



Frankfort-Schuyler Central School District Financial Management

Report of Examination

Period Covered:

July 1, 2014 – April 12, 2016

2016M-226



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

September 2016

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 district operations and Board of Education governance. Audits also can identify strategies to reduce district costs and to strengthen controls intended to safeguard district assets.

Following is a report of our audit of the Frankfort-Schuyler 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 New York State 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 Frankfort-Schuyler Central School District (District) is located in the Towns of Frankfort and Schuyler in Herkimer County. The District is governed by the Board of Education (Board), which is composed of 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 District's chief executive officer and is responsible, along with other administrative staff, for the District's day-to-day management under the Board's direction. The Business Administrator is mainly responsible for managing the District's finances, maintaining the accounting records and preparing reports.

The District operates two schools with approximately 985 students and 125 employees. The District's budgeted appropriations for the 2016-17 fiscal year are \$19.2 million, which are funded primarily with State aid and real property taxes.

Objective

The objective of our audit was to examine the District's financial management practices. Our audit addressed the following related question:

- Did the Board and District officials adequately manage the District's financial condition?

Scope and Methodology

We examined the District's financial management practices for the period July 1, 2014 through April 12, 2016. We expanded our scope period back to the 2011-12 fiscal year to analyze financial trends.

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

Comments of 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. District officials generally agreed with our recommendations and indicated they planned to take corrective action.

The Board has the responsibility to initiate corrective action. Pursuant to Section 35 of General Municipal Law, Section 2116-a (3)(c) of New York State 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 the CAP available for public review in the District Clerk's office.

Financial Management

The Board, Superintendent and Business Administrator are responsible for making sound financial decisions in the best interest of the District, the students they serve and District residents. The Board is responsible for adopting budgets that contain estimates of actual and necessary expenditures that are funded by planned realistic revenues. Fund balance represents resources remaining from prior fiscal years. New York State Real Property Tax Law limits the amount of fund balance a District may retain to no more than 4 percent of the subsequent year's budget. Additionally, Districts are legally allowed to establish reserve funds and accumulate funds for certain future purposes (e.g., capital projects, retirement expenditures). It is also important for the Board to adopt written policies governing reserve funds and for District officials to develop a comprehensive multiyear financial plan to estimate the future costs of ongoing services and capital needs.

The Board and District officials did not effectively manage the District's financial condition. District officials did not adopt budgets based on historical or known trends but instead overestimated expenditures by almost \$2.7 million over the last four fiscal years (2011-12 through 2014-15). The District appropriated \$2.4 million in fund balance as a financing source in the annual budgets for 2012-13 through 2015-16. However, the District's budgeting practices resulted in operating surpluses in three of these years, and we project the District will also likely end 2015-16 with an operating surplus. As a result, none of the appropriated fund balance will be needed to finance operations.

The District also retained an average of approximately \$342,000 of unrestricted funds in the debt service fund, \$1.1 million in the agency fund's group health insurance account and \$429,000 in excessive reserves. When adding back unused appropriated fund balance and excess money retained in the debt service, agency funds and reserves, the District's recalculated unrestricted fund balance exceeded the statutory limit, averaging more than 18 percent of the ensuing year's appropriations, or more than four times the statutory limit. From 2011-12 through 2015-16, District officials increased the tax levy by approximately 7 percent. As a result of these practices, District officials levied real property taxes that were higher than necessary to fund District operations.

Additionally, the Board did not adopt a written reserve fund policy or develop a multiyear financial plan, which would allow District

Budgeting and Fund Balance

officials to identify developing revenue and expenditure trends, set long-term priorities and goals, avoid large fluctuations in tax rates and more effectively manage the use of unrestricted fund balance.

The Board and District management are responsible for accurately estimating revenues and appropriations in the District's annual budget. Accurate budget estimates help ensure that the real property tax levy is not greater than necessary. The estimation of fund balance is also an integral part of the budget process.

We compared the District's appropriations with actual results of operations for 2011-12 through 2014-15 and found that District officials overestimated appropriations by almost \$2.7 million over these years. Of this amount, \$1.2 million occurred in fiscal year 2014-15 due largely from overestimating heating gas, electricity and materials and supplies costs by a combined total of \$652,378. Actual revenues were generally consistent with budgeted estimates over the same period.

