

**CITY OF TONAWANDA,
NEW YORK**

*Basic Financial Statements, Required
Supplementary Information and Federal and
New York State Department of Transportation
Financial Assistance Schedules for the
Year Ended December 31, 2012 and
Independent Auditors' Reports*

CITY OF TONAWANDA, NEW YORK
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INDEPENDENT AUDITOR'S REPORT

Honorable City Council
City of Tonawanda, New York:

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the City of Tonawanda, New York (the "City"), as of and for the year ended December 31, 2012, and the related notes to the financial statements, which collectively comprise the City's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Basis for Adverse Opinion on Discretely Presented Component Unit

Management has not included the City's legally separate component unit in the City's financial statements. Accounting principles generally accepted in the United States of America require the financial data for that component unit to be reported as a discretely presented component unit. The amounts by which this departure would affect the assets, liabilities, net position, revenues, and expenses of the discretely presented component unit have not been determined.

Adverse Opinion

In our opinion, because of the significance of the matter described in the “Basis for Adverse Opinion on Discretely Presented Component Unit” paragraph, the financial statements referred to previously do not present fairly, the financial position of the discretely presented component unit of the City, as of December 31, 2012, or the changes in financial position thereof for the year then ended, in accordance with accounting principles generally accepted in the United States of America.

Unmodified Opinions

In our opinion, the financial statements referred to previously present fairly, in all material respects, the respective financial position of the governmental activities, each major fund and the aggregate remaining fund information of the City as of December 31, 2012, and the respective changes in financial position and the respective budgetary comparisons for the General, Sewer and Water Funds for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management’s Discussion and Analysis as listed in the forgoing table of contents be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management’s response to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated March 20, 2013 on our consideration of the City’s internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the City’s internal control over financial reporting and compliance.

March 20, 2013

MANAGEMENT DISCUSSION AND ANALYSIS

CITY OF TONAWANDA, NEW YORK
Management's Discussion and Analysis
Year Ended December 31, 2012

As management of the City of Tonawanda, New York (the "City"), we offer readers of the financial statements of the City's primary government this narrative overview and analysis of the financial activities of the City for the year ended December 31, 2012. The financial statements referred to above include only the primary government of the City, which consists of all funds, organizations, institutions, agencies, departments, and offices that comprise the City's legal entity. The financial statements do not include financial data for the City's legally separate component unit, the Tonawanda Housing Authority, which accounting principles generally accepted in the United States of America require to be reported with the financial data of the City's primary government. We encourage readers to consider the information presented here in conjunction with other information contained in the City's financial statements, which follow this narrative.

Financial Highlights

- The liabilities of the City exceeded its assets at the December 31, 2012, resulting in a *net deficit* of \$3,032,419. This net deficit includes an *unrestricted net deficit* of \$15,193,934. This significant unrestricted net deficit is caused by long term liabilities of the City which are not required to be funded until due. The most significant items are pollution remediation obligation (\$11.9 million), compensated absences (\$2.8 million) and other post-employment benefits (\$2.0 million).
- During the year ended December 31, 2012, the City's net deficit improved by \$1,209,717 as a result of operating activities for the year.
- At the close of the current fiscal year, the City's governmental funds reported combined ending fund balances of \$3,433,800, a decrease of \$1,081,869 in comparison with the prior year.
- The General Fund reported an unrestricted, unassigned fund balance of \$2,105,176 at December 31, 2012. This represents approximately 11.0% of the annual expenditures in the General Fund.

Overview of the Financial Statements

This discussion and analysis are intended to serve as an introduction to the basic financial statements of the City's primary government. The basic financial statements of the City's primary government comprise three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements themselves.

Government-wide financial statements. The *government-wide financial statements* are designed to provide the reader with a broad overview of the City's finances, similar in format to a financial statement of a private-sector business.

The *statement of net position* presents information on all of the assets, liabilities and deferred inflows/outflows of resources of the City's primary government, with the difference between the two reported as *net position*. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the City's primary government is improving or deteriorating.

The *statement of activities* presents information showing how the government's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, *regardless of the timing of related cash flows*. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future periods (e.g. earned but unused vacation leave).

The government-wide statements include the City's governmental activities. The governmental activities include most of the City's basic services including general government, public safety, transportation, economic development, sanitation, sewer, water, and culture and recreation. Real property taxes, non-property taxes, charges for services and state aid fund most of these activities.

The government-wide financial statements can be found on the two pages immediately following this management's discussion and analysis section.

Fund financial statements. A *fund* is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The City, like other state and local governments uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the City can be divided into two categories: governmental funds and fiduciary funds.

Governmental funds. Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental funds focus on near-term inflows and outflows of spendable resources, as well as, on balances of spendable resources at the end of the fiscal year. Such information may be useful in evaluating a government's near-term financing requirements.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for *governmental funds* with similar information presented for *governmental activities* in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between *governmental funds* and *governmental activities*.

The City maintains seven individual governmental funds. Information is presented separately in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures, and changes in fund balances for the General, Sewer, Water and Capital Projects Funds, each of which is considered to be major funds. Data from the other three governmental funds are combined into a single aggregate presentation.

The City adopts an annual budget for its General, Sewer and Water Funds. A budgetary comparison statement has been provided for these funds to demonstrate compliance with this budget.

The financial statements for governmental funds can be found in the fund financial statements, following the government-wide financial statements.

Fiduciary fund. The City is trustee, or fiduciary, for its agency fund. All of the City's fiduciary activities are reported in a separate statement of fiduciary net assets. We exclude these activities from the City's government-wide financial statements because the City cannot use these assets to finance its operations.

The Fiduciary Fund financial statement is in the fund financial statements section of this report.

Notes to the financial statements. The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found following the fund financial statements section of this report.

Government-wide financial analysis

As noted earlier, net position may serve over time as a useful indicator of a government’s financial position. In the case of the City, liabilities exceeded assets by \$3,029,050 at the close of the 2012 fiscal year.

TABLE 1 — CONDENSED STATEMENT OF NET POSITION

	<u>2012</u>	<u>2011</u>
Current assets	\$ 10,243,426	\$ 9,365,921
Capital assets	<u>20,670,824</u>	<u>16,277,372</u>
Total assets	<u>30,914,250</u>	<u>25,643,293</u>
Current liabilities	5,984,493	4,185,538
Non-current liabilities	<u>27,962,176</u>	<u>25,699,891</u>
Total liabilities	<u>33,946,669</u>	<u>29,885,429</u>
Net position (deficit):		
Net investment in capital assets	10,624,151	9,576,539
Restricted	1,537,364	1,482,222
Unrestricted	<u>(15,193,934)</u>	<u>(15,300,897)</u>
Total net position (deficit)	<u>\$ (3,032,419)</u>	<u>\$ (4,242,136)</u>

The City’s investment in capital assets (such as land, buildings, machinery, equipment, and infrastructure) less any related debt used to acquire those assets that is still outstanding is the largest portion of total net position. The City uses these capital assets to provide services; consequently, these assets are not available for future spending. Although the City’s investment in capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets cannot be used to liquidate these liabilities.

The City also has certain portions of net position that are restricted for particular purpose. These restrictions increased slightly from 2011 to 2012, from \$1,482,222 to \$1,537,364.

The remaining component is unrestricted net position, which in the case of the City is a deficit balance of \$15,193,934, caused primarily by certain long-term obligations which are not required to be funded until due (i.e. compensated absences, indebtedness, pollution remediation obligations, other postemployment benefits etc.). This demonstrates that future funding will be necessary to liquidate long-term obligations.

The City’s total net position increased \$1,209,717 for the year ended December 31, 2012, as compared to a decrease of \$328,792 for the year ended December 31, 2011. The 2012 increase was the result of the City’s investment in infrastructure; whereas, the 2011 decrease was the result of operating activities.

A comparison of current assets to current liabilities for the government-wide activities as of December 31, 2012 and 2011 is provided in Table 2 below. The City had favorable current ratios of 1.71 and 2.24 which indicate that the City has sufficient assets to cover its current liabilities that will come due within a year.

TABLE 2 — CURRENT ASSETS AND LIABILITIES

	<u>2012</u>	<u>2011</u>
Current assets	\$ 10,243,426	\$ 9,365,921
Current liabilities	5,984,493	4,185,538
Ratio of current assets to liabilities	1.71	2.24

Governmental Activities. Table 3, as presented below, shows the changes in net position for the years ended December 31, 2012 and 2011:

TABLE 3 — CONDENSED STATEMENT OF ACTIVITIES

	<u>2012</u>	<u>2011</u>
Program revenues:		
Charges for services	\$ 3,069,116	\$ 2,847,629
Operating grants and contributions	295,293	186,512
Capital grants and contributions	2,606,558	1,513,215
General revenues	<u>18,063,459</u>	<u>17,723,363</u>
Total revenues	24,034,426	22,270,719
Program expenses	<u>22,824,709</u>	<u>22,599,511</u>
Change in net assets	1,209,717	(328,792)
Net position (deficit)—beginning	<u>(4,242,136)</u>	<u>(3,913,344)</u>
Net position (deficit)—ending	<u>\$ (3,032,419)</u>	<u>\$ (4,242,136)</u>

A summary of sources of revenues for the years ended December 31, 2012 and 2011 is presented below in Table 4:

TABLE 4 — REVENUES BY TYPE

	2012	2011	Increase/(decrease)	
			Dollars	Percent
Charges for services	\$ 3,069,116	\$ 2,847,629	\$ 221,487	7.8
Operating grants and contributions	295,293	186,512	108,781	58.3
Capital grants and contributions	2,606,558	1,513,215	1,093,343	72.3
Property taxes and tax items	10,192,543	10,003,951	188,592	1.9
Non-property tax items	4,830,921	4,786,165	44,756	0.9
Mortgage tax	161,551	119,726	41,825	34.9
Use of money and property	15,386	22,019	(6,633)	(30.1)
Sale of property and compensation for loss	48,290	54,985	(6,695)	(12.2)
Miscellaneous	212,664	134,413	78,251	58.2
Unrestricted state aid	2,602,104	2,602,104	-	0.0
Total program revenues	\$ 24,034,426	\$ 22,270,719	\$ 1,763,707	7.9

Overall revenues increased 7.9% from the 2011 fiscal year. Key elements of this increase are as follows:

- *Capital grants and contributions* — Increased \$1,093,343, or 72.3%, from the prior year. This increase is the result of the City’s receipt of funding from Erie County and the Federal government for the conclusion of the demolition and cleanup of the Spaulding Plant in 2012, as well as funds received from New York State for the Pavillion project.
- *Operating grants and contributions* — Increased \$108,781, or 58.3%, from 2011. This increase is mainly due to Federal grants received in 2012 for port security and fire equipment.
- *Miscellaneous* — Increased \$78,251, or 58.2%, from the prior year. This increase is largely the result of a one-time refund of prior years’ expense from insurance paid.
- *Other* — The City saw modest increases in property taxes and tax items (\$188,592), non-property tax items (\$44,756) and charges for services (\$221,487). These increases were the result of an increase in the real property tax rate, an increase in sales within the County and increase in a wide variety of charges to service users, respectively.

A summary of program expenses for the years ended December 31, 2012 and 2011 is presented on the following page in Table 5.

TABLE 5 — PROGRAM EXPENSES BY TYPE

	2012	2011	Increase/(decrease)	
			Dollars	Percent
General government support	\$ 2,668,352	\$ 2,640,871	\$ 27,481	1.0
Public safety	7,825,378	7,788,091	37,287	0.5
Transportation	5,156,115	4,615,023	541,092	11.7
Economic assistance and opportunity	32,450	46,348	(13,898)	(30.0)
Culture and recreation	1,713,907	1,691,092	22,815	1.3
Home and community services	5,086,194	5,531,790	(445,596)	(8.1)
Interest on debt	342,313	286,296	56,017	19.6
Total program expenses	<u>\$ 22,824,709</u>	<u>\$ 22,599,511</u>	<u>\$ 225,198</u>	1.0

Overall program expenses increased \$225,198, or 1.0% from the 2011 fiscal year. Key elements of this change are as follows:

- *Transportation* — Increased \$541,092 or 11.7% from the prior year. The most significant portion of this increase was due to development and maintenance at the Spaulding Commerce Park.
- *Home and Community Services* — decreased \$445,596 or 8.1% from the prior year. The decrease in 2012 was related to a larger increase in the estimate of the City’s pollution remediation obligation in the prior year.

Financial Analysis of the City’s Funds

As noted earlier, the City uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

Governmental funds — The focus of the City’s *governmental funds* is to provide information on near-term inflows, outflows, and balances of spendable resources. Such information is useful in assessing the City’s financing requirements. In particular, unassigned fund balance may serve as a useful measure of a government’s net resources available for spending at the end of the fiscal year.

