



# West Valley Central School District

## Financial Management

### Report of Examination

Period Covered:

July 1, 2009 — June 4, 2013

2013M-178



Thomas P. DiNapoli

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# State of New York Office of the State Comptroller

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

December 2013

Dear School District Officials:

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

Following is a report of our audit of the West Valley Central School District, entitled Financial Management. This audit was conducted pursuant to Article V, Section 1 of the State Constitution and the State Comptroller's authority as set forth in Article 3 of the General Municipal Law.

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

Respectfully submitted,

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

# Introduction

## Background

The West Valley Central School District (District) is located in the Towns of Ashford, East Otto, Ellicottville, Franklinville, Machias and Yorkshire in Cattaraugus County. The District is governed by the Board of Education (Board) which comprises seven elected members. The Board is responsible for the general management and control of the District's financial and educational affairs. The Superintendent of Schools (Superintendent) is the chief executive officer and is responsible, along with other administrative staff, for the District's day-to-day management under the Board's direction.

There is one school in operation within the District with approximately 300 students and 80 employees. The District's expenditures for the 2012-13 fiscal year were approximately \$7.6 million, which were funded primarily with real property taxes and State aid. The current Superintendent and Business Official began working for the District in July and August of 2012, respectively.

## Objective

The objective of our audit was to evaluate the District's financial operations including the use of unexpended surplus funds<sup>1</sup> and reserve funds. Our audit addressed the following related question:

- Does the Board properly manage District finances by preparing accurate, realistic budgets, and properly establish, reasonably fund, and properly use reserve funds?

## Scope and Methodology

We evaluated the Board's management of the District's financial operations for the period July 1, 2009 through June 4, 2013.

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

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<sup>1</sup> The Governmental Accounting Standards Board (GASB) issued Statement 54, which replaces the fund balance classifications of reserved and unreserved with new classifications: nonspendable, restricted, and unrestricted (comprising committed, assigned, and unassigned funds). The requirements of Statement 54 are effective for fiscal years ending June 30, 2011 and beyond. To ease comparability between fiscal years ending before and after the implementation of Statement 54, we will use the term 'unexpended surplus funds' to refer to that portion of fund balance that was classified as unreserved, unappropriated (prior to Statement 54), and is now classified as unrestricted, minus appropriated fund balance, amounts reserved for insurance recovery and tax reduction, and encumbrances included in committed and assigned fund balance (post-Statement 54).

**Comments of  
District Officials and  
Corrective Action**

The results of our audit and recommendations have been discussed with District officials and their comments, which appear in Appendix A, have been considered in preparing this report. Except as specified in Appendix A, District officials generally agreed with our recommendations and indicated they have initiated or planned to initiate corrective action. Appendix B includes our comment on an issue raised in the District's response letter.

The Board has the responsibility to initiate corrective action. Pursuant to Section 35 of the General Municipal Law, Section 2116-a (3)(c) of the Education Law and Section 170.12 of the Regulations of the Commissioner of Education, a written corrective action plan (CAP) that addresses the findings and recommendations in this report must be prepared and provided to our office within 90 days, with a copy forwarded to the Commissioner of Education. To the extent practicable, implementation of the CAP must begin by the end of the next fiscal year. For more information on preparing and filing your CAP, please refer to our brochure, *Responding to an OSC Audit Report*, which you received with the draft audit report. The Board should make this plan available for public review in the District Clerk's office.

# Financial Management

A school district's financial condition is a factor in determining its ability to provide educational services to students. The responsibility for accurate and effective financial planning rests with the Board, the Superintendent, and the Business Official. One of the most important tools for managing a district's financial operations is the budget process. District officials must ensure that budgets are prepared, adopted, and modified in a prudent manner, accurately depicting the district's financial activity while also using available resources to ensure that the tax burden is not greater than necessary. It is essential that officials develop reasonable budgets and manage unexpended surplus funds responsibly and in accordance with statute. Prudent fiscal management also includes maintaining sufficient balances in reserves to address long-term obligations or planned future expenditures. In doing so, district officials should adopt a policy governing the use of reserve funds and ensure that residents are fully informed of all reserve fund activity.