District officials told us that they overbudgeted appropriations to provide a cushion for unexpected expenditures and because they did not know how much State aid would be received from year-to-year. District officials informed us that they also planned for increases in energy rates and usage; however, mild winter conditions and steady provider rates for the 2014-15 fiscal year resulted in significantly lower energy costs. While it is prudent to have some provision for unanticipated expenditures, it can be done by maintaining ample fund balance, using reserves or adopting a conservative budget. Doing all three of these as fund balance and reserves are growing results in the tax levy being higher than necessary.

A district may retain a portion of fund balance at the end of the fiscal year for cash flow needs or unexpected expenditures. However, a district must use any unrestricted fund balance above the statutory limit to reduce its real property tax levy. Districts may also establish reserve funds to set aside reasonable portions of fund balance for specified purposes in compliance with statutory directives.

From 2011-12 through 2014-15, the District's unrestricted fund balance exceeded the statutory limit with fund balance levels ranging between 4.3 and 5.1 percent of the next year's budget. In addition, District officials appropriated fund balance that was not used to fund operations and retained unrestricted fund balance in certain restricted funds that made the District's unrestricted fund balance appear to be less than it actually was.

Figure 1: Unrestricted Fund Balance at Year-End				
	2011-12	2012-13	2013-14	2014-15
Total Beginning Fund Balance	\$3,397,778	\$2,475,433	\$2,621,213	\$2,667,823
Add: Operating Surplus/(Deficit)	(\$921,977)	\$145,780	\$62,588	\$829,063
Prior Period Adjustments	(\$368)	\$0	(\$15,978)	\$0
Total Ending Fund Balance	\$2,475,433	\$2,621,213	\$2,667,823	\$3,496,886
Less: Restricted Fund Balance	\$1,087,063	\$1,129,900	\$1,182,593	\$1,592,303
Less: Encumbrances	\$17,888	\$106,113	\$96,987	\$358,285
Less: Appropriated Fund Balance for the Ensuing Year	\$600,000	\$600,000	\$600,000	\$600,000
Total Unrestricted Fund Balance at Year-End	\$770,482	\$785,200	\$788,243	\$946,298
Ensuing Year's Budgeted Appropriations	\$17,369,455	\$17,657,224	\$18,355,071	\$18,727,743
Unrestricted Fund Balance as Percentage of Ensuing Year's Budget	4.4%	4.4%	4.3%	5.1%

From 2011-12 through 2014-15, District officials appropriated \$600,000 in fund balance as a financing source in each of the annual budgets even though the District experienced operating surpluses for three of these years. We project that the District will also end 2015-16 with an operating surplus. As a result, the District did not use, nor do we anticipate it will use, any of the \$2.4 million in appropriated fund balance to fund operations.

Debt Service Fund – This fund is used to account for and report the accumulation of resources that are set aside for paying principal and interest on long-term debt. For example, a debt service fund must be established and maintained to account for the proceeds of a sale of a capital asset with outstanding debt or if State or federal aid is received for a capital improvement for which there is outstanding debt. These funds should be used for the related debt service payments.

The District maintained a debt service fund with a balance of \$738,477 as of June 30, 2015, which includes the sale of a building in April 2015 for \$393,545 for which it still owes debt. The remaining non-sale balance of \$344,392 would be available to pay debt payments. The debt service fund retained an average balance of \$342,000 over the past four fiscal years (2011-12 through 2014-15). However, District officials pay the debt-related principal and interest from general fund appropriations each year instead of using this fund for its intended purpose. Debt payments averaged \$2 million from 2011-12 through 2015-16. Using debt service money for its intended purpose could allow general fund resources to be used for other purposes, including the reduction of real property taxes.

Agency Fund – This fund is used to account for District funds held purely in a custodial capacity. District officials hold such funds as an agent for individuals, private organizations or other governments. As part of its agency fund, the District maintained a group health insurance account for employee and retiree health insurance contributions. These funds are generally held in the agency fund and later transferred to the general fund to pay health insurance bills.