At December 31, 2012, the City’s governmental funds reported combined ending fund balance of \$3,343,800, a decrease of \$1,081,869 from the prior year. Approximately 38.4%, or \$1,319,636, of the total combined fund balance constitutes *unassigned fund balance or assigned for a specific use*, which is available for spending at the City’s discretion. Fund balance of \$500,000 is *assigned fund balance* for subsequent year’s expenditures and self-insurance. Fund balance of \$1,537,364 is *restricted* to indicate that it is not available for new spending because it has already been committed to (1) workers’ compensation, (2) general liability insurance, (3) tax stabilization and (4) to restore historical property. In addition, the City has \$576,800 of *nonspendable fund balance*, which is an offset of prepaid expenditures.

The *General Fund* is the chief operating fund of the City. At December 31, 2012, the unassigned fund balance of the General Fund was \$2,108,545, while the total fund balance was \$4,627,221. As a measure of the General Fund’s liquidity, it may be useful to compare both the unassigned and total fund balance to total fund expenditures. Unassigned fund balance represents approximately 11.0% of total General Fund expenditures, while total fund balance represents 24.2% of that same amount.

The General Fund fund balance increased by \$178,032 during the 2012 fiscal year. This amount is favorable compared to the adopted 2012 budget, which anticipated using \$275,000 of General Fund fund balance.

Other major funds are the Sewer, Water and Capital Project Funds, which realized changes in fund balances of \$208,692, (\$37,518) and (\$1,422,324), respectively. The significant decrease in the Capital Projects Fund is mainly the result of capital project expenditures made in anticipation of the issuance of long-term debt.

General Fund Budgetary Highlights

During the year there was a \$206,100 increase in appropriations between the original and final amended budget in the General Fund. The increase in appropriations was mainly due to police and fire department equipment and personal services expenditures. The increase in appropriations was mainly funded by increases in estimated federal aid revenues.

Original Budget Compared to Final Budget—During the year the City amended the General Fund budget to increase revenues and appropriations by \$205,992 and \$206,100, respectively. Additionally, there was a need to make amendments to reallocate appropriations among departments as actual expenditures became defined during the year.

Final Budget Compared to Actual Results—The difference between the total final budget and actual revenues, expenditures and other financing sources were follows:

	Final Budget	Actual	Variance
Total revenues	\$ 19,326,042	\$ 19,172,009	\$ (154,033)
Total expenditures	19,507,550	19,150,377	357,173
Other financing sources	<u>156,400</u>	<u>156,400</u>	<u>-</u>
Budgeted and actual (use) or increase to fund balance	<u>\$ (25,108)</u>	<u>\$ 178,032</u>	<u>\$ 203,140</u>

When comparing appropriations to actual expenditures, positive variances occurred in every category, with the largest in transportation. This category produced positive variances in many areas such as highway commodities such as salt and electricity, which were not fully utilized during the year due to the mild winter.

Overall, the budget anticipated a use of fund balance of \$25,000. However, actual results showed that General Fund fund balance increased by \$178,032. Thus, an overall positive variance from the budget of \$203,140.

In both the Sewer and Water Funds there were no changes to the total adopted appropriations.

Capital Asset and Debt Administration

Capital Assets. The City’s investment in capital assets for its governmental activities as of December 31, 2012, amounted to \$20,670,824 (net of accumulated depreciation). This investment in capital assets includes land, buildings and building improvements, infrastructure, vehicles and equipment.

The City’s infrastructure assets are recorded at historical cost, or estimated historical cost, in the government-wide financial statements. The City has recorded all infrastructure assets regardless of when acquired.

All depreciable capital assets were depreciated from acquisition date to the end of the current year as outlined in the City’s capital asset policy.

Capital assets net of depreciation for the governmental activities are presented below:

TABLE 6 — CAPITAL ASSETS (NET OF ACCUMULATED DEPRECIATION)

	<u>2012</u>	<u>2011</u>
Land	\$ 328,850	\$ 328,850
Buildings and improvements	3,246,771	2,416,247
Equipment	2,955,847	2,671,093
Infrastructure	<u>14,139,356</u>	<u>10,861,182</u>
Total	<u>\$ 20,670,824</u>	<u>\$ 16,277,372</u>

Long-term Obligations. At December 31, 2012, the City’s long-term obligations consisted of bonds payable, compensated absences payable, capital leases, workers’ compensation claims, landfill post-closure costs payable, pollution remediation obligations and other postemployment benefits, which changed as included on the next page.

TABLE 7 — LONG-TERM OBLIGATIONS

	<u>Balance 2012</u>	<u>Balance 2011</u>	<u>Change</u>
Compensated absences	\$ 2,800,212	\$ 2,636,267	\$ 163,945
Landfill post-closure costs payable	400,000	420,000	(20,000)
Pollution remediation obligations	11,900,000	10,950,000	950,000
Other postemployment benefits	2,021,535	1,757,379	264,156
Bonds payable	10,015,000	9,038,499	976,501
Capital leases	18,737	32,075	(13,338)
Workers' compensation claims	<u>806,692</u>	<u>865,671</u>	<u>(58,979)</u>
	<u>\$ 27,962,176</u>	<u>\$ 25,699,891</u>	<u>\$ 2,262,285</u>

Additional information on long-term debt can be found in the notes to the financial statements.

Economic Factors and Next Year’s Budget

Located in the Western New York region, the City has struggled with the trying times that have become a characteristic of the area. The unemployment rate for the Buffalo-Niagara statistical area was 8.4% in December 2012, which is an increase from a rate of 8.0% a year ago. This rate is consistent with the New York State average of 8.2% but is unfavorable in comparison with the national average of 7.8%.

Although recent inflationary trends in the region, particularly in the real estate sector compared favorably to national indices, over the past two decades the region has experienced a steady decline in population and business. Despite the economic hardships, the City’s overall financial position remained relatively stable during the fiscal year ended December 31, 2012.

The City assigned \$375,000 of the General Fund’s fund balance at December 31, 2012 for support of 2013 budgetary appropriations.

Requests for Information

This financial report is designed to provide a general overview of the City’s finances for all those with an interest in the City’s finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to Office of the City Treasurer, City of Tonawanda, 200 Niagara Street, Tonawanda, New York 14150.

BASIC FINANCIAL STATEMENTS

CITY OF TONAWANDA, NEW YORK
Statement of Net Position
December 31, 2012

	Primary Government Governmental Activities
ASSETS	
Cash and cash equivalents	\$ 2,795,794
Restricted cash and cash equivalents	2,868,678
Taxes receivable	1,567,048
Other receivables	534,860
Due from other governments	1,900,246
Prepaid items	576,800
Capital assets not being depreciated	328,850
Capital assets net of accumulated depreciation	20,341,974
Total assets	30,914,250
LIABILITIES	
Accounts payable	1,090,524
Accrued liabilities	630,041
Due to other governments	823,928
Bond anticipation notes	3,440,000
Non-current liabilities:	
Due within one year	3,376,301
Due within more than one year	24,585,875
Total liabilities	33,946,669
NET POSITION	
Net investment in capital assets	10,624,151
Restricted for:	
Tax stabilization	200,000
Workers' compensation insurance	1,114,722
Health insurance	129,654
Capital projects	91,988
Historical restoration	1,000
Unrestricted (deficit)	(15,193,934)
Total net position	\$ (3,032,419)

The notes to the financial statements are an integral part of this statement.

CITY OF TONAWANDA, NEW YORK

Statement of Activities

Year Ended December 31, 2012

Function/Program	Expense	Program Revenues			Net (Expense) Revenue and Changes in Net Position
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Primary Governmental Activities
Primary Government:					
Governmental activities:					
General government support	\$ 2,668,352	\$ 94,583	\$ 13,254	\$ -	\$ (2,560,515)
Public safety	7,825,378	587,990	217,894	1,304,936	(5,714,558)
Transportation	5,156,115	181,774	5,461	429,292	(4,539,588)
Economic assistance and opportunity	32,450	33,824	-	-	1,374
Culture and recreation	1,713,907	104,079	30,694	718,670	(860,464)
Home and community services	5,086,194	2,066,866	27,990	153,660	(2,837,678)
Interest on debt	342,313	-	-	-	(342,313)
Total primary government	<u>\$ 22,824,709</u>	<u>\$ 3,069,116</u>	<u>\$ 295,293</u>	<u>\$ 2,606,558</u>	<u>(16,853,742)</u>
General revenues:					
					10,192,543
					4,830,921
					161,551
					15,386
					48,290
					212,664
					2,602,104
					<u>18,063,459</u>
					1,209,717
					<u>(4,242,136)</u>
					<u>\$ (3,032,419)</u>

The notes to the financial statements are an integral part of this statement.

CITY OF TONAWANDA, NEW YORK

Balance Sheet—Governmental Funds

December 31, 2012

	General	Sewer Fund	Water Fund	Capital Projects	Other Governmental Funds	Total Governmental Funds
ASSETS						
Cash and cash equivalents	\$ 1,624,679	\$ 237,568	\$ 660,352	\$ -	\$ 273,195	\$ 2,795,794
Restricted cash and cash equivalents	1,444,376	-	-	1,423,302	1,000	2,868,678
Taxes receivable	1,567,048	-	-	-	-	1,567,048
Accounts receivables	29,102	435,756	58,153	-	11,849	534,860
Due from other funds	1,164,603	64,220	59,930	1,297,728	-	2,586,481
Due from other governments	1,812,303	-	-	87,943	-	1,900,246
Prepaid expenditures	574,300	2,500	-	-	-	576,800
Total assets	<u>8,216,411</u>	<u>740,044</u>	<u>778,435</u>	<u>2,808,973</u>	<u>286,044</u>	<u>12,829,907</u>
LIABILITIES						
Accounts payable	\$ 205,051	\$ 142,225	\$ -	\$ 743,248	\$ -	\$ 1,090,524
Accrued liabilities	557,609	5,112	-	-	1,892	564,613
Due to other funds	1,304,216	251,220	726,046	304,999	-	2,586,481
Due to other governments	646,971	161,572	-	-	15,385	823,928
Unearned revenue	-	-	-	-	11,849	11,849
Bond anticipation notes	-	-	-	3,440,000	-	3,440,000
Total liabilities	<u>2,713,847</u>	<u>560,129</u>	<u>726,046</u>	<u>4,488,247</u>	<u>29,126</u>	<u>8,517,395</u>
DEFERRED INFLOWS OF RESOURCES						
Unavailable revenue—property taxes	878,712	-	-	-	-	878,712
Total deferred inflows of resources	<u>878,712</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>878,712</u>
FUND BALANCES (DEFICIT)						
Nonspendable	574,300	2,500	-	-	-	576,800
Restricted	1,444,376	-	-	91,988	1,000	1,537,364
Assigned	500,000	177,415	52,389	-	255,918	985,722
Unassigned	2,105,176	-	-	(1,771,262)	-	333,914
Total fund balances (deficit)	<u>4,623,852</u>	<u>179,915</u>	<u>52,389</u>	<u>(1,679,274)</u>	<u>256,918</u>	<u>3,433,800</u>
Total liabilities, deferred inflows of resources and fund balances	<u>\$ 8,216,411</u>	<u>\$ 740,044</u>	<u>\$ 778,435</u>	<u>\$ 2,808,973</u>	<u>\$ 286,044</u>	<u>\$ 12,829,907</u>

The notes to the financial statements are an integral part of this statement.

CITY OF TONAWANDA, NEW YORK
Reconciliation of the Balance Sheet of Governmental Funds
to the Statement of Net Position
December 31, 2012

Amounts reported for governmental activities in the statement of net position (page 11) are different because:

Total fund balances (deficit)—governmental funds (page 13)	\$	3,433,800
Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds. The cost of the assets is \$45,897,805 and the accumulated depreciation is \$25,226,981.		20,670,824
Recognition of certain items which are deferred on the modified accrual basis, but should be recognized on the accrual basis.		
Real property taxes	\$ 878,712	
Loans receivable	<u>11,849</u>	890,561
To recognize interest accrual on long term debt (serial bonds), which are not recognized in the funds until paid.		(65,428)
Long-term liabilities that are not due and payable in the current period and therefore are not reported within the funds:		
Bonds payable	\$ (10,015,000)	
Landfill postclosure care costs	(400,000)	
Pollution remediation obligation	(11,900,000)	
Capital leases	(18,737)	
Other postemployment benefits	(2,021,535)	
Compensated absences	(2,800,212)	
Workers' compensation	<u>(806,692)</u>	<u>(27,962,176)</u>
Total net position—governmental activities	\$	<u>(3,032,419)</u>

The notes to the financial statements are an integral part of this statement.