District officials consistently over-estimated expenditures over the past four years by more than \$3.8 million, which resulted in operating surpluses totaling \$1.3 million. Therefore, the majority of the \$2.4 million in Board-appropriated unexpended surplus funds was not needed to fund District operations. Because the amount of unexpended surplus funds that can be legally retained is limited,<sup>2</sup> each year since 2009 District officials transferred money in excess of this limit to various District reserve funds. As a result, reserves totaled more than \$2.1 million as of June 30, 2013. District officials could not demonstrate a planned need for more than \$1.7 million of the reserves. Officials also did not appropriately use the debt reserve fund, which had a balance of more than \$380,000 as of June 30, 2013. Instead, District officials levied real property taxes and paid debt service with general fund appropriations. By routinely using these practices, District officials have withheld significant funds from productive use, levied unnecessarily high taxes, and compromised the transparency of District finances to taxpayers.

## **Budgeting and Unexpended Surplus Funds**

The Board is responsible for preparing and presenting the District budget to the public for voter approval. As part of its budget process, the Board is responsible for estimating expenditures and revenues (e.g., State aid), determining how much unexpended surplus funds will be available at fiscal year-end<sup>3</sup> to balance the budget, and the

<sup>2</sup> Real Property Tax Law limits the amount of unexpended surplus funds that can be legally retained by District officials to no more than 4 percent of the next fiscal year's budget.

<sup>3</sup> Available funds which may be used to fund the ensuing year's appropriations

expected real property tax levy. Accurate estimates help ensure that the real property taxes levied are not greater than necessary.

Estimating unexpended surplus funds is an integral part of the budget process. Fund balance represents resources remaining from prior fiscal years that can be used to lower real property taxes for the ensuing fiscal year. When adopting the budget in May, District officials must estimate the unexpended surplus funds that will be available at the June 30th fiscal year end. However, by August when taxes are levied, officials are in a better position to evaluate the actual amount of unexpended surplus funds available to offset real property taxes and should adjust the budget accordingly. Districts may also establish reserves to restrict a portion of unexpended surplus funds for a specific purpose in compliance with statutory directives. It is the Board’s responsibility to continually monitor the need for all established reserves to ensure that the taxpayers’ best interests are being met.

We compared the District’s budgeted revenues and expenditures with actual results of operations for the last four fiscal years and found that the District has overestimated expenditures by more than \$3.8 million. For example, District officials consistently overestimated certain expenditure groups including employee benefits by \$1.1 million; contractual expenditures<sup>4</sup> by \$957,129, instructional salaries by \$511,868, BOCES costs by \$609,113, supplies and materials by \$275,107 and non-instructional salaries by \$182,669.

<b>Fiscal Year</b>	<b>Budgeted Expenditures</b>	<b>Actual Expenditures</b>	<b>Difference</b>
<b>2009-10</b>	\$8,686,678	\$7,640,110	(\$1,046,568)
<b>2010-11</b>	\$8,707,554	\$7,696,395	(\$1,011,159)
<b>2011-12</b>	\$8,521,156	\$7,691,442	(\$829,714)
<b>2012-13</b>	\$8,609,708	\$7,636,009	(\$973,699)
<b>Totals</b>	<b>\$34,525,096</b>	<b>\$30,663,956</b>	<b>(\$3,861,140)</b>

District officials appropriated unexpended surplus funds to reduce the real property tax levy in each year, which should have resulted in planned operating deficits each year. However, because they consistently overestimated expenditures, the District instead experienced operating surpluses during these years, with actual revenues exceeding actual expenditures by \$1.28 million.

<sup>4</sup> These expenditures were primarily for utilities.

