procedures currently in place. Compliance does not necessarily mean efficiency and effectiveness.

Choosing the Right Auditor for the Right Audit

Some Examples:
- CPA - Certified Public Accountant (State License)
- CFF - Certified in Financial Forensics
- CMA – Certified in Management Accounting
- CISA – Certified Information Systems Auditor
- CIA – Certified Internal Auditor
- CFE – Certified Fraud Examiner
- ABV – Approved in Business Valuation
- PE – Professional Engineer (State License)

Choosing the Right Auditor - Specialists

- Performance Audit for Police Department
  - Hired a Retired Chief with good leadership ability, and business & management sensibilities. He was educated & well trained in Commonwealth Law Enforcement. Recommendations (from a 45 page report) included “Short Form” police report for minor service calls, and zone patrols. The cumulative effect was to improve department productivity, reducing the need for more officers.

- Benchmark Audit for Payroll & Benefit Practices
  - Hired a retired Human Resources Manager for PP&L, now in private consulting. Noted that our pay scales were nearly perfect (except for one employee deemed to be under paid) in that no one was over or under paid for there jobs in our geographic area.
  - Noted some weaknesses in documentation practices that were since amended avoiding potential liability issues
  - Moving Pension Benefits from Defined Benefit to Defined Contribution for all new hires. Potential savings from this move over long term. However, the responsibility for investment shifts from employer to employee. By moving to “Defined Contribution” in periods where fund would beat the actuary, the township loses; conversely, if the fund does worse than the actuary, the township saves.

- Compliance with State Purchasing Rules
  - A neighboring Borough was reported to have avoided State Open Bid Laws. We engaged our CPA to do specific compliance procedures to provide assurance that purchasing was executed in full compliance of the rules. The results yielded no major exceptions, but recommended some improved documentation on the $4,000 to 9,999 level purchasing.

The Elected Auditors

- With the financial complexities now present, having a person untrained and inexperienced in Accounting, Financial Reporting, and non conversant in audit standards and applicable GASB rules is NOT good.

- The auditors still set salaries for Employee-Supervisors

- Assign a special audit task to the Elected Auditors
  - In Richland, the auditors test 100% of all disbursement for legitimacy.

The “Audit” and Fraud

- The annual financial audit has a very limited standard in preventing or detecting fraud.

- Should (1) a fraud have occurred, and (2) the auditor be in compliance with the standards of practice, and (3) the auditor can prove said compliance, then the auditor will not be held liable for failure to prevent or detect said fraud.

It is a dereliction of duty for an official to rely on the audit report for that purpose, though the vast majority in fact do.
Review Audits
- Police
- EIT
- Annual Financial

Internal Control
Ask Graucho!

Control Areas
- Preventive Control
- Detective Control
- Operating Control
- Risk & Exposure
- Use of Quick Books

Small Shop Internal Control
- Bonding
- Disbursement - Payment of Bills
- Check Runs from System Disbursements, not typed out lists of bills
- Revenue
- SAS 99 – Auditors discussion on potential means of committing a fraud

Internal Control - Finance
In small Municipalities – keep it basic & at a high level:
- Two signatures on all checks
- Trended Financial Reporting
- Annual Audit of statements by a CPA
- Use Elected Auditors, or others, for a 100% check review
- Test Compliance with State Open Bid Laws

Comprehensive Municipal Financial Management – Part III
Financial Specifics I
Revenue Issues
Financial Specifics I
(Revenue Streams, Taxes, Fees & Fee Structures, Cable Franchise Fees, Build your Tax Base: Zoning, Codes, & Developer Management, Cash Management, Grants, Use of Volunteer Boards)

Earned Income Tax

Earned Income Tax Collection
The Core Issue:
Compare ACTUAL collection to what SHOULD BE collected
The question is “HOW do you get there?”

The new law does not get municipalities off the hook.