CITY OF TONAWANDA, NEW YORK

Statement of Revenues, Expenditures and Changes in Fund Balances (Deficits)—Governmental Funds

Year Ended December 31, 2012

	General	Sewer Fund	Water Fund	Capital Projects	Other Governmental Funds	Total Governmental Funds
REVENUES						
Real property taxes	\$ 9,559,242	\$ -	\$ -	\$ -	\$ -	\$ 9,559,242
Other tax items	479,818	-	-	-	-	479,818
Non property tax items	4,830,921	-	-	-	-	4,830,921
Departmental income	194,174	1,843,907	219,523	2,905	30,444	2,290,953
Intergovernmental charges	215,083	-	-	-	-	215,083
Use of money and property	10,187	1,067	-	3,601	531	15,386
Licenses and permits	132,941	-	-	-	-	132,941
Fines and forfeitures	430,139	-	-	-	-	430,139
Sale of property and compensation for loss	48,290	-	-	-	-	48,290
Miscellaneous	189,982	-	-	1,858,924	-	2,048,906
State aid	2,879,186	-	-	341,349	3,660	3,224,195
Federal aid	202,046	-	-	403,023	-	605,069
Total revenues	<u>19,172,009</u>	<u>1,844,974</u>	<u>219,523</u>	<u>2,609,802</u>	<u>34,635</u>	<u>23,880,943</u>
EXPENDITURES						
Current:						
General government support	1,986,226	-	-	3,500	-	1,989,726
Public safety	5,761,284	-	-	244,335	3,331	6,008,950
Transportation	1,928,039	-	-	3,447,084	-	5,375,123
Economic assistance and opportunity	33,256	-	-	-	-	33,256
Culture and recreation	877,482	-	-	1,056,855	23,807	1,958,144
Home and community services	1,145,568	1,079,797	-	1,890,352	16,248	4,131,965
Employee benefits	6,048,389	56,360	-	-	-	6,104,749
Debt service	1,370,133	343,725	257,041	-	-	1,970,899
Total expenditures	<u>19,150,377</u>	<u>1,479,882</u>	<u>257,041</u>	<u>6,642,126</u>	<u>43,386</u>	<u>27,572,812</u>
Excess (deficiency) of revenues over expenditures	<u>21,632</u>	<u>365,092</u>	<u>(37,518)</u>	<u>(4,032,324)</u>	<u>(8,751)</u>	<u>(3,691,869)</u>
OTHER FINANCING SOURCES (USES)						
Transfers in	156,400	-	-	-	-	156,400
Transfers out	-	(156,400)	-	-	-	(156,400)
Proceeds from long-term debt issuance	-	-	-	2,610,000	-	2,610,000
Total other financing sources and uses	<u>156,400</u>	<u>(156,400)</u>	<u>-</u>	<u>2,610,000</u>	<u>-</u>	<u>2,610,000</u>
Net change in fund balances (deficits)	178,032	208,692	(37,518)	(1,422,324)	(8,751)	(1,081,869)
Fund balances (deficits)—beginning	<u>4,445,820</u>	<u>(28,777)</u>	<u>89,907</u>	<u>(256,950)</u>	<u>265,669</u>	<u>4,515,669</u>
Fund balances (deficit)—ending	<u>\$ 4,623,852</u>	<u>\$ 179,915</u>	<u>\$ 52,389</u>	<u>\$ (1,679,274)</u>	<u>\$ 256,918</u>	<u>\$ 3,433,800</u>

The notes to the financial statements are an integral part of this statement.

CITY OF TONAWANDA, NEW YORK
Reconciliation of the Statement of Revenues, Expenditures and Changes in Fund
Balances (Deficits) of Governmental Funds to the Statement of Activities
For the Year Ended December 31, 2012

Amounts reported for governmental activities in the statement of activities (page 12) are different because:

Net change in fund balances (deficit)—total governmental funds (page 15) \$ (1,081,869)

Governmental funds report capital outlays as expenditures. However, in the statement of activities, assets with an initial, individual cost of more than \$5,000 are capitalized and the cost is allocated over their estimated useful lives and reported as depreciation expense. The amount of current year capital and additions and depreciation are as follows:

Capital asset additions	\$ 5,988,125	
Capital asset deletions	(179,693)	
Depreciation expense	(1,414,980)	4,393,452

The issuance of long-term debt (e.g. bonds) provides current financial resources to governmental funds, while the repayment of the principal of long-term debt consumes the current financial resources of governmental funds. Neither transaction, however, has any effect on net position.

Issuance of serial bonds	\$ (2,610,000)	
Repayment of serial bonds	1,633,499	
Decrease in accrued interest expense	(4,913)	
Repayment of capital leases	13,338	(968,076)

In the statement of activities, certain operating expenses (compensated absences, workers' compensation, other postemployment benefits, landfill postclosure care costs and pollution remediation obligations) are measured by the amounts earned during the year. In the governmental funds, however, these amounts are recognized when paid.

Compensated absences	\$ (163,945)	
Workers' compensation	58,979	
Other postemployment benefits	(264,156)	
Landfill postclosure care costs	20,000	
Pollution remediation obligation	(950,000)	(1,299,122)

Revenues in the statement of activities that do not provide current financial resources are reported as deferred inflows in the funds. 165,332

Change in net position of governmental activities \$ 1,209,717

The notes to the financial statements are an integral part of this statement.

CITY OF TONAWANDA, NEW YORK
Statement of Revenues, Expenditures and Changes in Fund Balance
Budget and Actual—General Fund
Year Ended December 31, 2012

	<u>Budgeted Amounts</u>		<u>Actual</u>	<u>Variance</u>
	<u>Original</u>	<u>Final</u>	<u>Amounts</u>	<u>with Final</u> <u>Budget</u>
REVENUES				
Real property taxes	\$ 9,895,996	\$ 9,895,996	\$ 9,559,242	\$ (336,754)
Other tax items	554,000	554,000	479,818	(74,182)
Non property tax items	4,840,000	4,840,000	4,830,921	(9,079)
Departmental income	204,850	207,650	194,174	(13,476)
Intergovernmental charges	196,200	196,200	215,083	18,883
Use of money and property	21,800	21,800	10,187	(11,613)
Licenses and permits	151,000	151,000	132,941	(18,059)
Fines and forfeitures	355,000	355,000	430,139	75,139
Sale of property and compensation for loss	59,000	59,000	48,290	(10,710)
Miscellaneous local sources	29,000	29,000	189,982	160,982
State aid	2,813,204	2,815,543	2,879,186	63,643
Federal aid	-	200,853	202,046	1,193
Total revenues	<u>19,120,050</u>	<u>19,326,042</u>	<u>19,172,009</u>	<u>(154,033)</u>
EXPENDITURES				
Current:				
General government support	2,107,096	1,989,344	1,986,226	3,118
Public safety	5,316,031	5,798,623	5,761,284	37,339
Transportation	2,114,052	2,059,177	1,928,039	131,138
Economic assistance and opportunity	32,856	33,256	33,256	-
Culture and recreation	971,571	921,871	877,482	44,389
Home and community services	1,156,274	1,174,124	1,145,568	28,556
Employee benefits	6,239,171	6,160,956	6,048,389	112,567
Debt service	<u>1,364,399</u>	<u>1,370,199</u>	<u>1,370,133</u>	<u>66</u>
Total expenditures	<u>19,301,450</u>	<u>19,507,550</u>	<u>19,150,377</u>	<u>357,173</u>
Excess (deficiency) of revenues over expenditures	<u>(181,400)</u>	<u>(181,508)</u>	<u>21,632</u>	<u>203,140</u>
OTHER FINANCING SOURCES				
Transfers in	<u>156,400</u>	<u>156,400</u>	<u>156,400</u>	<u>-</u>
Total other financing sources	<u>156,400</u>	<u>156,400</u>	<u>156,400</u>	<u>-</u>
Net change in fund balance*	(25,000)	(25,108)	178,032	203,140
Fund balance—beginning	<u>4,445,820</u>	<u>4,445,820</u>	<u>4,445,820</u>	<u>-</u>
Fund balance—ending	<u>\$ 4,420,820</u>	<u>\$ 4,420,712</u>	<u>\$ 4,623,852</u>	<u>\$ 203,140</u>

*The net change in fund balance was included in the budget as an appropriation (i.e. spenddown) of fund balance.

The notes to the financial statements are an integral part of this statement.

CITY OF TONAWANDA, NEW YORK
Statement of Revenues, Expenditures and Changes in Fund Balance (Deficit)
Budget and Actual—Sewer Fund
Year Ended December 31, 2012

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u>	<u>Variance with Final Budget</u>
	<u>Original</u>	<u>Final</u>		
REVENUES				
Departmental income	\$ 1,852,534	\$ 1,852,534	\$ 1,843,907	\$ (8,627)
Use of money and property	1,000	1,000	1,067	67
Miscellaneous local sources	<u>1,000</u>	<u>1,000</u>	<u>-</u>	<u>(1,000)</u>
Total revenues	<u>1,854,534</u>	<u>1,854,534</u>	<u>1,844,974</u>	<u>(9,560)</u>
EXPENDITURES				
Current:				
Home and community services	1,295,084	1,295,409	1,079,797	215,612
Employee benefits	58,841	58,841	56,360	2,481
Debt service	<u>344,209</u>	<u>343,884</u>	<u>343,725</u>	<u>159</u>
Total expenditures	<u>1,698,134</u>	<u>1,698,134</u>	<u>1,479,882</u>	<u>218,252</u>
Excess (deficiency) of revenues over expenditures	<u>156,400</u>	<u>156,400</u>	<u>365,092</u>	<u>208,692</u>
OTHER FINANCING USES				
Transfers out	<u>(156,400)</u>	<u>(156,400)</u>	<u>(156,400)</u>	<u>-</u>
Total other financing uses	<u>(156,400)</u>	<u>(156,400)</u>	<u>(156,400)</u>	<u>-</u>
Net change in fund balance*	-	-	208,692	208,692
Fund balance (deficit)—beginning	<u>(28,777)</u>	<u>(28,777)</u>	<u>(28,777)</u>	<u>-</u>
Fund balance—ending	<u>\$ (28,777)</u>	<u>\$ (28,777)</u>	<u>\$ 179,915</u>	<u>\$ 208,692</u>

*The net change in fund balance was included in the budget as an appropriation (i.e. spenddown) of fund balance.

The notes to the financial statements are an integral part of this statement.

CITY OF TONAWANDA, NEW YORK
Statement of Revenues, Expenditures and Changes in Fund Balance
Budget and Actual—Water Fund
Year Ended December 31, 2012

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u>	<u>Variance with Final Budget</u>
	<u>Original</u>	<u>Final</u>		
REVENUES				
Departmental income	\$ 257,041	\$ 257,041	\$ 219,523	\$ (37,518)
Total revenues	<u>257,041</u>	<u>257,041</u>	<u>219,523</u>	<u>(37,518)</u>
EXPENDITURES				
Debt service	<u>257,041</u>	<u>257,041</u>	<u>257,041</u>	<u>-</u>
Total expenditures	<u>257,041</u>	<u>257,041</u>	<u>257,041</u>	<u>-</u>
Net change in fund balance*	-	-	(37,518)	(37,518)
Fund balance—beginning	<u>89,907</u>	<u>89,907</u>	<u>89,907</u>	<u>-</u>
Fund balance—ending	<u>\$ 89,907</u>	<u>\$ 89,907</u>	<u>\$ 52,389</u>	<u>\$ (37,518)</u>

*The net change in fund balance was included in the budget as an appropriation (i.e. spenddown) of fund balance.

The notes to the financial statements are an integral part of this statement.

CITY OF TONAWANDA, NEW YORK
Statement of Fiduciary Net Position
Agency Fund
December 31, 2012

	<u>Agency Fund</u>
ASSETS	
Cash and cash equivalents	\$ 406,551
Total assets	<u>\$ 406,551</u>
LIABILITIES	
Agency liabilities	\$ 405,221
Accounts payable	<u>1,330</u>
Total liabilities	<u>\$ 406,551</u>

The notes to the financial statements are an integral part of this statement.

CITY OF TONAWANDA, NEW YORK
Notes to the Financial Statements
Year Ended December 31, 2012

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Departure from Generally Accepted Accounting Principles

The financial statements of the City of Tonawanda, New York (the “City”) have been prepared in conformity with accounting principles generally accepted in the United States of America (“GAAP”) as applied to government units, except that the City’s financial statements do not include the financial activities of the Tonawanda Housing Authority, a component unit of the City. The Governmental Accounting Standards Board (“GASB”) is the accepted standard setting body for establishing governmental accounting and financial reporting principles. The more significant of the City’s accounting policies are described below.