As of June 30, 2015, the District had a total of \$1.2 million in the agency fund’s group health insurance account. Further, significant amounts have been retained in this account over the past five years. During 2014-15, District officials did not transfer the entire amount of health insurance contributions received from employees and retirees to the general fund to pay for health insurance related expenditures. Although employee and retiree contributions totaled \$324,525, District officials made a lump sum transfer to the general fund totaling \$315,000, while retaining the difference of \$9,525 in this account.

When we asked District officials about the balance in this account, they explained that the \$1.2 million balance included \$600,000 set aside in case they wanted to leave their health insurance consortium, with the remainder set aside for upcoming capital projects. This is not an appropriate use for the group health insurance money held in the agency fund. Since the funds are not being held in a custodial capacity and were not properly restricted as reserve funds, they are uncommitted surplus fund balance.

Although the District appropriated fund balance and retained unrestricted funds in its debt service, agency funds and excess reserves, its unrestricted fund balance still exceeded the statutory limit each year. When these amounts are added back, the District’s recalculated unrestricted fund balance further exceeds the statutory limit each year, averaging more than 18 percent of the ensuing year’s appropriations, or more than four times the statutory limit.

Figure 2: Unused Fund Balance				
	2011-12	2012-13	2013-14	2014-15
Total Unrestricted Funds at Year-End	\$770,482	\$785,200	\$788,243	\$946,298
Add: Appropriated Fund Balance Not Used to Fund Ensuing Year's Budget	\$600,000	\$600,000	\$600,000	\$600,000 ^a
Add: Agency Fund Balance	\$952,710	\$1,257,616	\$1,200,254	\$1,208,169
Add: Debt Service Balance	\$338,884	\$339,598	\$344,490	\$344,932
Add: Excess Reserve Funds ^b	\$222,871	\$347,871	\$422,871	\$722,871
Total Recalculated Unrestricted Funds	\$2,884,947	\$3,330,285	\$3,355,858	\$3,822,270
Ensuing Year's Budgeted Appropriations	\$17,369,455	\$17,657,224	\$18,355,071	\$18,727,743
Recalculated Unrestricted Funds as Percentage of Ensuing Year's Budget	16.6%	18.9%	18.3%	20.4%
^a We projected the anticipated amount of unused appropriated fund balance based on prior year trends. ^b This includes the reserve balances for unemployment insurance and repair reserves.				

As a result of the District's budgeting practices, it appeared the District needed to both raise taxes and use fund balance to close projected budget gaps. However, the District's budgets resulted in operating surpluses in three of these years. Despite having excessive unrestricted fund balance, District officials increased the tax levy 7 percent, from \$6.7 million in 2011-12 to \$7.2 million in 2015-16. We reviewed the District's 2015-16 budget and determined that the District budgeted similarly as in previous years. Therefore, it is likely that the District will have an operating surplus and not need to use the \$600,000 in appropriated fund balance.

By not using appropriated funds; maintaining excessive money in the debt service, agency and reserve funds; and using budgeting practices that generate operating surpluses, the Board and District officials have withheld significant funds from productive use and levied property taxes that were higher than necessary. These practices decrease the transparency of District finances to residents.

Reserve Funds

Reserve funds may be established by Board action, pursuant to various laws, and can be used to provide financing for specific purposes. Generally, districts are not limited as to how much money can be held in reserves unless the Board has established such a limitation. However, it is important that districts maintain reserve balances that are reasonable. Reserve balances above reasonable amounts represent funds a district could have used for other purposes, including reducing tax increases. It is important that the Board adopts a written policy that clearly states its rationale for establishing reserve funds, objectives for each reserve established, optimal or targeted funding

levels and conditions under which each fund's assets will be used or replenished.

The District maintained six reserve funds with balances totaling nearly \$1.6 million at the end of 2014-15 (employee benefit accrued liability – \$621,998, repair – \$500,000, unemployment insurance – \$222,871, retirement contributions – \$150,000, tax certiorari – \$64,434 and insurance – \$33,000). The Board did not ensure the repair and unemployment insurance reserves with balances totaling \$722,871 were reasonable. Additionally, the Board did not adopt a written reserve policy that states the Board's financial objectives for each reserve, the optimal or targeted funding levels and conditions under which each fund's assets will be used, replenished and discontinued.