**Table 2: General Fund Operating Results and Unexpended Surplus Funds**

Fiscal Year	2009-10	2010-11	2011-12	2012-13	Total
<b>Actual Revenues</b>	\$8,203,875	\$8,032,042	\$7,815,770	\$7,892,720	\$31,944,407
<b>Actual Expenditures</b>	\$7,640,110	\$7,696,395	\$7,691,442	\$7,636,009	\$30,663,956
<b>Operating Surplus</b>	\$ 563,765	\$ 335,647	\$ 124,328	\$256,711	\$ 1,280,451
<b>Appropriated to the Next Year's Budget</b>	\$565,000	\$619,500	\$619,500	\$619,500	
<b>Ending Unexpended Surplus Funds</b>	<b>\$348,302</b>	<b>\$340,846</b>	<b>\$377,537</b>	<b>\$783,673</b>	

District officials appropriated \$619,500 of unexpended surplus in each of the last three fiscal years. The practice of consistently appropriating unexpended surplus funds not needed to finance operations, in effect, is a reservation of surplus funds that is neither regulated by statute nor subject to the statutory limit for unexpended surplus funds.

Although revenues exceeded expenditures, during this same period the Board still increased the real property tax levy each year from \$2.8 million in 2009-10 to \$3.2 million in 2012-13, a 12 percent increase. In addition, the District's adopted 2013-14 budget includes a real property tax increase of 2 percent more than the amount levied in 2012-13.

As a result of its unrealistic budget practices, the amount of unexpended surplus funds for the 2009-10, 2010-11, and 2011-12 fiscal years would have exceeded the legally allowed limit if District officials did not transfer the surplus funds to various reserves at year-end. For 2012-13, the District's unexpended surplus funds were more than double the legally allowed limit or 9 percent of the ensuing years' appropriations. Therefore, officials cannot assure District taxpayers that their best interests are being served.

## Reserves

Reserve funds may be established by Board action, pursuant to various laws, and are used to provide financing only for specific purposes, such as unemployment insurance and workers' compensation payments. The statutes under which reserves are established determine how they may be funded, expended or discontinued. Generally, school districts are not limited to how much money can be held in reserves. However, it is important that the reserve balances maintained are reasonable. To do otherwise (funding reserves at greater than reasonable levels) essentially results in real property tax levies that are higher than necessary. Further, reserve funds should not be merely a "parking lot" for excess cash or unexpended surplus funds. School districts should balance the desirability of accumulating reserves for future needs with the obligation to make sure taxpayers are not overburdened by these practices.

A governing board that establishes and funds reserves on a regular basis should adopt a written policy that communicates its rationale for establishing the reserve, the reserve's objectives, the optimal or targeted funding levels, and the conditions under which the funds' assets will be used or replenished. Reserve fund transactions should be transparent to the public. Reserves are typically funded from amounts raised through the annual budget process, transfers from unexpended balances of existing appropriations and surplus moneys. Ideally, District officials should include in the annual budget the amounts they anticipate placing in reserve funds instead of routinely funding reserves at year-end from excess unexpended surplus funds.

Making provisions to raise resources for reserve funds explicit in the proposed budget gives voters the opportunity to access the Board's plan for funding reserves, which increases transparency. Additionally, a Board resolution is generally necessary to authorize reserve fund transfers when appropriations for transfers to reserves are not anticipated in the annual budget. Such resolutions should include specific details about the amount to be transferred and the reserve to be funded to help further promote transparency.

The District's six reserves totaled \$2.1 million as of June 30, 2013, an increase of 15 percent since June 30, 2010. This increase resulted because the Board transferred surplus funds to reserves at the end of each fiscal year except 2012-13. District officials had used this strategy to lower unexpended surplus funds below the statutory limit, which is not an appropriate rationale for adding to reserves.

We analyzed the District's reserves for reasonableness and adherence to statutory requirements and found that the reserve funds were in excess of the amounts needed for authorized purposes and not supported by a plan or other documentation validating the amounts retained. Further, while establishing resolutions were in place for the retirement contribution, tax certiorari, and workers' compensation reserves, these resolutions did not address the rationale for establishing them, the objective for each, the optimal or targeted funding levels, and the condition under which the funds' assets would be used or replenished. Moreover, there were no Board resolutions establishing the unemployment insurance and employee benefit accrued liability reserves.<sup>5</sup>

This lack of planning suggests that District officials maintained these reserve balances to reduce the District's unexpended surplus funds below the legal limit and did not perform any analysis or identify

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<sup>5</sup> If a debt service reserve is statutorily required no board action is necessary to establish it.

future District fiscal needs. District officials were developing such a plan for these reserve funds as of the end of our fieldwork.