A good solution?
Data interface with Pennsylvania State Income Tax returns. These are available to School Districts, but not municipalities. Since we collect for the school district, we did such an interface and came up with about 100 potential non filers, as opposed to about 7,400 filers. That amounts to a 98.7% compliance rate.

Municipalities need to make collectors provide accountability.

EIT Basics:
Watch your townships EIT interests.

Earned Income Tax Collection
- Increase “Top Line” Collections – the primary issue
  - Increased Accuracy over Payers
  - Identity & Press Claims against other collectors incorrectly with holding home municipality tax payments
  - Identify & Press Claims against non filing delinquent taxpayers
  - Estimated Payments
- Accelerate Collections – Third Party Holdbacks in the past went up to 9 months
- Maximize Investment Income
  - Coordinate between School District & Municipality/Municipalities
  - Break point between outside vs. self collection
  - Accounting for the sources of cash receipts – e.g. Non Resident Payers
  - Metrics for community planning
Aim for the biggest “Net Collection”

- 2% of $2 million = $40,000
- Net Collection = $1,960,000
- 5% of $2.3 million = $115,000
- Net Collection = $2,185,000

**EIT – Cost of Collection**

*Secondary issue*

Typically run 2-6% of remittances – Richland achieved a 1.5% cost of collection in 2005-6.

**Earned Income Tax Collection**

*“Metrics” for Financial Planning*

- Number of Commercial Payers Submitting Quarterlies
- Number of Returns Filed
- Number of Quarterly Estimates: Typically Self Employed
- Gross Community Income
- Claims For and Against

*Use data to size office, monitor collections, project enabling revenue and apply to community planning.*

**EIT ASSESSMENT PROCESS**

- Day to day administrative office operations
- Systems – Hardware/Software
- Reporting – Financial/Management
- Controls - Accounting/Auditing/Operational
- Personnel – Capabilities/Performance
- Organization - Management
- Planning - Strategy/Process

**EIT Policy Issues**

- Deny deductibility of “hobby losses” against Earned Income
- Catch non-filers, match data files against school district.
- Deposit Cash ASAP

**Earned Income Tax Chart of Accounts:**

**EIT Receipts:**
- Estimated Payments
- Final EIT Payments with Tax Returns
- Resident Withholding
- Penalties
- Non Resident Withholding
- Late Fees
- Claims Due

**EIT Disbursements:**
- Tax Refunds
- Claims Paid
- Home Municipality
- School District
End Result:

- Richland increased its collections by $260,000, the School District increased its collection by $520,000 – a 27% increase in the first year since the consult.

- To be sure, some of this was due to natural growth, but much was due to improved reporting, procedures & internal controls.

Optimal Collection Agency:

*By School District*

Points to Remember

- Usually collected by an independently elected collector
- Core issue is simple:
  - Make sure you receive –timely- the tax due the municipality
  - The amount equals: Assessment x Millage
  - There will always be differences for late payers – these should be minor

Property Tax

Other Revenue
Cable Franchise Fees

1. Make sure Street Lists & Zip Codes are correct:
   - FY 2001 DCED Report – Richland received $116,000 from (Census -9,920) in Cable Fees when Plumstead received $38,000 (Census -11,409)

2. Collection Issue: Quarterly vs. Annual Remittance

3. Can charge different rates with legal maximum
   - Items 1 & 2 are business issues, item 3 gets into policy/philosophy

Service Fee Structure

- Charge maximum possible on those issues and development with greatest impacts on public resources
- Charge least possible, or eliminate charges altogether on non-impact construction like accessory use. These items can take as much admin time as a high impact issue. Wise to require property owners not construct on utility easements and comply with setback requirements.
- Review periodically for COLA – benchmark with municipal neighbors.
- Eliminating certain fees on accessory use usually will save more in administrative time than the loss in revenue, and avoids pushing the municipality into the next volume level that requires additional labor.
  