Repair Reserve – The repair reserve is used to pay the cost of repairs to capital improvements or equipment that do not recur annually or at shorter intervals. Although this reserve had a balance of \$500,000, District officials have not expended any of these funds since the reserve was established in 2013. District officials explained they paid for repairs from general fund appropriations. Further, officials increased this reserve by \$375,000 since it was established. District officials were unable to provide us with documentation clearly stating the optimal or targeted funding levels of this reserve and the conditions under which this reserve fund would be used. Therefore, we question whether the amount held in this reserve is appropriate and necessary.

Unemployment Insurance Reserve – This reserve is used to reimburse the New York State Unemployment Insurance Fund for payments made to claimants on the District's behalf. Although this reserve had a balance of \$222,871, the average annual expenditure over the last five years was approximately \$15,311. Based on this cost level, the District's current reserve balance would cover unemployment insurance claims for approximately 14.5 years. Because the District budgets for these expenditures annually in the general fund and levies taxes to fund them, we question why the Board and District officials are continuing to retain a balance in this reserve.

Multiyear Financial Plan

It is important for District officials to develop a comprehensive multiyear financial plan to estimate the future costs of ongoing services and capital needs. An effective multiyear plan projects operating and capital needs and financing sources over a three- to five-year period. Such plans allow District officials to identify developing revenue and expenditure trends, set long-term priorities and goals and avoid large fluctuations in tax rates.

A multiyear financial plan can also be a vital tool to help District officials to assess the effects and merits of alternative approaches to address financial issues, such as using unrestricted fund balance to finance operations. Long-term financial plans work in conjunction with Board-adopted policies and procedures to provide necessary guidance to employees on the financial priorities and goals set by District officials. Additionally, District officials should monitor and update long-term financial plans on an ongoing basis to ensure that their decisions are guided by the most accurate information available.

District officials have not developed a multiyear operational plan. District officials told us that they are working on a plan with their fiscal advisors. A multiyear financial plan could have been a valuable resource for officials that would have allowed them to make more informed financial decisions during the budget process, which may have prevented the District's accumulation of fund balance that exceeded the statutory limit.

Recommendations

The Board should:

1. Develop estimates of expenditures and the use of fund balance in the annual budget based on historical and known trends.
2. Ensure that the amount of the District's unrestricted fund balance is in compliance with the statutory limit.
3. Use surplus funds as a financing source for:
 - Funding one-time expenditures;
 - Funding needed reserves; and
 - Reducing District property taxes.
4. Ensure that reserve fund balances are maintained at reasonable levels and take appropriate action, in accordance with statute, to remedy reserves with excess funds.
5. Adopt a reserve fund policy that states its financial objectives for the reserves, optimal funding levels and conditions under which the assets will be used.
6. Develop and adopt a comprehensive multiyear financial and capital plan that addresses the use of reserves and unrestricted fund balance. This plan should be updated regularly.

District officials should:

7. Use the debt service fund money for its intended legal purpose.
8. Use the agency fund's group health insurance account money as a financing source to pay for group health insurance, fund needed and properly established reserves or reduce real property taxes.

APPENDIX A

RESPONSE FROM DISTRICT OFFICIALS

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

The response letter contains references to attachments. Because the response letter sufficiently explains the relevance of these documents, they are not included here.

Administrative Offices
605 Palmer Street
(315) 894-5083 Superintendent
(315) 895-7781 Business Office
(315) 895-7011 Fax



**Frankfort-Schuyler
Central School District
Frankfort, NY 13340**

Middle-Senior High School
605 Palmer Street
(315) 895-7461 Principal
(315) 895-4032 Fax
(315) 895-7733 Special Education

Frankfort-Schuyler Elementary School
610 Reese Road
(315) 895-7491 Principal
(315) 895-4102 Fax

September 20, 2016

Via E-Mail & First Class Mail

████████████████████
Office of State Comptroller
Binghamton Regional Office
State Office Building, Room 1702
44 Hawley Street
Binghamton, New York 13901-4417

**Re: Frankfort-Schuyler Central School District
Audit Response and Corrective Action Plan**

Dear ██████████ and Taxpayers of the Frankfort-Schuyler Central School District:

The Frankfort-Schuyler Central School District is in receipt of the Draft Audit Report *Financial Management* for the period of July 1, 2014 through April 12, 2016, prepared by the Office of the State Comptroller. On behalf of the Board of Education and the District administration, we would like to thank the Comptroller's staff for their professionalism and courtesy in conducting their duties associated with this audit.