Workers' Compensation Reserve – General Municipal Law (GML) authorizes boards to establish this reserve to pay for workers' compensation costs, related medical expenses and self-insurance administrative costs. At the end of any fiscal year, if the money in this reserve exceeds the amount needed to satisfy all existing obligations and pending claims, the Board may transfer the excess amount to certain other reserve funds or apply the excess to the budget appropriations of the next succeeding fiscal year.

As of June 30, 2013, the reserve's balance of \$295,509 was more than necessary. The District incurred average workers' compensation expenditures of approximately \$34,000 over the last four fiscal years. The District paid these costs from general fund appropriations, essentially funded through the annual tax levy, rather than using the funds reserved for this purpose. Based on this cost level, the District's current reserve balance could be used to pay workers' compensation claims for approximately 8.7 years, assuming the appropriation for these future expenditures were consistently budgeted for and funded by the reserve instead of the real property tax levy. In addition, the reserve balance was not supported by a plan or other documentation validating the amounts retained.

Unemployment Insurance Reserve – GML authorizes boards to create this reserve to reimburse the State Unemployment Insurance Fund (SUIF) for payments made to claimants where the school district has elected to use the "benefit reimbursement" method based on actual unemployment claims. At the end of any fiscal year, if the money in this reserve exceeds the amount required to be paid into the SUIF and any additional amounts required to pay all pending claims, the Board may elect to transfer the excess amount to certain other reserve funds or apply this excess to the budget appropriations of the next succeeding fiscal year.

As of June 30, 2013, the reserve had a reported balance of \$153,608, which is larger than necessary. While the District incurred average unemployment insurance costs of approximately \$14,000 since 2009-10, District officials did not use reserve funds to pay these expenditures. Instead officials paid these costs from general fund appropriations, essentially funded through the annual real property tax levy, rather than using the funds reserved for this purpose. Based on this average cost level, the District's current reserve balance would cover unemployment insurance claims for approximately 11 years, assuming the appropriation for these future expenditures were consistently budgeted for and funded by the reserve instead of the real

property tax levy. In addition, the reserve balance was not supported by a plan or other documentation validating the amounts retained.

Retirement Contribution Reserve – GML authorizes the Board to create a retirement contribution reserve to finance retirement contributions payable to the New York State and Local Employees' Retirement System. The District cannot include the cost of financing contributions for employees covered by the New York State Teachers' Retirement System. A portion of the funds in this reserve may be transferred to certain other reserves in accordance with statutory requirements.

As of June 30, 2013, the reserve had a reported balance of \$461,014. While the District has appropriated and used approximately \$30,000 from the reserve for the last two years, officials are still paying the majority of contributions to NYSLRS from general fund appropriations. Based on this usage level, the District's current reserve balance would cover retirement contribution costs for the next 14 years. In addition, the reserve balance was not supported by a plan or other documentation validating the amounts retained.

Tax Certiorari Reserve – Education Law authorizes districts to establish a reserve fund for paying judgments and claims for tax certiorari proceedings. Money held in such a reserve may not exceed the amount which might reasonably be deemed necessary to meet anticipated judgments and claims arising out of such proceedings, and any money not used to pay judgments and claims must be returned to the general fund within four years of the day that they were deposited.

As of June 30, 2013, the tax certiorari reserve had a balance of \$130,514. According to the Business Official, there were no tax certiorari proceedings against the District in the last four or five years and she does not anticipate any proceedings or claims over the next few years. Accordingly, we question why the Board is reserving any balance for this purpose.