Financial Reporting Entity

The City, which was originally incorporated as a Village in 1854 and was established as a City in 1903, is governed by the charter of the City of Tonawanda, other general laws of the State of New York and various local laws and ordinances. The Common Council, which is the legislative body responsible for the overall operation of the City, consists of a council president and four aldermen. The Mayor serves as Chief Executive Officer and the City Treasurer as Chief Fiscal Officer.

The financial reporting entity includes organizations, functions and activities over which elected officials exercise oversight responsibility. Oversight responsibility is determined on the basis of financial interdependency, selection of governing authority, designation of management, ability to significantly influence operations and accountability for fiscal matters.

Blended component units, although legally separate entities, are, in substance, part of the City’s operations. Discretely presented component units should be reported in a separate column in the government-wide financial statements to emphasize that it is legally separate from the City.

Blended component unit—The Tonawanda Public Library was established by the City and granted a charter by the Board of Regents as provided in Article 5 of the Education Law. The Library’s Trustees are appointed by the Mayor. The City is financially responsible for maintenance of the library building. All other library operations are financed by the County of Erie pursuant to contract. Title to real property used by the library is held by the City. Based upon these factors, the financial activities of the Tonawanda Public Library Fund are reported as a governmental fund (within Other Governmental Funds).

Discretely presented component units—The Tonawanda Housing Authority was created in 1942 pursuant to an act of the New York State Legislature, the creation of which was reaffirmed in 1957 through Public Housing Law, Article 13, Title 9. The members of the Housing Authority Board are appointed by the Mayor. The City is responsible for operating deficits not covered by the subsidy from the State. The Authority’s debt is supported by debt service subsidies received under contract from the state government. The City is liable for the repayment of the loan and interest. Contractual provisions regarding the various housing projects have to be approved by the State Department of Housing and Community Renewal. Based upon these factors, the financial activities of the Tonawanda Housing Authority should be reported as a discrete presentation within the City’s government-wide financial statements. However, the City has elected not to report such financial activities within these financial statements.

Description of Government-Wide Financial Statements

The government-wide financial statements (i.e., the statement of net position and the statement of activities) report information on all of the nonfiduciary activities of the primary government and its component units. All fiduciary activities are reported only in the fund financial statements. *Governmental activities*, which normally are supported by taxes, intergovernmental revenues, and other nonexchange transactions, are reported separately from *business-type activities*, which rely to a significant extent on fees and charges to external customers for support. Likewise, the *primary government* is reported separately from certain legally separate *component units* for which the primary government is financially accountable.

Basis of Presentation—Government-wide Financial Statements

While separate government-wide and fund financial statements are presented, they are interrelated. The governmental activities column incorporates data from governmental funds and internal service funds, while business-type activities incorporate data from the government's enterprise funds. Separate financial statements are provided for governmental funds, proprietary funds, and fiduciary funds, even though the latter are excluded from the government-wide financial statements.

Basis of Presentation—Fund Financial Statements

The fund financial statements provide information about the government's funds, including its fiduciary and blended component unit. Separate statements for each fund category—governmental and fiduciary—are presented. The emphasis of fund financial statements is on major governmental funds, each displayed in a separate column. All remaining governmental funds are aggregated and reported as nonmajor funds. Major individual governmental funds are reported as separate columns in the fund financial statements.

The City considers the following governmental funds as major funds:

- ◆ *General Fund*—is the City's primary operating fund. It accounts for all financial resources of the general government, except those accounted for in another fund.
- ◆ *Sewer Fund*—This fund is used to record all revenues and expenditures related to the transportation and treatment of City sewage.
- ◆ *Water Fund*—This fund is used to record all revenues and expenditures related to operation and maintenance of the City's water system.
- ◆ *Capital Projects Fund*—This fund is used to account for financial resources to be used for the acquisition or construction of major capital facilities.

Additionally, the City reports the following fiduciary fund type that is used to account for assets held by the City in a custodial capacity:

Agency Fund—The Agency Fund is used to account for assets held by the City as an agent for individuals, other governments, or other funds. The Agency Fund is custodial in nature and does not involve measurement of results of operations. The Agency Fund accounts, such as payroll withholdings, are reported as liabilities.

During the course of operations the government has activity between funds for various purposes. Any residual balances outstanding at year end are reported as due from/to other funds and advances to/from other funds. While these balances are reported in fund financial statements, certain eliminations are made in the preparation of the government-wide financial statements.

Further, certain activity occurs during the year involving transfers of resources between funds. In fund financial statements these amounts are reported at gross amounts as transfers in/out. While reported in fund financial statements, certain eliminations are made in the preparation of the government-wide financial statements. Transfers between the funds included in governmental activities are eliminated so that only the net amount is included as transfers in the governmental activities column.

Measurement Focus and Basis of Accounting

The accounting and financial reporting treatment is determined by the applicable measurement focus and basis of accounting. Measurement focus indicates the type of resources being measured such as *current financial resources* or *economic resources*. The basis of accounting indicates the timing of transactions or events for recognition in the financial statements.

The government-wide financial statements are reported using the *economic resources measurement focus* and the *accrual basis of accounting*. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenues in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

The governmental fund financial statements are reported using the *current financial resources measurement focus* and the *modified accrual basis of accounting*. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the City considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, expenditures related to debt service and compensated absences are recorded only when payment is due. General capital asset acquisitions have not been reported as expenditures in governmental funds.

Property taxes, sales taxes, franchise taxes, licenses, and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenues of the current fiscal period. Entitlements are recorded as revenues when all eligibility requirements are met, including any time requirements, and the amount is received during the period or within the availability period for this revenue source (within 60 days of year-end). Expenditure-driven grants are recognized as revenue when the qualifying expenditures have been incurred and all other eligibility requirements have been met, and the amount is received during the period or within the availability period for this revenue source (within 60 days of year-end). All other revenue items are considered to be measurable and available only when cash is received by the government.

Budgets and Budgetary Accounting—Annual budgets for all governmental funds, except the Special Grant Fund, Special Purpose Fund and the Capital Projects Fund, are adopted on a basis consistent with accounting principles generally accepted in the United States of America, except that encumbrances are treated as budgeted expenditures in the year of incurrence of the commitment to purchase. All unencumbered appropriations lapse at the end of the fiscal year. On January 1, encumbrance assignments outstanding at year-end are reappropriated to the ensuing year's original budget. Budgetary comparisons presented in this report are on the budgetary basis and represent the budget as modified.

The Special Grants Fund, Special Purpose Fund and the Capital Projects Fund appropriations are not included in the City's annual budget. Instead, appropriations are approved through a City Council resolution at the grant/project's inception and lapse upon completion/termination of the grant/project.

Encumbrance accounting, under which purchase orders, contracts and other commitments for the expenditure of monies are recorded in order to set aside that portion of the applicable appropriation, is employed as an extension of budgetary control in all governmental funds.

Assets, Liabilities, Deferred Inflows of Resources and Net Position/Fund Balance

Cash, Cash Equivalents and Investments—Cash and cash equivalents include cash on hand, demand deposits, time deposits and short-term, highly liquid investments which are readily convertible to known amounts of cash and have a maturity date within 90 days of the City’s original acquisition. The City had no investments at December 31, 2012, however, when the City does have investments they are recorded at fair value based on quoted market value.

Restricted cash and cash equivalents represent unspent proceeds from serial bonds and bond anticipation notes, amounts set aside for capital projects, and amounts restricted for tax stabilization, workers’ compensation, insurance and historical restoration.

Prepaid Items—Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items in both the government-wide and fund financial statements. The cost of prepaid items is recorded as expenditures/expenses when consumed rather than when purchased.

Capital Assets—Capital assets, which include property, buildings, equipment and infrastructure assets (e.g. roads, bridges, drainage systems and similar items) are reported in the applicable governmental or business-type activities columns in the government-wide financial statements. Capital assets are defined by the City as assets with an initial individual cost of more than the established threshold of \$5,000 and an estimated useful life in excess of two years. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation.

The City has elected to retroactively report all major infrastructure assets regardless of when acquired or constructed.

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend asset lives are not capitalized.

Major outlays for capital assets and improvements are capitalized as projects are incurred.

Property, plant, and equipment of the City are depreciated using the straight line method over the following estimated useful lives:

<u>Assets</u>	<u>Years</u>
Buildings and building improvements	10 - 50
Machinery and equipment	5 - 20
Infrastructure	15 - 50

Deferred Outflows of Resources—In addition to assets, the statement of financial position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, *deferred outflows of resources*, represents a consumption of net position that applies to a future period(s) and so will *not* be recognized as an outflow of resources (expense/expenditure) until then. The government only has one item that qualifies for reporting in this category. It is the deferred charge on refunding reported in the government-wide statement of net position. A deferred charge on refunding results from the difference in the carrying value of refunded debt and its acquisition price. This amount is deferred and amortized over the shorter of the life of the refunded or refunding debt.

Deferred Inflows of Resources—In addition to liabilities, the statement of financial position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, *deferred inflows of resources*, represents an acquisition of net position that applies to a future period(s) and so will *not* be recognized as an inflow of resources (revenue) until that time. The City has only one type of item, which arises only under a modified accrual basis of accounting, that qualifies for reporting in this category. Accordingly, the item, *unavailable revenue*, is reported only in the governmental funds balance sheet. The governmental funds report unavailable revenues from two sources: property taxes and special assessments. These amounts are deferred and recognized as an inflow of resources in the period that the amounts become available.

Net Position Flow Assumptions—Sometimes the government will fund outlays for a particular purpose from both restricted (e.g., restricted bond or grant proceeds) and unrestricted resources. In order to calculate the amounts to report as restricted—net position and unrestricted—net position in the government-wide financial statements, a flow assumption must be made about the order in which the resources are considered to be applied. It is the government’s policy to consider restricted—net position to have been depleted before unrestricted—net position is applied.

Fund Balance Flow Assumptions—Sometimes the government will fund outlays for a particular purpose from both restricted and unrestricted resources (the total of committed, assigned, and unassigned fund balance). In order to calculate the amounts to report as restricted, committed, assigned, and unassigned fund balance in the governmental fund financial statements a flow assumption must be made about the order in which the resources are considered to be applied. It is the government’s policy to consider restricted fund balance to have been depleted before using any of the components of unrestricted fund balance. Further, when the components of unrestricted fund balance can be used for the same purpose, committed fund balance is depleted first, followed by assigned fund balance. Unassigned fund balance is applied last.

Fund Balance Policies—Fund balance of governmental funds is reported in various categories based on the nature of any limitations requiring the use of resources for specific purposes. The City can establish limitations on the use of resources through either a commitment (committed fund balance) or an assignment (assigned fund balance).

The committed fund balance classification includes amounts that can be used only for the specific purposes determined by a formal action of the government’s highest level of decision-making authority. The City Council is the highest level of decision-making authority for the City that can, by adoption of an ordinance prior to the end of the fiscal year, commit fund balance. Once adopted, the limitation imposed by the ordinance remains in place until a similar action is taken (the adoption of another ordinance) to remove or revise the limitation.

Amounts in the assigned fund balance classification are intended to be used by the City for specific purposes but do not meet the criteria to be classified as committed. The City Council has by resolution authorized the City Treasurer to assign fund balance. The City Council may also assign fund balance as it does when appropriating fund balance to cover a gap between estimated revenue and appropriations in the subsequent year’s appropriated budget. Unlike commitments, assignments generally only exist temporarily. In other words, an additional action does not normally have to be taken for the removal of an assignment. Conversely, as discussed above, an additional action is essential to either remove or revise a commitment.

Revenues and Expenditures

Program Revenues—Amounts reported as *program revenues* include 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and 2) grants and contributions (including special assessments) that are restricted to meeting the operational or capital requirements of a particular function or segment. All

taxes, including those dedicated for specific purposes, and other internally dedicated resources are reported as general revenues rather than program revenues.

Property Taxes—The City Treasurer prepares the levy for real property taxes in late December of each year. Unpaid tax levies become deferred inflows of resources as of fiscal year-end.

Compensated Absences—The City labor agreements and City Council rules and regulations provide for sick leave, vacations, and miscellaneous other paid absences. Upon retirement, certain eligible employees qualify for paid hospitalization insurance premiums and/or payment for fractional values of unused sick leave. These payments are budgeted annually without accrual.

Estimated sick leave and compensatory time accumulated by governmental fund type employees are reported as liabilities in the government-wide financial statements.

Payment of sick leave and compensatory time is dependent upon many factors; therefore, timing of future payments is not readily determinable. However, management believes that sufficient resources will be made available for the payments of sick leave and compensatory time when such payment becomes due.