The Frankfort-Schuyler Central School District is committed to providing an exceptional educational program to prepare students for college and career success. The District is committed to ensuring that its finances are administered responsibly and in a manner that inspires public trust and confidence. Towards this end, the District's fiscal management policies reflect its overarching objectives of promoting transparency, public participation, and fiscal stability. Specifically, the District's financial management policies and procedures strive to:

1. Encourage advance planning through the best possible budgeting procedures.
2. Explore all practical sources of income.
3. Guide the expenditure of funds so as to extract the greatest educational return.
4. Expect top quality accounting and reporting procedures.
5. Maintain the highest level of unit expenditure needed to provide high quality education within the ability of the community to pay.

(Policy No. 4010).

We communicate clearly and often with the public about our financial strategies, and our annual budget materials seek to provide a transparent and informative environment. The District has consistently communicated its objective of sustaining its long-term financial health. The children and taxpayers of the Frankfort-Schuyler Central School District have lost considerable revenue due to the Gap Elimination Adjustment. These fiscal challenges have been exacerbated by the freezing of Foundation Aid. School districts throughout the State have been forced to make drastic cuts to programs and services in response to unplanned external fiscal challenges.

The District has sought to counteract unplanned fiscal challenges, and preserve the long-term financial strength of its educational programs, by implementing forward-looking financial planning. The District's financial management practices and reserve fund maintenance reflects a long term budgeting strategy which has allowed the District to avoid the fiscal disasters which have impacted other school districts in recent years. The District has not only maintained its educational programs through these fiscal challenges, but it has continued to expand the educational opportunities available to its students to prepare them for success in the ever-changing 21st century educational landscape. Indeed, the District recently updated all computer lab and library technology machines, updated each classroom with wireless access points, and provided each classroom with chrome books and/or tablets for each student. Simultaneously, the District has successfully maintained property taxes within New York State's Property Tax Cap since its enactment.

The State Comptroller's office spent several months at Frankfort-Schuyler Central School District reviewing our financial management procedures, processes, and policies. The scope of the audit was to examine the District's financial management for the period July 1, 2014 through April 12, 2016. As expected, the audit did not uncover any instances of fraud, or malfeasance with the School District's financial management. The District has reviewed the Comptroller's findings and recommendations from this audit, and has already taken corrective actions to strengthen our financial management. These actions will be recounted in our corrective action plan.

The audit report advised the District to implement policies to communicate the financial objectives of its reserve funds, maintain the District's reserve funds at "reasonable levels", and develop a multiyear operational and capital plan to address use of reserves and unrestricted fund balance. The District has already begun to take corrective action by developing a multiyear operational and capital plan with its fiscal advisors, Fiscal Advisors and Marketing, Inc. Additionally, the District has adopted a written policy that clearly describes the purpose and use of its reserve funds.

The District agrees with the Comptroller's position that reserve funds should be maintained at reasonable levels. The District also recognizes that funding levels must sustain the District's long-term planning objectives, and promote the future financial stability of the District. The Board and Administration have incorporated the Comptroller's findings to improve its

reserve fund management, and will continue to seek to strengthen its policies and procedures to benefit the children and taxpayers in the Frankfort-Schuyler Central School District.

Comptroller Recommendation 1:

Develop estimates of expenditures and the use of fund balance in the annual budget based on historical and known trends.

District Response:

The Board recognizes that historical and known trends are helpful in estimating the appropriate fund balance in the annual budget.

The Board of Education systematically reviews every budget line of the appropriations and makes efforts to adopt realistic estimates for expenditures. The Board's philosophy is to leave enough flexibility in the budget to meet any worst case financial demand which may arise during the school year, while maintaining adequate funds to secure the financial health of the District for future students.