Debt Service Reserve – In certain circumstances, moneys must be restricted for debt service. For example, proceeds from the sale of property must be restricted if related debt remains outstanding. In addition, unexpended debt proceeds and related interest earnings must be restricted and used to pay debt service on that debt issue or for related capital expenditures. Districts are not allowed to establish a debt reserve for any other purpose.

As of June 30, 2013, the reserve, properly reported in the debt service fund, had a balance of \$383,587. The Business Official stated that the amount held in the reserve related to bonds issued in the late

1990s and early 2000s, which remain outstanding. Even though the Board-adopted budget included a transfer from the debt service fund of \$65,000 annually, District officials did not make any transfers or pay debt service payments from this reserve. Rather, the budget included the entire amount of annual debt service costs<sup>6</sup> in general fund appropriations and levied taxes to fund all but the \$65,000. Funds held appropriately in the debt service fund must be used to retire the related outstanding debt.

Employee Benefit Accrued Liability Reserve – GML requires that this reserve be used only for the cash payment of accrued and unused sick, vacation and certain other accrued but unused leave time earned by employees, as well as expenses related to the administration of the reserve. To be funded from this reserve, the accrued and non-liquidated benefits must be due and payable to the employee upon separation of service, as authorized by contract or collective bargaining agreement. The Board is responsible for ensuring that the balance in this reserve is appropriate, and the basis of funding is adequately supported by the monetary value of accrued leave time due as cash payments to employees upon separation from service.

Although this reserve had a balance of approximately \$723,700 as of June 30, 2013, District officials provided supporting documentation for only \$505,000. However, this amount included approximately \$502,800 for sick and vacation leave that was accrued by employees who were ineligible for payments or had not met the requirements to receive payments. As a result, this reserve was over-funded by more than \$720,000.

By maintaining excessive and/or unnecessary reserves combined with ongoing budgeting practices that repeatedly generated operating surpluses, the Board and District officials essentially retained significant excess funds. As a result, the District's real property taxes were unnecessarily high and financial transparency to the taxpayers was diminished.

## **Recommendations**

1. The Board and District officials should develop realistic estimates for expenditures and unexpended surplus funds when preparing the annual budget.
2. District officials should include the planned funding and use of all reserves in their annually adopted budget plan to provide increased transparency for the District's voters.
3. District officials should develop and implement comprehensive policies for establishing and using reserve funds that include

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<sup>6</sup> Serial bond debt service costs for 2012-13 were approximately \$773,000.

optimal or targeted funding levels and the conditions under which the funds will be used or replenished.

4. The Board should adopt resolutions identifying specific amounts to be transferred into specific reserve funds, when establishing or funding them.
5. The Board and District officials should review all reserves at least annually to determine if the amounts reserved are necessary, reasonable, and in compliance with statutory requirements.
6. The Board should determine whether the unemployment insurance and employee benefit accrued liability reserves are necessary and if so, should adopt resolutions properly establishing them in accordance with statutory requirements.
7. District officials should develop and implement a plan for using the reserve fund surplus balances identified in this report in a manner that benefits District taxpayers.

## **APPENDIX A**

### **RESPONSE FROM DISTRICT OFFICIALS**

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



# West Valley Central School

5359 School Street, P.O. Box 290  
West Valley, NY 14171

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*Home of the "Wildcats"*

November 15, 2013

Mr. Robert Meller, Chief Examiner  
Office of the State Comptroller  
295 Main Street, Suite 1032  
Buffalo, NY 14203-2510

Dear Mr. Meller,

This letter is in response to the NYS Office of the State Comptroller's Draft Report of Examination for the period July 1, 2009 – June 4, 2013. Please consider this as the District's response to the audit as well as the District's Corrective Action Plan.

Approximately fourteen years ago the District began a downward financial spiral resulting in operating deficits in the amount of \$668,285 over a period of five years. These deficits occurred as a result of reducing the tax levy with fund balance. Once the decision was made to utilize fund balance to reduce the tax levy sufficient revenues were not present, in future years, to support the budget. (If the tax levy is reduced in one specific year the effect of the reduction is cumulative over future years.) In order to rectify the deficits the District had to increase taxes significantly in ensuing years. Double digit tax increases occurred in more than one year. (The District's current tax rate on true value is \$23.83 per thousand. A 1% increase in the tax levy raises approximately \$32,000.) If the same scenario occurred today, coupled with the tax levy limit and a weak economy it is unlikely the District would be able to pass a budget to recoup needed tax revenue. This would put the District in severe fiscal stress. Through the use of conservative budgeting practices the District has chosen to strengthen its overall financial position in recent years by increasing its reserves.