Other

Insurance—The City self-insures for workers' compensation losses up to \$200,000 per incident. The City has obtained outside insurance for claims in excess of that amount. The City also purchases insurance covering liability for most risks including, but not limited to, general liability, vehicle liability and excess. Judgments and claims are recorded when it is probable that an asset has been impaired or a liability has been incurred, the amount of loss can be reasonably estimated and the estimated amount of loss exceeds insurance coverage. General liability insurance is limited to \$1 million per occurrence, and an aggregate \$3 million limit.

Estimates—The preparation of the financial statements, in conformity with GAAP, requires management to make estimates and assumptions that affect the reported amounts of revenues, expenditures, assets, and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and during the reported period. Actual results could differ from those estimates.

Other Postemployment Benefits—In addition to providing pension benefits, the City provides health insurance coverage and survivor benefits for retired employees and their survivors. Substantially all of the City's employees may become eligible for these benefits if they reach normal retirement age while working for the City, as discussed in Note 7.

Adoption of New Accounting Pronouncements—During the year ended December 31, 2012, the City implemented GASB Statements No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*. This statement amends the net asset reporting requirements in GASB Statement No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*, and other pronouncements by incorporating deferred outflows of resources and deferred inflows of resources into the definitions of the required components of the residual measure and by renaming that measure as net position, rather than net assets. The Town also elected to early implement the provisions of GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*. This statement establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources, certain items that were previously reported as assets and liabilities. GASB Statements No. 63 and 65 did not have a material impact on the City's financial position or results from operations.

Additionally, during the year ended December 31, 2012, the City completed the process of evaluating the impact that will result from adopting GASB Statements No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*, No. 60, *Accounting and Financial Reporting for Service Concession Arrangements*; No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*; and No. 64, *Derivative Employer Plans; Instruments: Application of Hedge Accounting Termination Provisions—an amendment of GASB Statement No. 53*. GASB Statements No. 57, 60, 62 and 64 did not have a material impact on the City's financial position or results from operations.

Future Impacts of Accounting Pronouncements—The City has not completed the process of evaluating the impact that will result from adopting GASB Statements No. 61, *The Financial Reporting Entity: Omnibus—an amendment of GASB Statements No. 15 and No. 34*; and No. 66, *Technical Corrections—2012—an amendment of GASB Statements No. 10 and No. 62*, effective for the year ending December 31, 2013; No. 67, *Financial Reporting for Pension Plans—an amendment of GASB Statement No. 25*; and No. 69, *Government Combinations and Disposals of Government Operations*, effective for the year ending December 31, 2014; and No. 68, *Accounting and Financial Reporting for Pensions—an amendment of GASB Statement No. 27*, effective for the year ending December 31, 2015. The City is therefore unable to disclose the impact that adopting GASB Statements No. 61, 66, 67, 68 and 69 will have on its financial position and results of operations.

Stewardship, Compliance and Accountability

Budgets and Budgetary Accounting—The City follows these procedures in establishing the budgetary data reflected in the financial statements:

- ◆ Prior to August 1, all City boards and departments are required to submit budget estimates, including appropriations and estimated revenues, for the following fiscal year to commence on January 1.
- ◆ Following various meetings between the Budget Committee, a public hearing is held to obtain taxpayer comments and discuss revisions.
- ◆ The Common Council then adopts formal budgets for the General, Water and Sewer Funds no later than the third Tuesday of November. All adopted budgets are for the fiscal year beginning the previous January 1.
- ◆ Capital Project funds are subject to project budgets determined primarily by the bonding authorizations used to fund a particular project rather than annual budgetary appropriations, these budgets do not lapse at year end, rather, they lapse upon termination of the project.
- ◆ The annual operating budgets for the Public Library Fund are proposed and adopted by the Board of Trustees of the Erie County Public Libraries.
- ◆ Budgets for the Special Grant Fund are established upon City Common Council acceptance of grants for Community Development activities.
- ◆ During the fiscal year, the Common Council and/or City Treasurer can legally amend the operating budgets and is empowered to implement supplemental appropriations. Budget amendments are required for departmental budgetary control.

Property Taxes—Real property taxes are collected by the City Treasurer. Taxes are levied annually on April 1 for the fiscal year beginning the previous January 1. City taxes are payable without penalty until May 1. Thereafter, a 1% penalty is charged for each month that the taxes are overdue.

All City property taxes are the enforcement responsibility of the City. County and school taxes are also collected by the City. A settlement of collected County taxes is made on May 1 with the County Commissioner of Finance and enforcement of subsequent collections is the responsibility of the County. The City purchases unpaid school taxes after they have been outstanding for three years and then assumes responsibility for their collection. The City enforces all tax liens.

The City recognizes revenues in the fund financial statements only to the extent that they have been collected, or are expected to be collected, within 60 days of the year end.

Deficit Fund Equity—The Capital Projects Fund had a deficit fund balance of \$1,679,274 at December 31, 2012. This deficit is temporary in nature and expected to be remedied when the City converts its short-term financing into long-term bonds.

2. CASH AND CASH EQUIVALENTS

The City’s investment policies are governed by state statutes. City monies must be deposited in FDIC-insured commercial banks or trust companies located within the state. In addition, the City has its own written investment policy. The Treasurer is authorized to use demand accounts and certificates of deposit. Permissible investments include obligations of the U.S. treasury and U.S. agencies, repurchase agreements and obligations of New York State or its localities. Investments with original maturities not exceeding 90 days are considered to be cash equivalents.

Collateral is required for demand deposits and certificates of deposit at 100 percent of all deposits not covered by federal deposit insurance. Obligations that may be pledged as collateral are obligations of the United States and its agencies and obligations of the state and its municipalities and school districts.

Total cash and cash equivalents reported by the City at December 31, 2012 are as follows:

Governmental funds	\$ 5,664,472
Fiduciary fund	<u>406,551</u>
Total	<u>\$ 6,071,023</u>

Cash and cash equivalents consisted of:

Deposits	\$ 6,069,573
Petty cash (uncollateralized, uninsured)	<u>1,450</u>
Total	<u>\$ 6,071,023</u>

Deposits—All deposits are carried at cost which approximates market.

	Bank Balance	Carrying Amount
Insured (FDIC)	\$ 929,768	\$ 929,768
Uninsured but collateralized - collateral held by bank’s trust department in City’s name	<u>5,430,769</u>	<u>5,139,805</u>
Total deposits	<u>\$ 6,360,537</u>	<u>\$ 6,069,573</u>

Custodial Credit Risk—Deposits—Custodial credit risk is the risk that in the event of a bank failure, the City’s deposits may not be returned to it. As noted above, by State statute all deposits in excess of FDIC insurance coverage must be collateralized. As of December 31, 2012, the City’s deposits were FDIC insured or collateralized.

Restricted Cash and Cash Equivalents—The City reports unspent proceeds from debt and amounts to support restricted fund balances as restricted cash and cash equivalents. At December 31, 2012, the City reported \$2,868,678 of restricted cash and cash equivalents within its governmental activities.

Interest rate risk—In accordance with its investment policy, the government manages exposures by limiting investments to low risk type investments governed by New York State Statues.

3. RECEIVABLES

Major revenues accrued by the City funds at December 31, 2012, include:

Accounts receivable—represent city tax receivable, school tax collection fee, canal fest reimbursement, sewer rents, water surcharges and other miscellaneous items. These amounts have been reported as deferred revenues on the balance sheet of the governmental funds and are recognized as revenue when the amounts are both measurable and available.

Due from other governments—represents amounts due from other units of government, such as Federal, New York State, County of Erie or other local governments. Amounts due to the City at December 31, 2012 are presented below:

General Fund:		
Erie County—Sales Tax	\$	1,653,236
NYS 8th Judicial District		109,783
Due from Federal—Fire Grant		38,484
Miscellaneous		10,800
		<u>\$ 1,812,303</u>
Capital Projects Fund:		
Erie County—CDBG Streets	\$	<u>87,943</u>

Rehabilitation loans receivable—Rehabilitation loans receivable at December 31, 2012 consist of the following:

Other Governmental Funds:	
Individual home improvement revolving loans ranging in amount from \$1,724 to \$6,142 with an interest rate of 4% and repayment terms, secured by second mortgages on the individual properties.	\$ 11,849
Total	<u>\$ 11,849</u>

4. CAPITAL ASSETS

Capital asset activity for the City's governmental activities for the year ended December 31, 2012 was as follows:

	Balance 1/1/2012	Additions	Deletions	Balance 12/31/2012
Capital assets, not being depreciated:				
Land	\$ 328,850	\$ -	\$ -	\$ 328,850
Total capital assets, not being depreciated	<u>328,850</u>	<u>-</u>	<u>-</u>	<u>328,850</u>
Capital assets, being depreciated:				
Buildings and building improvements	6,785,617	1,046,379	-	7,831,996
Machinery and equipment	5,961,321	773,285	(179,693)	6,554,913
Infrastructure	27,013,585	4,168,461	-	31,182,046
Total capital assets, being depreciated	<u>39,760,523</u>	<u>5,988,125</u>	<u>(179,693)</u>	<u>45,568,955</u>
Less accumulated depreciation for:				
Buildings and improvements	4,369,370	215,855	-	4,585,225
Machinery and equipment	3,290,228	439,000	(130,162)	3,599,066
Infrastructure	16,152,403	890,287	-	17,042,690
Total accumulated depreciation	<u>23,812,001</u>	<u>1,545,142</u>	<u>(130,162)</u>	<u>25,226,981</u>
Total capital assets, being depreciated, net	<u>15,948,522</u>	<u>4,442,983</u>	<u>(49,531)</u>	<u>20,341,974</u>
Governmental activities capital assets, net	<u>\$ 16,277,372</u>	<u>\$ 4,442,983</u>	<u>\$ (49,531)</u>	<u>\$ 20,670,824</u>

Depreciation expense was charged to the functions of the governmental activities as follows:

Governmental Activities:	
General government support	\$ 41,326
Public safety	207,349
Transportation	914,420
Culture and recreation	134,567
Home and community services	247,480
	<u>\$ 1,545,142</u>

5. ACCRUED LIABILITIES

Accrued liabilities reported by governmental funds of the City as of December 31, 2012, were as follows:

	General Fund	Sewer Fund	Nonmajor Funds	Total Governmental Funds
Salary and employee benefits	\$ 295,523	\$ 5,112	\$ -	\$ 300,635
Incurred but not reported claims	262,086	-	-	262,086
Other liabilities	-	-	1,892	1,892
Total	<u>\$ 557,609</u>	<u>\$ 5,112</u>	<u>\$ 1,892</u>	<u>\$ 564,613</u>

6. PENSION PLANS

Plan Description—The City participates in the New York and Local Employees’ Retirement System (“ERS”), the New York State and local Police and Fire Retirement System (“PFRS”) and the Public Employees’ Group Life Insurance Plan (“Systems”). These are cost-sharing multiple-employer retirement systems. The Systems provide retirement benefits as well as death and disability benefits. Obligations of employers and employees to contribute and benefits to employees are governed by the New York State Retirement and Social Security Law (“NYSRSSL”). As set forth in the NYSRSSL, the Comptroller of the State of New York (“Comptroller”) serves as sole trustee and administrative head of the Systems. The Comptroller shall adopt and may amend rules and regulations for the administration and transaction of the business of the Systems and for custody and control of their funds. The Systems issue a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to the New York State and Local Retirement Systems, 110 State Street, Albany, NY 12244.

Funding Policy—The Systems are noncontributory except for employees who joined the New York State and Local Employees’ Retirement System after July 27, 1976 who contribute 3% of their salary for the first ten years of membership, and employees who joined on or after January 10, 2010 who generally contribute 3% of their salary for their entire length of service. Those joining after April 1, 2012 (Tier 6) are required to contribute three and one-half percent (3.5%) of their annual salary until March 31, 2013, after which the contribution percentage will be based on salary. Under the authority of the NYSRSSL, the Comptroller annually certifies the actuarially determined rates expressly used in computing the employers’ contributions based on salaries paid during the New York State Local Retirement Systems fiscal year ending March 31.

The City of Tonawanda is required to contribute at an actuarially determined rate. The required contributions for the current year and two preceding years were:

	<u>ERS</u>	<u>PFRS</u>
2012	\$ 558,578	\$ 1,058,041
2011	546,566	945,463
2010	380,931	671,948

Legislation requires participating employers to make payments on a current basis. The City’s contributions made to the Systems were equal to 100 percent of the contributions required for each year, and has not bonded or amortized any of the excess amounts.