  Philosophy will drive Fees

Developer Contributions

- Mitigates against Developer Impacts
- Park & Recreation Fee Ordinance
- Maintain a Strict S.A.L.D.O., where municipality can trade waivers and variances for infrastructure and capital donations:
  - Traffic Lights
  - Stream Impact Issues
  - Round About & Other Traffic Improvements
  - Open Space Donations
  - Fire & Police Support Donations

Philosophy will drive how you treat with Developers

Developer Contributions

Real Examples

- Round About & Road Extension $2 million
- Over 300 Acres in Donated Park Land ~ $3 million
- Traffic Lights ($60,000-$250,000 each)
- Intersection Relocations (> $500,000)
- Rebuilt Bridges ($250,000 +)
- Bike & Hike Trail Systems ~ 3 miles to date

Non Tax Revenue Ideas

- Improved Collections of already Enacted Taxes
  - Cable Franchise Tax
  - Earned Income Tax
- Community Based Fund Raisers
  - Golf Outings
  - Sponsorships for Community Days
- In-Kind
  - Volunteers Organization
  - Developer Contributions
  - Cash
  - In Kind
  - News Letter – Advertising Sales
  - Services & Permit Fee Structure
  - Cash Management

Grants

- Closed Loop Traffic System
- Police Equipment Grants & COPS UHP
- Rivers Conservation
- Community Development Block Grant
- DCNR Grants
- Parks Acquisition & Development Grants
- Stream Stabilization & Cleanup – Shelly Stream
**Grants & Professional Fees**

- Bidding for Professional Services, really does not work to cost/value advantage for a specific project – Not required in PA.
- RFP for new Appointed Engineer can work: interview and see how they differentiate their service from the others: Ask:
  - How do you bring value above your competitors
  - How will you manage your cost to our municipality?
- Competition is good: spread the work around – we use 3 Engineering Firms.
- References
- Standing offer to Engineers: Bring in a grant, and you get the work. This has worked very well for our township – idea came from one of our Engineering Firms (One of their Shareholders was a Township Manager for over 20 years)

**Volunteer Boards**

- Parks - Community Day
- Facilities Committee – Police, Street Lights
- Preservation Board – Open Space
- Trails Committee – Walking, Nature & Bike Paths
- Police Panel – Hiring Searches

**Comprehensive Municipal Financial Management – Part IV**

**Financial Specifics II**

**Expenditures**

- Example – Good Spending
  - Creating Professional Manager Position
  - Total Outlay: $2,500
  - Total Cumulative Benefit AFTER Cost: $9,200

- Example – Good Spending
  - Recycling Consultant
  - Total Revenue: $539
  - Total Expense: $469

- Example – Good Spending
  - Cable Franchise Fee Audit
  - Total Revenue: $12,000
  - Total Expense: $10,500
  - Total Revenue: $5,900
  - Total Expense: $5,400
  - Total Revenue: $4,500
  - Total Expense: $4,200
  - Total Revenue: $3,500
  - Total Expense: $3,300
  - Total Revenue: $2,500
  - Total Expense: $2,400
  - Total Revenue: $2,000
  - Total Expense: $1,900
  - Total Revenue: $1,500
  - Total Expense: $1,400
  - Total Revenue: $1,000
  - Total Expense: $1,000
  - Total Revenue: $500
  - Total Expense: $500
  - Total Revenue: $100
  - Total Expense: $100
  - Total Revenue: $50
  - Total Expense: $50
  - Total Revenue: $20
  - Total Expense: $20
  - Total Revenue: $10
  - Total Expense: $10
  - Total Revenue: $5
  - Total Expense: $5
  - Total Revenue: $1
  - Total Expense: $1
  - Total Revenue: $0
  - Total Expense: $0

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*U. Makefield projects 22% 2011 tax bump
Doverlawn Township seeking at tax increase.*
Inspections

- Issue – dedication of developer built infrastructure coupled with ongoing municipal maintenance and liability
- More of an “Internal Operating Control”

Code Enforcement

In a word:

Complaint Driven!

Aggressive Code Enforcement is very costly, including unwanted lawsuits.