The Audit Report's identification of "over-budgeted appropriations" is a reflection of factors, beyond the District's control, that lead to a difference in the budget appropriation versus actual expenses. For instance, in fiscal years when heating and gas rates decline, or when the area endures a mild winter, actual utility expenses are substantially lower than budgeted. This leads to the misperception that the appropriation was over-budgeted, despite its reasonableness at the time of conception. Moreover, the Audit Report's fund balance calculations do not factor unexpected revenue received by the District during recent years (ie. BOCES refunds). Similarly, such added revenue is unplanned, and accounts for a portion of the fund balance cited in the Audit Report.

The District agrees with the Comptroller's position that effective planning permits the most efficient use of funds. Towards this end, the District has developed a reserve plan, attached hereto, which sets forth a detailed analysis of each of the District's reserves. Specifically, the reserve plan identifies the following purpose, current balance, and ideal funding level for each reserve:

Reserve for Retirement Contributions (Employees Retirement System)

Purpose: Used to pay for employer contributions to the NYS Employee Retirement System;

Balance as of 6/30/2016: \$300,000;

Ideal Funding Level: \$288,000 - \$432,000 (2-3 years' retirement billings).

Reserve for Employees Benefits Accrued Liability

Purpose: Used to pay unused accumulated leave time contractually provided to certain groups of employees. This typically includes payment for unused sick, compensatory and/or vacation pay;

Balance as of 6/30/2016: \$567,478.40;

Ideal Funding Level: Funding should equal short & long term liability for compensated absences (\$728,731 on 6/30/2016).

Reserve for Unemployment

Purpose: Used to cover the cost of reimbursing the State Unemployment Insurance funds for payments made to claimants;

Balance as of 6/30/2016: \$222,871.15;

Ideal Funding Level: Amount equal to satisfy existing obligations and pending claims.

Reserve for Insurance

Purpose: Used to cover the cost of any loss, claim, action or judgment for which a school district is authorized or required to purchase insurance;

Balance as of 6/30/2016: \$33,000;

Ideal Funding Level: Amount equal to satisfy existing obligations, pending claims, notice of claims filed or for the anticipated purchase of additional insurance coverage.

Reserve for Repairs

Purpose: Used to cover the cost of repairs to capital improvements or equipment of a type that does not recur annually or at shorter intervals;

Balance as of 6/30/2016: \$969,377;

Ideal Funding Level: Estimated costs of up-coming repairs such as roofs, hot water heaters, heating vent units, metal siding on old gymnasium, parking lot and sidewalk repair at the middle school and high school.

Reserve for Tax Certiorari

Purpose: Used to cover the cost of judgments and claims resulting from tax certiorari proceedings;

Balance as of 6/30/2016: \$64,433.74;

Ideal Funding Level: Amount equal to satisfy existing claims and the estimated amount of anticipated judgments.

The District has designed a multiyear operational and capital plan, which in part provides for the lawful transfer of any excess reserve funds. Specifically, the multiyear operational and capital plan calls for the lawful transfer of \$100,000 of excess reserves to the District's capital outlay project. The capital outlay project will fund annual improvements that will be based on the Building Condition Survey, and approved by the voters annually. Moreover, the multiyear operational and capital plan provides for the establishment of a Capital Reserve Fund. The District will seek voter approval in May of 2017 for the establishment of the Capital Reserve Fund in an amount of \$7.5 million, with a ten (10) year term.

The District has also developed a reserve fund policy (Board Policy #4046) attached hereto, which explicitly governs the establishment, purpose, and use of its reserve funds.

The District will continue to monitor its use of fund balance in a manner which comports with prudent financial planning and Board Policy #4046.

Comptroller Recommendation 2:

Ensure that the amount of the District's unrestricted fund balance is in compliance with the statutory limit.

District Response:

The District will follow the Comptroller's guidance to ensure that its unrestricted fund balance is in compliance with the statutory limit.

To prepare the District for fiscal challenges during difficult economic times, the Board of Education has built contingencies into the budget to account for unexpected expenses. These contingencies allow the District to be prepared for unforeseeable increases to the budget, such as increases in the number of special education students, fluctuations in utility prices, health insurance premium increases, etc. The contingencies also provide the District flexibility to make sensible long-term financial decisions.