7. OTHER POSTEMPLOYMENT BENEFITS

Plan Description—The City pays for a portion of eligible retirees’ health insurance, depending on the type of health plan provided. Eligibility for post-employment benefits depends upon the union group as follows:

Funding Policy—Authorization for the City to pay retiree health insurance premiums was enacted through a union contract, which was ratified by the City’s Common Council. To be eligible employees must have 20 years of continuous full-time service with the City and been hired prior to 2003. Upon retirement, the City pays 100% of the cost of the medical benefits for life. In addition Retirees are eligible to receive prescription drug copayment reimbursements back to \$3 for all prescriptions. Surviving spouses are eligible to receive benefits at the same rate as retirees. Retirees hired in 2003 and later are not eligible to receive City paid medical benefits.

The City’s annual other post-employment benefit (“OPEB”) cost is calculated based on the annual required contribution (“ARC”) of the employer, an amount actuarially determined in accordance with the parameters of GASB Statement No. 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities over a period not to exceed 30 years.

The table below shows the components of the City’s annual OPEB cost for the past two years, the amount actually contributed to the plan, and changes in the net OPEB obligation.

	Governmental Activities	
	2012	2011
Annual required contribution	\$ 2,190,549	\$ 2,190,549
Interest on net OPEB obligation	67,195	67,195
Adjustment to annual required contribution	<u>(61,792)</u>	<u>(61,792)</u>
Annual OPEB cost (expense)	2,195,952	2,195,952
Expected contributions	<u>(1,931,796)</u>	<u>(1,931,796)</u>
Increase in net OPEB obligation	264,156	264,156
Net OPEB obligation—beginning of year	<u>1,757,379</u>	<u>1,493,223</u>
Net OPEB obligation—end of year	<u>\$ 2,021,535</u>	<u>\$ 1,757,379</u>

Funding Status and Fund Progress—The plan was unfunded as of December 31, 2012, and the actuarial accrued liability for benefits for governmental activities was \$47,731,182.

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the health care costs trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress presents multiyear trend information about whether the actuarial value of plan assets, if any, is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

The City's Schedule of Funding Progress is presented below:

Fiscal Year Ended	Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability ("AAL")	Unfunded AAL ("UAAL")	Funded Ratio	Covered Payroll	Ratio of UAAL to Budget Covered Payroll
12/31/2010	1/1/2008	\$ -	\$ 37,331,140	\$ 37,331,140	0.0%	N/A	N/A
12/31/2011	5/1/2012	-	47,731,182	47,731,182	0.0%	N/A	N/A
12/31/2012	5/1/2012	-	47,731,182	47,731,182	0.0%	N/A	N/A

The Schedule of the City's contributions is shown below:

Year Ended December 31,	Annual Required Contribution	Contributions Made	Percentage Contributed
2010	\$ 1,856,852	\$ 1,439,494	77.5%
2011	2,195,952	1,931,796	88.0%
2012	2,195,952	1,931,796	88.0%

Actuarial Methods and Assumptions—Calculations are based on the types of benefits provided under the terms of the substantive plan (the plan as understood by the employer and the plan members) at the time of the valuation and on the pattern of cost sharing between the employee and plan members. Calculations reflect a long-term perspective, so methods and assumptions used include techniques that are designed to reduce short-term volatility.

In the May 1, 2012 actuarial valuation, the Entry Age Normal Method was used. Under this method, each participant's projected benefit is allocated on a level basis over the earnings or service of the participant between entry age and assumed exit ages. The actuarial assumptions included a valuation date and measurement date of May 1, 2012. The expected interest rate, salary scale, and inflation rate was 4.5%, 4.0%, and 3.0%, respectively. The RP-2000 projected to 2010, weighted 50% White Collar, 50% Blue Collar tables were used for mortality rates. The unfunded actuarial accrued liability is being amortized over 30 years, therefore the remaining amortized period at December 31, 2012 was 25 years.

8. LABOR CONTRACTS AND CONTINGENCIES

Labor Relations—City employees are represented by four bargaining units with the remainder covered by Common Council rules and regulations. The City of Tonawanda Employee Association, Uniformed Professional Firefighters and the City of Tonawanda Police Benevolent Association have contracts with the City negotiated through December 31, 2016. The City of Tonawanda Civil Service Employee Association has an unsettled contract and is in negotiations as of December 31, 2012.

Assessments—The City is a defendant in various litigation under Article 7 of the Real Property Tax Law of the State of New York to review tax assessments. While the City vigorously defends assessments, the likelihood of success is on a case-by-case basis, and is dependent upon many factors including market values and appraised amounts. No potential amount or potential range of loss is determinable. However, management believes that the level of such potential loss, if any, would be immaterial and no provisions have been made within the financial statements.

Grants—In the normal course of operations, the City receives grant funds from various Federal and State agencies. These grant programs are subject to audit by agents of the granting authority, the purpose of which is to ensure compliance with conditions precedent to the granting of funds. Any disallowed expenditures resulting from such audits could become a liability of the governmental funds. While the amount of expenditures which may be disallowed cannot be determined at this time, management expects any amounts to be immaterial.

Pollution Remediation Obligations—On December 31, 2009, the City was issued Order on Consent #R9-20090408-23 by the New York State Department of Environmental Conservation (“NYSDEC”) for its violation of Article 17 of the Environmental Conservation Law and its implementing regulations found in Title 8 and 6 of the Official Compilation of the Codes, Rules and Regulations of the State of New York which govern the control and prevention of water pollution. As part of this notice the City conducted and submitted a system-wide Sanitary Sewer System Evaluation Survey (SSES) to reduce wet weather flows and eliminate sanitary sewer overflows in the City of Tonawanda. As of December 31, 2012 the NYSDEC has required that the City commit an estimated \$11,900,000 in capital outlays over the next five-years to remedy the above mentioned sanitary sewer overflows. The City has received notice of a grant award from the County of Erie to offset a portion of this liability beginning in 2013. At December 31, 2012, the award amounted to \$1,855,000.

Other—In addition, the City is involved in litigation arising in the ordinary course of its operations. The City believes that its ultimate liability, if any, in connection with these matters will not have a material effect on the City’s financial condition or results of operations.

9. SHORT-TERM DEBT

The purpose of all of the short-time borrowings was to provide resources for various capital construction or improvement projects. The form of financing used in all cases was bond anticipation notes. The amounts issued for governmental activities are accounted for in the capital projects fund.

State law requires that bond anticipation notes issued for capital purposes be converted to long-term obligations within five years after the original issue date, if not completely repaid. However, bond anticipation notes issued for assessable improvement projects may be renewed for periods equivalent to the maximum life of the permanent financing, provided that stipulated annual reductions of principal are made.

The following is a summary of the City’s short-term debt activity for the year ended December 31, 2012:

<u>Description</u>	<u>Interest Rate</u>	<u>Maturity Date</u>	<u>Balance 1/1/2012</u>	<u>Issued</u>	<u>Paid</u>	<u>Balance 12/31/2012</u>
Bond Anticipation Note	0.90%	6/14/2012	\$ 2,335,000	\$ -	\$ 2,335,000	\$ -
Bond Anticipation Note	0.69%	6/13/2013	-	3,440,000	-	3,440,000
			<u>\$ 2,335,000</u>	<u>\$ 3,440,000</u>	<u>\$ 2,335,000</u>	<u>\$ 3,440,000</u>

10. LONG-TERM OBLIGATIONS

Compensated absences—As explained in Note 1, the City records the value of governmental fund type compensated absences in the government-wide financial statements. The annual budgets of the operating funds provide funding for these benefits as they become payable.

Landfill post-closure care costs—State and federal laws and regulations require the City to perform certain maintenance and monitoring functions in addition to remediation work on the City's landfill site. Both post-closure costs and remediation work are to be paid in the future. The total estimated post-closure care and remediation work cost liability is reported in the City's government-wide financial statements. The \$400,000 reported as the accrued landfill post-closure care liability at December 31, 2012 represents the cumulative amount reported to date based on 100% capacity used. The amount reported is based on what it would cost to perform all post-closure and remediation work in 2012.

Other postemployment benefits—As explained in Note 7, the City provides health insurance coverage for retirees. The City's annual postemployment benefit ("OPEB") cost is calculated based on the annual required contribution of the employer, an amount actuarially determined in accordance with the parameters of GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. The estimated long-term OPEB liability is \$2,021,535 as of December 31, 2012.

Bond transactions—The City may issue bonds in order to acquire land, equipment, construct buildings and improvements and construct or improve infrastructure assets. This enables the cost of these capital assets to be borne by the present and future taxpayers receiving the benefit of the capital assets. The bonds are full faith and credit debt of the City.

Capital leases—The City has entered into lease agreements as lessee for financing the acquisition of certain machinery and equipment. The lease agreements qualify as capital leases for accounting purposes and, therefore, have been recorded at the present value of the future minimum lease payments as of the inception date.

Risk management—The City is exposed to various risks of losses related to injuries to employees. Effective March 1, 1996 the City established a self-insurance program for workers' compensation claims. The City self-insures for losses up to \$200,000 per incident. The City has obtained outside insurance for claims in excess of that amount. The City currently reports all of its risk management activities in its General Fund. Claims expenditures and liabilities are reported when it is probable that a loss has occurred and the amount of that loss can be reasonably estimated. These losses include an estimate of claims that have been incurred but not reported.

Total claims and judgments expenditures of \$424,410 were recorded in the General Fund for the year ended December 31, 2012.

Pollution remediation obligation—The New York State Department of Environmental Conservation issued an Order on Consent during the fiscal year ended December 31, 2009 requiring that the City remedy sanitary sewer overflows determined harmful to the local water system. The total estimated liability, at December 31, 2012, to address the violation is \$11,900,000. This estimated liability is recorded in the City's government-wide financial statements.

10. LONG-TERM OBLIGATIONS (continued)

The following is a summary of changes in long-term debt for the year ended December 31, 2012:

	Balance 1/1/2012	Additions	Deletions	Balance 12/31/2012	Due Within One Year
Compensated absences	\$ 2,636,266	\$ 325,806	\$ 161,859	\$ 2,800,212	\$ 140,011
Accrued landfill post-closure costs	420,000	-	20,000	400,000	20,000
Other postemployment benefits	1,757,379	2,195,952	1,931,796	2,021,535	-
Bonds payable	9,038,499	2,610,000	1,633,499	10,015,000	1,750,000
Capital leases	32,075	-	13,338	18,737	5,845
Workers' compensation	865,671	365,431	424,410	806,692	235,445
Pollution remediation obligations	10,950,000	3,945,000	2,995,000	11,900,000	1,225,000
	<u>\$ 25,699,890</u>	<u>\$ 9,442,189</u>	<u>\$ 7,179,902</u>	<u>\$ 27,962,176</u>	<u>\$ 3,376,301</u>

Bonds payable—The following is a summary of City bond transactions for the year ended December 31, 2012:

Description	Issue Date	Original Issue	Interest Rate (%)	Balance 1/1/2012	Issued 2012	Paid 2012	Balance 12/31/2012
General Fund							
Recreation & Water Line	6/01	\$ 1,620,000	4.375-4.75	\$ 465,000	\$ -	\$ (130,000)	\$ 335,000
Energy Performance	6/01	269,500	4.375-4.75	60,000	-	(20,000)	40,000
Wales Ave Landfill Closure	6/03	2,394,500	4.375-4.75	1,345,000	-	(140,000)	1,205,000
Public Improvement	6/04	1,690,000	4.25-5.0	975,000	-	(75,000)	900,000
Fire Ladder Truck	9/08	685,000	2.86	300,000	-	(150,000)	150,000
Fire Headquarters Roof	6/09	115,000	3.05	85,000	-	(15,000)	70,000
Street Improve. (Refunding)	6/09	1,280,000	2.00-3.25	254,000	-	(200,000)	54,000
Roads & Equipment	6/10	980,000	3.50-4.00	880,000	-	(110,000)	770,000
Various Purpose	6/11	1,728,499	2.40	1,728,499	-	(293,499)	1,435,000
Public Improvement	6/12	710,000	3.69	-	710,000	-	710,000
Total General		<u>11,472,499</u>		<u>6,092,499</u>	<u>710,000</u>	<u>(1,133,499)</u>	<u>5,669,000</u>
Water Fund							
Recon. Water Plan (Refunding)	6/09	1,567,710	2.00-3.25	1,306,000	-	(230,000)	1,076,000
Total Water		<u>1,567,710</u>		<u>1,306,000</u>	<u>-</u>	<u>(230,000)</u>	<u>1,076,000</u>
Sewer Fund							
Pump Station - EFC	2/96	825,000	2.95-5.20	195,000	-	(45,000)	150,000
Sewer Improvement	1/02	1,233,250	1.5-5.0	745,000	-	(60,000)	685,000
Sewer Pump and Improve.	6/09	600,000	3.05	460,000	-	(80,000)	380,000
Sewer Improve. (Refunding)	6/09	52,290	2.00-3.25	30,000	-	(10,000)	20,000
Sewer System Evaluation	6/11	210,000	2.40	210,000	-	(75,000)	135,000
Public Improvement	6/12	1,900,000	3.69	-	1,900,000	-	1,900,000
Total Sewer		<u>4,820,540</u>		<u>1,640,000</u>	<u>1,900,000</u>	<u>(270,000)</u>	<u>3,270,000</u>
Total All Funds		<u>\$17,860,749</u>		<u>\$9,038,499</u>	<u>\$2,610,000</u>	<u>\$ (1,633,499)</u>	<u>\$ 10,015,000</u>

Annual principal and interest requirements to amortize bond debt outstanding as of December 31, 2012 are as follows:

	<u>Bond Principal</u>	<u>Bond Interest</u>	<u>Total</u>
2013	\$ 1,750,000	\$ 362,617	\$ 2,112,617
2014	1,340,000	276,589	1,616,589
2015	1,140,000	236,547	1,376,547
2016	1,020,000	200,808	1,220,808
2017	840,000	169,206	1,009,206
2018-2022	2,535,000	484,462	3,019,462
2023-2027	530,000	217,900	747,900
2028 and thereafter	<u>860,000</u>	<u>176,600</u>	<u>1,036,600</u>
Total	<u>\$ 10,015,000</u>	<u>\$ 2,124,729</u>	<u>\$ 12,139,729</u>

There is a statutory debt limit applicable to cities within New York State. The City is in compliance with this debt limit.