Professional Fees

- Maintain by Profession, by Project in a “roll up” to detail format.
- Best managed by assuring paid in part or in full by other entities (grants or developers)
- Cover wherever you can with user charges
- Develop a billing – payment process that captures charges by fund, profession, and project.
- Taxpayer funded fees are best targeted to a specific project.
- Don’t entertain developers unless they are current in their bills

Police Economy

Police Cost Basics
- Almost Entirely a Fixed Cost Operation
- Cost to deploy one officer in Bucks County > $110,000
- Each Officer will effectively provide about 1,760 Hours of Productive Service (in a good year) which includes court time. The rest is PTO, Training, etc.
- In 2002-3, Richland had the highest Officer-Call Ratio in the entire southeast, including Philadelphia
- Went from zero to an 11 person department in five years without new taxes, and avoided increasing taxes for a further five years

How did we achieve this?
- Five Year Time & Grade Scale
- Discreet on 24-7 and other coverage – Look when calls occur
- Liberal Personnel Policies
- Liberal use of technology
- Grants (Equipment, COPS UHP)

Fire Service Economy

- There is none: It is an emotional, cultural, historical, social and political issue.
- Pennsylvania has twice as many companies and half as many volunteers as it needs
- Consolidated transactions, front ended subsidies – Improved Cash Flow
- Pushing local companies to joint venture and consolidate

Comprehensive Municipal Financial Management – Part V

Financial Specifics III

Other Issues
Governing in a Bad Economy

- A time to audit!
- A GREAT time for Union Negotiations
- Crafting Tax Increases
  - OPT
  - Real Estate Tax
  - Voter Referendum EIT
- Operations Improvements
- Reorganizing staff (early retirement, bringing back part time)

Cash Management

- Invest the “Cash Flow” or current period revenues and expenses short term
- Invest the accumulated Fund Balance long term
- Vehicles available are PLGIT, CD’s, Treasury Bills
- “Ladder” these instruments to assure liquidity and attain greatest yields.
- Develop Reporting/Accounting structures

Cash Management (In 000)

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- Develop Reporting/Accounting structures

Richland Township – 2005
Real Estate Tax vs. Interest Income

Accounting Softwares

- QuickBooks is a popular small business package
- Other packages: Peachtree, Account Edge, Bookkeeper, DaEasy, Simply Accounting, CYMA, Cougar Mountain
- Relatively inexpensive (typically less than $500)
- Some control issues

Your Treasurer

- Need not be a CPA, or even have a 4 year degree in accounting, but
- Should be knowledgeable on Balance Sheets (Assets, Liabilities, Equity), Revenue & Expense Statements, & Capital vs. Operating. Double entry Accounting/Bookkeeping an absolute must.
- Good Organization Abilities: Organize transactions, presentation, funds, etc.
- Note there is a National shortage of skilled accounting people; the average age of a practicing CPA is about 53 years old.
- You can also engage CPA’s to supplement your Treasurer function.
Developer Escrow Fund

- Maintain separate Ledger and Bank Account
- Can charge an administrative fee (~5%)
  - (Also a non-tax revenue)
- If Developers Account is in arrears, approvals, releases, etc. are withheld!

Capital Plan

- The essence of the one completed plan at Richland Township in Bucks County was to eliminate about $1.2 million of expected capital outlays over the next ten years, when compared to the similar outlays the past ten years.
- It is a “roll forward living document” – when the new police building was over budget, we were able to fund it by quick ID of future outlays that could be deferred.