The District's credit rating was recently reviewed by Standard & Poor's. Standard & Poor's affirmed our existing credit rating of A+. As part of their rationale they noted the rating was, in part, a reflection of, "conservative budgeting practices, with consistently positive financial performances and maintenance of strong reserve levels." They also remarked that the District's total fund balance as of June 30, 2012 was rated as strong. Standard & Poor's ratings measure credit quality. Lower ratings create increased risk for investors and result in higher interest rates. If a District experiences a decline in its credit rating, higher interest rates for indebtedness would increase costs for taxpayers at both the state and local level. The Board of Education supports maintaining total reserves at a sufficient level to maintain a strong credit rating.

An Equal Opportunity Employer

The West Valley Central School District is unique as, within its boundaries, located on approximately 3,300 acres, is the West Valley Demonstration Project. The WVDP came about as the result of a Federal initiative started back in 1957 by the U.S. Atomic Energy Commission to privatize the reprocessing of spent nuclear fuel. New York State became involved in this program believing it would promote industrial development within the State. New York State purchased land, in the Town of Ashford, for the facility in approximately 1961. A private firm by the name of Nuclear Fuel Services, Inc. operated the facility and reprocessed spent nuclear fuel until 1976 at which time they, for a variety of reasons, determined that it was not feasible. Today, as governed by the West Valley Demonstration Project Act, passed by Congress in 1980, the Department of Energy, in cooperation with the New York State Energy Research and Development Authority, are decommissioning the facility and constructing storage areas for the reprocessed fuel until such time it can be moved to a permanent storage site. It is likely the transfer of the reprocessed fuel will not happen anytime in the near future.

What makes this pertinent is that the West Valley Community and School District has, for many years, lived with the aftermath of the decision to locate a nuclear reprocessing facility within its boundaries. Not only has the District's tax base been impacted by the nuclear facility's property tax exempt status, the ability to grow the District's tax base is limited due to the stigma attached to a community that houses high level nuclear waste. The District receives a small PILOT payment, each year, from New York State for the nuclear facility in the amount of \$280,046. The amount of the PILOT has remained the same since 1997. There is no guarantee the PILOT payment from New York State will continue, nor do we anticipate increases in the PILOT payment in the near future.

There is much emotion behind what the Town of Ashford and the hamlet of West Valley was promised to have in store for it as a result of being home to the nuclear facility. In the long term the promises have faded away. During the peak years of the facility the plant provided jobs to many members of the community. Although the hamlet has always been small there was a time one could at least purchase a gallon of milk, or gasoline. Today that is not the case as residents must look outside the area for employment and basic amenities. During this time, of which is approaching fifty years, the West Valley Central School District has remained an integral and critical component of this small community. The education received by its students is one thing the community has been and continues to be proud of. However, the question continually looming in the background is, how long will the District be able to provide services to the community in a manner that promotes both the best interest of the students and taxpayers? As of this writing the Board of Education is committed to keeping the District viable for as long as possible in spite of the challenges it faces.

The District takes exception to your reporting approach noted on the top of page seven. The chart which notes that the District has overestimated expenditures by \$3.8 million dollars is technically accurate but also misleading. The District's concern is, to the layperson, it gives the appearance that we have constructed our budget with little thought or proper analysis. Highlighting the total figure of 3.8 million dollars misleads the reader as every fiscal year is a separate accounting cycle and leads up to its own specific financial results for a specific year.