Capital leases—The future minimum lease obligations and the net present value of these minimum lease payments as of December 31, 2012 are as follows:

<u>Fiscal Year Ending December 31,</u>	<u>Governmental Activities</u>
2013	\$ 7,100
2014	7,101
2015	<u>7,107</u>
Total minimum lease payments	21,308
Less: amount representing interest	<u>(2,565)</u>
Present value of minimum lease payments	<u>\$ 18,743</u>

Risk management—At December 31, 2012 the amount of liabilities relating to workers' compensation was \$806,692. This liability is the City's best estimate based on available information. Changes in the reported liability resulted from the following:

	<u>Beginning of Year Liability</u>	<u>Current Year Claims and Changes in Estimates</u>	<u>Claim Payments</u>	<u>Balance at Fiscal Year - End</u>
2012	\$ 865,671	365,431	\$ 424,410	\$ 806,692
2011	850,793	536,845	521,967	865,671

11. NET POSITION AND FUND BALANCE

A. Net Position—The government-wide financial statements utilize a net position presentation. Net position is categorized net investment in capital assets, restricted, and unrestricted.

- **Net investment in capital assets**—This category groups all capital assets, including infrastructure, into one component of net position. Accumulated depreciation and the outstanding balances of debt that are attributable to the acquisition, construction or improvement of these assets reduce the balance in this category.
- **Restricted amounts**—This category presents external restrictions imposed by creditors, grantors, contributors or laws and regulations of other governments and restrictions imposed by law through constitutional provisions or enabling legislation.
- **Unrestricted amounts**—This category represents net investment in assets of the City not restricted for any project or other purpose.

The following presents a reconciliation of net investment in capital assets. The City has excluded bonds for the water system which related to assets transferred to the Erie County Water Authority. Also, the bond relating to the landfill has been excluded from the reconciliation as it relates to post-closure and remediation work which is not included in the City's capital assets.

Capital assets, net of accumulated depreciation		\$ 20,670,824
Less:		
Total outstanding bonds	\$ (10,015,000)	
Total bond anticipation notes	(3,440,000)	
Total outstanding capital leases	(18,737)	
Add: debt issued, which was not used for capital assets included in capital asset inventory and unspent debt proceeds used for capital projects:		
Bonds issued for landfill remediation	1,205,000	
Bonds issued for water system	1,076,000	
Unspent debt proceeds used for capital projects	<u>1,146,064</u>	<u>(10,046,673)</u>
Net investment in capital assets		<u>\$ 10,624,151</u>

B. GASB No. 54—The GASB has issued Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*. This Statement defines the different types of fund balances that a governmental entity must use for financial reporting purposes. GASB 54 requires the fund balance to be properly reported within one of the fund balance categories listed below.

Nonspendable—Amount of assets that cannot be spent in the current period because of their form or because they must be maintained intact. As of December 31, 2012, the City had \$576,800 of prepaid items that were classified as nonspendable funds.

Restricted—Amounts that are subject to externally enforceable legal purpose restrictions imposed by creditors, grantors, contributors, or laws and regulations of other governments; or through constitutional provisions or enabling legislation. As of December 31, 2012, the City had the following restricted funds, as presented on the following page.

	General Fund	Capital Projects Fund	Other Governmental Funds	Total
Tax stabilization reserve	\$ 200,000	\$ -	\$ -	\$ 200,000
Workers' compensation reserve	1,114,722	-	-	1,114,722
Insurance reserve	129,654	-	-	129,654
Capital projects	-	91,988	-	91,988
Historical restoration reserve	-	-	1,000	1,000
Total restricted fund balance	<u>\$ 1,444,376</u>	<u>\$ 91,988</u>	<u>\$ 1,000</u>	<u>\$ 1,537,364</u>

Committed—Amounts that are subject to a purpose constraint imposed by a formal action of the City's highest level of decision-making authority, or by their designated body or official. As of December 31, 2012, the City of Tonawanda Common Council has not committed any fund balance to a specific purpose.

Assigned—Amounts that are subject to a purpose constraint that represents an intended use established by the City's Common Council, or by their designated body or official. The purpose of the assignment must be narrower than the purpose of the general fund, and in funds other than the general fund, assigned fund balance represents the residual amount of fund balance. As of December 31, 2012, the balances below were considered to be assigned.

	General Fund	Sewer Fund	Water Fund	Other Governmental Funds	Total
Assigned for:					
Subsequent years' expenditures	\$ 375,000	\$ -	\$ -	\$ -	\$ 375,000
Self-insurance	125,000	-	-	-	125,000
Specific use	-	177,415	52,389	255,918	485,722
Total assigned fund balance	<u>\$ 500,000</u>	<u>\$ 177,415</u>	<u>\$ 52,389</u>	<u>\$ 255,918</u>	<u>\$ 985,722</u>

Significant encumbrances are amounts encumbered in excess of \$50,000. As of December 31, 2012, the City did not have any encumbrances that were considered to be significant.

Unassigned—Represents the residual classification of the government's General Fund, and could report a surplus or deficit. As of December 31, 2012, the unassigned fund balance was \$337,283, which is the net of the deficit unassigned balance in the Capital Projects Fund of \$1,771,262.

Order of Fund Balance Spending Policy—The City's policy does not address the order of spending fund balance. The default would expend fund balances in the following order: nonspendable fund balances, restricted fund balance, committed fund balance, assigned fund balance, and unassigned fund balance at the end of the fiscal year by adjusting journal entries.

12. INTERFUND RECEIVABLES, PAYABLES AND TRANSFERS

Interfund receivables and payables and interfund transfers as of and for the year ended December 31, 2012 are presented below:

Fund	Interfund			
	Receivables	Payables	Transfers In	Transfers Out
Governmental Funds:				
General Fund	\$ 1,164,603	\$ 1,304,216	\$ 156,400	\$ -
Sewer Fund	64,220	251,220	-	156,400
Water Fund	59,930	726,046	-	-
Capital Projects Fund	1,297,728	304,999	-	-
Total Governmental Funds	<u>\$ 2,586,481</u>	<u>\$ 2,586,481</u>	<u>\$ 156,400</u>	<u>\$ 156,400</u>

The outstanding balances between funds result from payments made on behalf of other funds or temporary advances. All of these balances are expected to be collected/paid within the subsequent year. Transfers made during the year were included in the original budget for operations.

13. SUBSEQUENT EVENTS

Management has evaluated subsequent events through March 20, 2013, which is the date the financial statements are available for issuance, and have determined there are no subsequent events that require disclosure under generally accepted accounting principles.

FEDERAL AWARDS

CITY OF TONAWANDA, NEW YORK
Schedule of Expenditures of Federal Awards
Year Ended December 31, 2012

<u>Federal Grantor/Pass-Through Grantor/Program Title</u>	<u>Federal CFDA Number</u>	<u>Disbursements/ Expenditures</u>
U.S. Department of Agriculture		
Direct Program:		
Urban and Community Forestry Grant	10.675	\$ <u>82,426</u>
Total U.S. Department of Agriculture		<u>82,426</u>
U.S. Department of Housing and Urban Development		
Passed through County of Erie, New York:		
Community Development Block Grant - Entitlement Grants	14.218	<u>320,597</u>
Total U.S. Department of Housing & Urban Development		<u>320,597</u>
U.S. Department of Justice		
Direct Program:		
Bulletproof Vest Program	16.607	<u>2,135</u>
Total U.S. Department of Justice		<u>2,135</u>
U.S. Department of Homeland Security		
Passed through County of Erie, New York:		
Justice Assistance Grant	97.067	22,284
Direct Programs:		
Assistance to Firefighters Grant	97.044	88,601
Port Security Grant	97.116	<u>75,772</u>
Total U.S. Department of Justice		<u>186,657</u>
Total Expenditures of Federal Awards		<u>\$ <u>591,815</u></u>

The notes to this schedule of expenditures of federal awards are an integral part of this schedule.

CITY OF TONAWANDA, NEW YORK
Notes to the Schedule of Expenditures of Federal Awards
Year Ended December 31, 2012

Note 1 — Basis of Presentation

The accompanying schedule of expenditures of federal awards includes the federal grant activity of City of Tonawanda, New York (the "City") and is presented on the GAAP basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments and Non-Profit Organizations*. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of the basic financial statements.

Note 2 — Reconciliation of Federal Assistance to Financial Statements

The schedule of expenditures of federal awards reconciles to the federal aid revenues per the City's financial statements as follows:

Federal aid per the City's schedule of expenditures of federal awards for the year ended December 31, 2012	\$ 591,815
Add: Medicaid reimbursement	<u>13,254</u>
Total expenditures of Federal awards per financial statements	<u><u>\$ 605,069</u></u>

* * * * *

INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

Honorable City Council
City of Tonawanda, New York

We have audited in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities, each major fund, each major fund, and the aggregate remaining fund information of the City of Tonawanda, New York (the "City"), as of and for the year ended December 31, 2012, and the related notes to the financial statements, which collectively comprise the City's basic financial statements, and have issued our report thereon dated March 15, 2013 (which report contains an adverse opinion on the City's discretely presented component unit).

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the City's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control. Accordingly, we do not express an opinion on the effectiveness of the City's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying schedule of findings and questioned costs, we identified certain deficiencies in internal control that we consider to be material weaknesses and significant deficiencies.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiency presented as item 2012-01 to be a material weakness in internal control.

A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with

governance. We consider the deficiencies described in the accompanying schedule of findings and questioned costs as items 2012-02 through 2012-05 to be significant deficiencies.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

The City's Response to Findings

The City's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Responses. The City's responses were not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on them.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

March 20, 2013

**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE
FOR EACH MAJOR PROGRAM AND ON
INTERNAL CONTROL OVER COMPLIANCE IN
ACCORDANCE WITH OMB CIRCULAR A-133**

Honorable City Council
City of Tonawanda, New York

Report on Compliance for Each Major Federal Program

We have audited the City of Tonawanda, New York's (the "City") compliance, with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of City's major federal programs for the year ended December 31, 2012. The City's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the City's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the City's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of the City's compliance.

Opinion on Each Major Federal Program

In our opinion, the City complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended December 31, 2012.

Report on Internal Control Over Compliance

Management of the City is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the City's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the City's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.

Report on Schedule of Expenditures of Federal Awards Required by OMB Circular A-133

We have audited the financial statements of the City as of and for the year ended December 31, 2012, and have issued our report thereon dated March 15, 2013, which contained an adverse opinion on the governmental activities and an unmodified opinion on the primary government. Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of expenditures of federal awards is fairly stated in all material respects in relation to the financial statements as a whole.

March 20, 2013

CITY OF TONAWANDA, NEW YORK
Schedule of Findings and Questioned Costs
Year Ended December 31, 2012

Part I. SUMMARY OF AUDITORS' RESULTS

Financial Statements

Type of auditors' report issued:

Adverse on Discretely Presented
Component Unit, Unmodified on
Governmental Acitivites*

* The independent auditors' report on the financial statements expressed an adverse opinion related to the omission of financial activities of a legally separate component unit.