The District recognizes that the amount of the District's unrestricted fund balance must remain in compliance with the 4% statutory limit. To ensure compliance with the statutory limit, the District is in the process of implementing a multiyear operational and capital plan. The operational and capital plan is designed to maintain the District's unrestricted fund balance within the statutory limit. Specifically, the District plans to reduce excess funds through lawful transfers to both the capital outlay project and the capital reserve fund subsequent to its establishment.

In compliance with the Comptroller's recommendation, the District will continue its efforts to maintain the unrestricted fund balance at an appropriate level.

Comptroller Recommendation 3:

District officials should use surplus funds as a financing source for:

- Funding one-time expenditures
- Funding needed reserves
- Reducing District property taxes

District Response:

The Board will comply with the Comptroller's recommendation to use surplus funds to fund one-time expenditures and needed reserves, and reduce property taxes.

The District maintains surplus funds to secure the financial strength of its educational programs and provide strategic flexibility where necessary. As way of example, the District maintains surplus funds sufficient to exit its health insurance consortium, which enables the District to explore more fiscally prudent health insurance plans. While other school districts are constrained to remain in outdated and expensive health insurance plans for decades, the District has the flexibility to choose more cost effective plans as they become available. The District has strategically used surplus funds to lessen the impact of recent fiscal challenges, while also maintaining tax rates within New York State's Property Tax Cap.

The District will continue to strategically maintain surplus funds in a manner which ensures future financial viability at the lowest cost to District taxpayers.

Comptroller Recommendation 4:

Ensure that reserve fund balances are maintained at reasonable levels and take appropriate action, in accordance with statute, to remedy reserves with excess funds.

District Response:

The Board will follow the Comptroller's recommendation to confirm that all reserve fund balances are necessary, reasonable and in compliance with statutory requirements.

The District appreciates the Audit Report's guidance regarding ideal fund balances, and will continue to work with financial advisors and auditors to maintain fund balances which preserve the District's long-term financial stability.

The Audit Report represents that the District has overfunded the repair reserve, and has not expended money from the repair reserve since 2013. In funding the repair reserve, the Board relies on the Building Condition Survey which provides the amount of funding required. The amount of funding in the reserve mirrors the Building Condition Survey's recommended amount. Indeed, in June of 2016, the Board expended approximately \$132,000 to fund the resurfacing of the school track.

Nonetheless, the District recognizes that continual review of reserve balances promotes efficiency. Accordingly, the District has conferred with its financial advisor, Fiscal Advisors and Marketing, Inc., and auditors, and commenced review of its reserve balances to identify and address those reserves containing excess funds. As referenced above, the District's reserve plan identifies ideal funding levels to facilitate the identification and transfer of excess reserves. The

District will ensure that its reserve fund balances comply with statutory requirements through lawful transfers to its capital outlay project, and capital reserve fund.

The District will continue to evaluate its reserve fund balances annually, and will amend reserve balances as necessary to maintain legal compliance and promote fiscal stability.

Comptroller Recommendation 5:

Adopt a reserve policy that states its financial objectives for the reserves, optimal funding levels and conditions under which the assets will be used.

District Response:

On June 7, 2016 the District adopted a reserve policy which governs the establishment, maintenance, and expenditures of the District's reserves in compliance with all applicable legal requirements. This newly created Board Policy is Policy #4046, and is attached hereto. The policy was last reviewed on August 19, 2016. The Board will review the policy at least twice per year, and will insert amendments as necessary.

Moreover, the District's reserve plan sets forth each reserve fund's financial objective, optimal funding level and conditions under which assets will be used. The Board will review the District's reserve plan annually, and will update the plan as necessary.

The District is confident that these oversight procedures will assure that each reserve fund is used in adherence with Board Policy and legal requirements.

Comptroller Recommendation 6:

Develop and adopt a comprehensive multiyear financial and capital plan that addresses the use of reserves and unrestricted fund balance. This plan should be updated regularly.

District Response:

The District has developed a reserve plan, comprehensive multiyear operational and capital plan, and reserve fund policy to address oversight of the District's reserve funds and unrestricted fund balance. The District's operational and capital plan provides for the lawful transfer of excess reserve funds to fund the District's capital outlay project and capital reserve fund. The Board will establish procedures to prepare and review this plan annually to assure consistency with the District's short-term and long-term financial goals.