See  
Note 1  
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The District is and will continue to be cognizant of those areas of the budget that are inherently subject to change. For example increased costs for special education students moving into the District, changes in costs for electricity, natural gas, and fuel, and the idea that retirements of staff, and the need to hire additional staff are not always known while the District is in the budget planning process. Our philosophy is to leave enough flexibility in our budget to weather the perfect storm and to meet any financial demand which may arise during a given school year.

As noted by the chart on the bottom of page seven the District's operating surpluses have decreased in recent years. (There is an increase in year 2012-2013 due to unplanned retirements.) Like most school districts in New York State we have felt the pressures of cuts in state aid and the property tax limit. In response to this we have maintained our actual expenditures at levels that are essentially flat. The District has accomplished this during a time where costs for retirement and health insurance have increased significantly. The District is committed to a continual process of looking for efficiencies and financial savings to the extent possible.

The District also takes exception to the last sentence in the Budgeting and Unexpended Surplus Funds section regarding assuring District taxpayers that their best interests are being served. The District is committed to keeping its financial position strong so it will be able to meet challenges brought to it by our unique circumstances, decreased funding from the state, a weak tax base, and declining enrollment. We believe that financial strength provides us the flexibility to meet any number of economic challenges that may arise in the future.

Please consider the following as the District's Corrective Action Plan:

**Recommendation:** The Board and District Officials should develop realistic estimates for expenditures and unexpended surplus funds when preparing the annual budget.

**Action Plan:** The District does develop realistic estimates for expenditures and is aware of the contingencies included within specific budget codes and how it impacts appropriated fund balance while preparing the annual budget. The District also estimates what it believes will be unexpended surplus at the end of a fiscal year while preparing its budget. The District will continue to provide for and include additional amounts in its budget in the event we realize unexpected costs for special education, utilities, health insurance, etc. The District has no control over unexpended budget amounts due to unexpected retirements. The District will work toward adjusting its budgeted expenditures and appropriated balance downward, but will be very conservative in its approach to doing so. This process will begin while planning the 2014-2015 budget. The Board of Education, Superintendent, and Business Official will be responsible for implementation of this plan.

**Recommendation:** District officials should include the planned funding and use of all reserves in their annually adopted budget plan to provide increased transparency for the District's voters.

**Action Plan:** The District includes use of reserves to support its budget into budget documents provided to the public. The District will continue to do so in future budget cycles. The District will discuss during its future public budget meetings how much surplus it expects to have at the end of year, as well as the amount of surplus it expects to have in the following budget year. The District will take a conservative approach to its estimates. The Board of Education, Superintendent, and Business Official will be responsible for implementation of this plan.

**Recommendation:** District officials should develop and implement comprehensive policies for establishing and using reserve funds that include optimal or targeted funding levels and the conditions under which the funds will be used or replenished.

**Action Plan:** District officials have drafted a Reserve Plan and will be working on finalizing the plan during the current school year. Within this document the District will work towards developing a system to monitor, use, and replenish its reserves.

**Recommendation:** The Board should adopt specific resolutions identifying specific amounts to be transferred into specific reserve funds, when establishing or funding them.

**Action Plan:** The Board of Education will pass resolutions each year identifying specific amounts to be transferred into reserve funds beginning with the fiscal year ending June 30, 2014. The Board of Education, Superintendent, and Business Official will be responsible for implementation of this plan.

**Recommendation:** The Board and District officials should review all reserves at least annually to determine if the amounts reserved are necessary, reasonable, and in compliance with statutory requirements.

**Action Plan:** The Board and District officials are in the process of finalizing a Reserve Plan. It is estimated that the Reserve Plan will be finalized prior to the end of the current fiscal year. The Board and District officials will, each year, through an update of its Reserve Plan review all reserves. The Board of Education, Superintendent, and Business Official will be responsible for implementation of this action plan.

**Recommendation:** The Board should determine whether the unemployment insurance and employee benefit accrued liability reserves are necessary and if so, should adopt resolutions properly establishing them in accordance with statutory requirements.