Capital Plan

- Inventory of ALL Long Term Assets
- Target Replacement Schedule for Existing Asset Base – optimize with a bias for cost savings (look at Road Maint Schedule)
- Plan YOUR Outlays for NEW Infrastructure and other capital outlays
- Policy Recommendations
- Major Factor in S&P award of AA+ Bond Rating

Round About

Financial Impacts
- Built & Paid by Developer, then dedicated to Township, thus avoiding Prevailing Wage Rules
- No traffic light
- Fewer and less severe accidents & resulting Police Calls

Renewable Energy Complex

Rough Specs:
- Cost: $2.0mm, (offset by $500k Grant)
- Debt Service: ~ $84,000/Yr – 20 Yrs
- Town Electric: ~ $160,000/Yr
- Electric Savings: ~ $60,000/Yr
- Electric Credits: ~ $160,000
- Cash Flow after Debt Service
- Site Development Permanent
- Expected Life of System 40-50 Yrs
- Panels – Warranty for 20 Years
- Panels could work up to 50 Years; replaced light a light bulb on a lamp
Capital Asset Management

- Large or small, Utilities & Municipalities are capital as opposed to labor intensive operations. Management of capital fixed assets GREATLY impacts the effectiveness of your Utility.
- Note concepts & principles to employ a fixed asset management process TAILORED for your utility/township, to enable a solid “Return on Investment”.
- Note “right sizing” solutions to your scale of operations.

Why Asset Management?

- Minneapolis Bridge Collapse
- City of Atlanta - $4 billion sewer/water renewal
- National Treated Water Loss Rate: 20%
- Water Main Break – Sellersville, PA - May 27, 2008
- 2008 Main Break – Bensalem, PA
- And-------

Definitions:

- “Enterprise” Solutions
  Early software technologies were primarily single task “stand alone” routines. Newer Software designs now integrate across an enterprises’ operating needs. In essence each system talks to the other and updates the various data base elements throughout a system. As applied to WSA, the Asset Management System will update the General Ledger, Payroll, GIS and all related data base systems.

- Geographic Information System (GIS)
  Computerized Mapping System that displays the utility infrastructure and is capable of detailing all information related to any item, area or subset of the map presented.

- General Ledger & Other Subsidiary Ledgers
  These are an organizations financial books, where all financial activities are recorded and eventually compiled into financial statements.

- Asset Management:
  Process whereby the FIXED TANGIBLE ASSETS are managed for OPTIMAL USEFUL ECONOMIC LIFE. This includes (1) a maintenance program designed to maximize an assets operational life, and (2) a CAPITAL REPLACEMENT PROGRAM that recognizes the point in time it becomes wasteful to continue to maintain an existing asset. This process is done intuitively every day in all walks of life. An AMS will add multiples on “an order of magnitude” in the PRECISION of when to maintain and when to replace/retire.

- It’s simply cost effective – very much so!

- Asset Management Software Vendors:
  Microsoft EXCEL
  GBA

- Lot’s of literature on Asset Management
  Returns typically range between 6% & 12% on the asset base.
Summary: Best Management Practices

- A Strategic Vision of your community
- Design the GAAP Based Treasurer Report
- Prepare Five Year Operating Budget/Plan
- Work on the “Line Item Metrics”
- Long Term Capital Plan

Then – Reinvest into Operations, Public Policy & Infrastructure

Our Objectives Today:

- Present operating issues, then relate them to financial impacts
- Treasurer’s Report is nothing more than a score card; Operations drive finance more than the other way around. (But for money, there will be no operations.)
- Orient thinking to SUCCINCT FINANCIAL REPORTING on salient issues.
- Reports provide plenty of detail; BUT always have a Lead schedule that presents the “Big Picture”. Without an organized summary, it becomes eyewash and everyone zones out.
- Give YOU ideas on achieving the best practical Treasury Function.
- Most municipalities will not have a CFO, Payroll Manager, Billing Department etc.
- The takeaway?
  - A vision of the concepts & principals which can be implemented in your community. That vision when implemented will give your local government financial strength & vitality enabling solid municipal services throughout your community.

Our Objective is NOT:

- To make you an accountant or teach you accounting
- All this is aimed at one thing: Informed Wise DECISIONS by users of financial information.

Comprehensive Municipal Financial Management – Part VI

Interactive Exercises

Prepare a Budget, Read a Treasurer’s Report, Read an Audit Report