Internal control over financial reporting:

- | | | | | |
|--|---------------|-----|---------------|---------------|
| 1. Material weakness (es) identified? | <u>✓</u> | Yes | <u> </u> | No |
| 2. Significant deficiency (ies) identified? | <u>✓</u> | Yes | <u> </u> | None reported |
| 3. Noncompliance material to financial statements noted? | <u> </u> | Yes | <u>✓</u> | No |

Federal Awards:

Internal control over major programs:

- | | | | | |
|---|---------------|-----|----------|---------------|
| 4. Material weakness (es) identified? | <u> </u> | Yes | <u>✓</u> | No |
| 5. Significant deficiency (ies) identified? | <u> </u> | Yes | <u>✓</u> | None reported |

Type of auditors' report issued on compliance for major programs:

Unqualified

- | | | | | |
|---|---------------|-----|----------|----|
| 6. Any audit findings disclosed that are required to be reported in accordance with OMB Circular A-133 (section .510(a))? | <u> </u> | Yes | <u>✓</u> | No |
|---|---------------|-----|----------|----|

7. The City's major program was:

Name of Federal Program	CFDA Number
Community Development Block Grant — Entitlement Grants	14.218

- | | |
|---|-------------------------------|
| 8. Dollar threshold used to distinguish between Type A and Type B programs? | \$ <u>300,000</u> |
| 9. Auditee qualified as low-risk auditee? | <u> </u> Yes <u>✓</u> No |

Part II. FINANCIAL STATEMENT FINDINGS SECTION

We consider the significant deficiency presented below to be a material weakness in internal control.

Finding 2012-01 — Financial Activities of Tonawanda Housing Authority

Criteria—GASB Statement No. 14, as amended by GASB Statement No. 39, establishes the standards for defining and reporting on the financial reporting entity. These statements apply to the reporting entity and to the separately issued financial statements of governmental component units. In addition, this Statement should be applied to governmental and nongovernmental component units when they are included in a governmental financial reporting entity.

Condition—The City does not include the financial activities of Tonawanda Housing Authority, a component unit of the City of Tonawanda, New York in the City’s basic financial statements.

Cause—The Tonawanda Housing Authority keeps its accounting records and prepares its financial statements on a basis of accounting as required by the U.S. Department of Housing and Urban Development (“HUD”). This basis differs significantly from generally accepted accounting principles. Therefore, the City has elected to not include the financial activities of the Tonawanda Housing Authority in the City’s basic financial statements.

Effect—The independent auditors’ report is adverse on the discretely presented component unit for such exclusion.

Recommendation—We recommend that the City consider including the Tonawanda Housing Authority in its financial statements.

Management’s Response—The City has determined that it is not efficient to recognize the component unit and that not reporting this component unit does not materially affect the financial statements.

We consider the deficiencies presented below to be significant deficiencies in internal control.

Finding 2012-02 — Segregation of Duties

Criteria—Key cash functions should have a clear segregation of duties between the collection of cash, deposit of cash, posting to the general and accounts receivable ledgers, and the paying of bills.

Condition—We found that the same employee has the ability to collect the cash receipts, prepare the deposit, issue checks, perform bank reconciliations and post journal entries to the system.

Cause—Currently, the assistant treasurer has the ability to collect cash, prepare deposits, post journal entries, reconcile bank statements and issue checks.

Effect—The absence of segregation of duties presents the opportunity for the misappropriation of assets and the potential misstatement of the financial statements.

Recommendation—We recommend that the City develop a more structured policy regarding employee job functions to promote segregation of duties.

Management’s Response—Management has evaluated the feasibility of segregating duties within the Treasurer’s Office. As a result, management does not feel that changes to the current operations are

cohesive with management style or practical under economic circumstances. Segregation of duties will not be expected in future years. Other mitigating controls will be evaluated by management.

Finding 2012-03 — Capital Assets

Criteria—All items presented in the capital assets listing should be capitalized and maintained in accordance with generally accepted accounting principles.

Condition—While reviewing the capital asset listing for the City, we noted that not all items within the listing appeared to be consistent with generally accepted accounting principles. We noted instances where there was negative depreciation and items that are below the City's capitalization threshold.

Cause—The City's capital assets schedule is not compiled and maintained in accordance with generally accepted accounting principles.

Effect—The City risks over/understatement of its capital assets.

Recommendation—We recommend that the City perform a detailed reviewed of its capital assets schedule and identify items that should not be included in the schedule and eliminate these items from its presentation.

Management's Response—Management will review the capital asset listing to identify and resolve any items that are not consistent with generally accepted accounting principles.

Finding 2012-04 — Financial Accounting System

Criteria—For proper segregation of duties, no employees with the ability to post financial data should have administrator rights to the financial software.

Condition—We noted that an employee with the ability to edit financial data currently has administrator rights.

Effect—Employees who have the ability to edit financial data should not have administrator rights to the financial software, as an administrator has the ability to create and delete users.

Cause—Employees within the City have improper administrator rights in the financial accounting system.

Recommendation—Employees who have the ability to edit financial data should not have system administrator rights for proper segregation of duties. We recommend that the City's Information Technology department possess the rights to create and delete users, but should not be given full administrators rights, as this would allow individuals with this department to inappropriately edit financial data.

Management's Response—Management will consider restricting administrator rights to the IT Department to determine the feasibility and practicality of implementing this system.

Finding 2012-05 — Information Technology General Controls

Criteria—The City should have a formal information security policy that addresses computer and financial software access. City employees should have a unique password to log on to the network, as well as a different password for financial accounting software, both of which should expire on a regular basis. Additionally, the City should have a formal written backup policy and disaster recovery plan that address how the City would function in the event of a disaster, natural or otherwise. Finally, the City should periodically perform an information technology risk assessment to mitigate the City’s risk to any information technology threats and address any existing deficiencies.

Condition—Currently, the City does not have a formal information security policy that addresses computer and financial software access. Employees are not required to change passwords after an extent of time, since they do not expire. The City does not have a formal written backup policy or disaster recovery plan that detail what would happen and how the City would function in the event of a disaster. Finally, the City does not perform a formal, periodic information technology risk assessment.

Effect—The absence of a formal information security policy prevents the City from holding employees accountable should they use their computers or laptops for personal business or accessing inappropriate websites. In addition, not having a formal policy regarding financial data increases the risk of misappropriation of this data. The City does not have a formal written backup policy, and although backups are performed, if the employee who performs the backups were to become unavailable for an extended length of time, other employees would not have a written guide to back up the system. A formal written disaster recovery policy is essential in the event of a disaster so that the City will be able to function in the event of this scenario. The absence of formal information technology risk assessments increases the City’s exposure to risk from internal and external information technology risks.

Cause—The City does not have policies or procedures in place regarding information security, passwords, backups, disaster recovery, and formal informational technology risk assessments.

Recommendation—The City should create and implement formal written policies or procedures regarding information security, passwords, backups, disaster recovery, and formal information technology risk assessments.

Management’s Response—Management will consider the feasibility of implementing these policies.

Part III. FEDERAL AWARD FINDINGS AND QUESTIONED COSTS SECTION

No findings noted for the fiscal year ended December 31, 2012.

CITY OF TONAWANDA, NEW YORK
Schedule of Prior Federal Award Findings
Year Ended December 31, 2012 (Follow-up on December 31, 2011 Findings)

Finding 2011-06 — Subrecipient Monitoring

Criteria—In accordance with OMB Circular A-133, the City, as a pass-through entity of the Tonawanda Towers is responsible for award identification, during-the-award monitoring and subrecipient audits.

Condition—We noted, that as of the date of our report date, that the City, as a pass-through entity of Section 8 Moderate Rehabilitation monies, has not performed an audit of its subrecipients for the fiscal year ended December 31, 2011.

Cause—An audit has not been performed.

Effect—The City is non-compliant with requirements of its contract agreement with HUD and the subrecipient compliance requirements dictated by OMB circular A-133.

Recommendation—We recommend that the City performs an audit of its subrecipient as soon as possible and that the City remains up to date with all future audits and monitoring requirements.

Management's Response— During 2011, the U.S. Department of Housing and Urban Development released the City from its oversight responsibility relating to the Tonawanda Towers.

Current Year Follow-Up—As of December 31, 2011, the City is no longer responsible for oversight relating to the Tonawanda Towers.

CITY OF TONAWANDA, NEW YORK
Schedule of Expenditures of New York State Department of Transportation Assistance
Year Ended December 31, 2012

Program Title / Description	NYS Reference Number	Expenditures
Consolidated Highway Improvement Program ("CHIPS")	532056	\$ 333,849
New York State Marchiselli Aid	575757	<u>7,500</u>
 Total New York State Department of Transportation Expenditures		 \$ <u>341,349</u>

See note to the schedule of expenditures of New York State Department of Transportation assistance.

CITY OF TONAWANDA, NEW YORK
Note to Schedule of Expenditures of New York State Department of Transportation Assistance
Year Ended December 31, 2012

1. BASIS OF PRESENTATION

The accompanying schedule of expenditures of New York State Department of Transportation (the "NYSDOT") assistance includes the financial assistance provided by NYSDOT.

The accompanying schedule is presented on the modified accrual basis of accounting.

**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE AND
INTERNAL CONTROL OVER NEW YORK STATE
TRANSPORTATION ASSISTANCE EXPENDED BASED ON AN
AUDIT OF THE FINANCIAL STATEMENTS PERFORMED IN
ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS***

Honorable City Council
City of Tonawanda, New York:

Report on Compliance for New York State Transportation Assistance Programs

We have audited the City of Tonawanda, New York's, (the "City") with the types of compliance requirements described in Draft Part 43 of the New York State Codification of Rules and Regulations (NYCRR) that are applicable to each state transportation assistance program tested for the year ended December 31, 2012. The programs tested are identified in the summary of audit results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with the laws, regulations, contracts and grants applicable to each program tested.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the City's programs based on our audit of the types of compliance requirements referred to above. We conducted our audit in compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and Draft Part 43 of NYCRR. Those standards and Draft Part 43 of NYCRR require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a state transportation assistance programs tested has occurred. An audit includes examining, on a test basis, evidence about City's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each state transportation assistance program. However, our audit does not provide a legal determination on City's compliance.

Opinion on Each State Transportation Assistance Program

In our opinion, the City complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its state transportation assistance programs for the year ended December 31, 2012.

Report on Internal Control Over Compliance

Management of City is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the City's internal control over compliance with requirements that could have a

direct and material effect on state transportation assistance programs tested to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each state transportation assistance program and to test and report on internal control over compliance in accordance with Draft 43 of NYCRR, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the City's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a state transportation assistance program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a state transportation assistance program will not be prevented, or detected and corrected, on a timely basis. *A significant deficiency in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance with a type of compliance requirement of a state transportation assistance program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of the internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in the internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Report on Schedule of State Transportation Assistance Expended

We have audited the financial statements of the City as of and for the year ended December 31, 2012, and have issued our report thereon dated March 15, 2013, which contained an adverse opinion on governmental activities and an unmodified opinion on the primary government. Our audit was conducted for the purpose of forming an opinion on the City's financial statements taken as a whole. The accompanying schedule of state transportation assistance expended is presented for purposes of additional analysis as required by Draft 43 of NYCRR, and is not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of state transportation assistance expended is fairly stated in all material respects in relation to the financial statements as a whole.

Purpose of this Report

This report is intended solely to describe the scope of our testing of compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control over compliance. This report is for the information and use of the City Council, management, the New York State Department of Transportation, the Office of the State Comptroller of the State of New York. Accordingly, this communication is not suitable for any other purpose.

March 20, 2013

CITY OF TONAWANDA, NEW YORK
Schedule of Findings and Questioned Costs of
New York State Department of Transportation Assistance
For the Year Ended December 31, 2012

Part I. SUMMARY OF AUDITORS' RESULTS

New York State Department of Transportation Assistance:

Internal control over major programs:

- | | | | |
|---|-----------|---|--|
| 1. Material weakness(es) identified? | _____ Yes | _____ <input checked="" type="checkbox"/> No | |
| 2. Significant deficiency (ies) identified? | _____ Yes | _____ <input checked="" type="checkbox"/> None Reported | |

Type of auditors' report issued on compliance for programs tested:

Unmodified

- | | | | |
|---|-----------|--|--|
| 3. Any audit findings disclosed that are required to be reported in accordance with Draft Part 43 of NYCRR? | _____ Yes | _____ <input checked="" type="checkbox"/> No | |
| 4. The City's programs tested were: | | | |

Name of Program

Consolidated Highway Improvement Program (CHIPS)

Part II. COMPLIANCE FINDINGS AND QUESTIONED COSTS

No matters are reportable.