**Action Plan:** The Board of Education, at its June 25, 2013, adopted a resolution establishing the Employee Benefit Accrued Liability Reserve and the Unemployment Insurance Reserve. The Board will establish a rationale for these reserves in its Reserve Plan Document. It is estimated that the Reserve Plan will be finalized prior to the end of the current fiscal year. The Board of Education, Superintendent, and Business Official will be responsible for implementation of this action plan.

**Recommendation:** District officials should develop and implement a plan for using the reserve fund surplus balances identified in this report in a manner that benefits District taxpayers.

**Action Plan:** District officials have developed a plan to utilize the unassigned fund balance, in excess of 4%, to fund the local share of a small capital project. The District is proposing repairs to a compromised roof, as well as other infrastructure needs. The District anticipates a vote on this project in February 2014. At that time the District will ask the taxpayers to approve the transfer of the amount in excess of 4% to the capital project fund to cover the local share. The District also will be asking the taxpayers to approve the creation of a Capital Reserve Fund. The timing of the vote to do so is currently under discussion. The Board of Education, Superintendent, and Business Official will be responsible for implementation of this action plan.

In closing we would like to say that we appreciate the high level of professionalism that was represented by your office during the audit. The District respects and appreciates the responsibilities of the New York State Comptroller's office as well as the comments made in your report. In an era that is fraught with abuse and irresponsible behaviors by both individuals in government and the private sector the need to have checks and balances is critical. Constructive and meaningful assistance has been and always will be appreciated by our District. The District asks you to keep in mind that not every situation in local government fits into the same equation. We are all unique with varying history and uncertain futures.

Respectfully submitted,

Eric J. Lawton  
Superintendent of Schools

Michael Frascella  
President, Board of Education

## APPENDIX B

### OSC COMMENT ON THE DISTRICT'S RESPONSE

#### Note 1

Table 1 on page 6 of our report (page 7 in the draft report) was included to show the major cause of the annual operating surpluses. Each year District officials used a portion of the cumulative surplus toward the ensuing year's budget, which would lower the real property tax levy. If the surplus was actually used during the ensuing year, an operating deficit, rather than a surplus, would have resulted and the District's unexpended surplus would have been reduced. We understand that the District does not want to repeat past practices by depleting the unexpended surplus. However, District officials should develop realistic expenditure estimates and utilize unexpended surplus funds in a manner that best serves the District and its taxpayers when preparing the annual budget.

## APPENDIX C

### AUDIT METHODOLOGY AND STANDARDS

Our overall goal was to assess the adequacy of the internal controls put in place by officials to safeguard District assets. To accomplish this, we performed an initial assessment of the internal controls so that we could design our audit to focus on those areas most at risk. Our initial assessment included evaluations of the following areas: financial condition, cash receipts and disbursements, payroll, cafeteria operations, transportation and information technology. During our initial assessment, we interviewed appropriate District officials, performed limited tests of transactions and reviewed pertinent documents such as District policies, Board minutes and financial records and reports.

After reviewing the information gathered during our initial assessment, we determined where weaknesses existed, and evaluated those weaknesses for the risk of potential fraud, theft and/or professional misconduct. We then decided upon the reported objective and scope by selecting for audit those areas most at risk. We selected unexpended surplus funds and reserve funds for further audit testing. To accomplish our objective and obtain relevant audit evidence, we performed the following procedures:

- We interviewed District officials to gain an understanding of the processes and procedures in place over the District's financial management.
- We reviewed ST-3 reports as submitted to the Office of the State Comptroller to document unexpended surplus funds, reserve funds, revenues and expenditures. We also compared the amounts reported in the District's externally audited financial statements with bank statements, general ledgers, journals and other source documents to verify reliability.
- We reviewed the real property tax warrants, receipts and levy increases.
- We compared unexpended surplus funds to the ensuing year's appropriations to determine if the District was within the statutory limit.
- We reviewed Board minutes, resolutions and other documentation to determine that reserve funds were created, funded and expended properly; liabilities were properly recorded and transfers to the debt service fund were appropriate.
- We performed budget-to-actual comparisons of revenues and expenditures to determine if there were operating surpluses or deficits and whether the budgets were realistic and supported.

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

## APPENDIX D

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