The District is confident that its newly developed policies and procedures will further strengthen its financial management.

Comptroller Recommendation 7:

Use the debt service fund money for its intended legal purpose.

District Response:

This recommendation is premised upon the debt service fund's balance of \$738,477 as of June 30, 2015. The Audit Report presupposes that this balance was not designated for any purpose.

To the contrary, debt service fund balance was designated to offset Bond Anticipation Notes for upcoming capital projects. As intended, \$306,749.99 was used in July 2016 for this purpose. The District will also transfer funds to offset Bond Anticipation Notes for a capital project in July of 2017.

The Board will continue to use the debt service fund as legally authorized.

Comptroller Recommendation 8:

Use the agency fund's group health insurance account money as a financing source to pay for group health insurance, fund needed and properly established reserves and/or reduce real property taxes.

District Response:

As authorized by the Education Law and the Teacher's Association Collective Bargaining Agreement, the District has established a trust and agency account in which employee payroll deductions are stored, and ultimately disbursed to cover the employee portion of healthcare insurance liability.

Annually, the entire amount of money derived from payroll deductions is used to fund the employee portion of the liability on a dollar-for-dollar basis. The agency fund has accrued an excess balance of approximately \$1.2 million as a result of general fund transfers, which were designed to cover the residual fees from the District health consortium plan in the event the District changes plans. The District has estimated that approximately \$600,000 will be necessary to secure a more favorable healthcare insurance plan in the near future, at a substantial long-term net gain.

Pursuant to Comptroller guidance, the District is in the process of lawfully transferring the excess balance of approximately \$600,000 to an authorized reserve fund. The District, with its financial advisors, has designed a plan to transfer the excess to its general fund, capital reserve, or to fund health expenses as necessary. The transfers will occur in \$60,000 increments over the next 10 years. The Board will continue to use the health insurance account in a custodial capacity to pay for employee's group health insurance liability.

Conclusion:

September 20, 2016

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The School District would like to thank the Comptroller's Office for their thoroughness and professionalism during the time they spent in the District.

The Audit Report offers constructive guidance to strengthen our management of the District's finances, supplementing action already taken by the District to strengthen our financial management policies and reserve fund procedures. We have addressed in this response our plans to implement the Audit Report's recommendations, including actions already initiated. In furtherance of the District's guiding principles, we will implement the Comptroller's Office guidance in a manner which promotes transparency, and preserves the District's long-term financial health for future generations.

Lisa Morgan
Board President

Robert F. Reina
Superintendent of Schools

APPENDIX B

AUDIT METHODOLOGY AND STANDARDS

To achieve our audit objective and obtain valid evidence, we performed the following procedures:

- We interviewed District officials and reviewed the Board minutes, resolutions and policies to gain an understanding of the process and procedures over the District's financial management.
- We reviewed general fund results of operations for the 2011-12 through 2014-15 fiscal years.
- We analyzed the trend in total fund balance, including the use of appropriated fund balance, in the general fund for the 2011-12 through 2014-15 fiscal years. We compared the appropriated fund balance to the same year's operating results to determine if the appropriated fund balance was actually used.
- We calculated the unrestricted fund balance in the general fund as a percentage of the ensuing year's appropriations to determine if the District was within the statutory limitation during the 2011-12 through 2014-15 fiscal years.
- We analyzed the debt service fund to identify the trend in fund balance and to determine if fund balance had been used during the last four years.
- We reviewed the agency fund's health insurance contributions to determine if the District properly transferred the correct amount from the agency fund to the general fund during 2014-15. We also inquired of District officials about the more than \$1 million that remained in this account over the past three years.
- We compared the budgeted revenues and appropriations to the actual revenues and expenditures for the general fund for fiscal years 2011-12 through 2014-15 to determine if the District's budgets were reasonable.
- We reviewed the trend of real property tax rates, levies and assessments for the 2011-12 through 2015-16 fiscal years.
- We reviewed District reserve accounts and related records to determine if funding levels appeared reasonable.

We conducted this performance audit in accordance with 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 C

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