



Red Creek Central School District Financial Condition

Report of Examination

Period Covered:

July 1, 2012 - June 9, 2016

2016M-365



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

December 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 Red Creek Central School District, entitled Financial Condition. 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 Red Creek Central School District (District) is located in the Towns of Butler and Wolcott in Wayne County and the Towns of Victory, Conquest and Sterling in Cayuga 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 Assistant Superintendent for Business and Finance (Assistant Superintendent) is responsible for overseeing the District's financial operations, under the direction of the Superintendent and Board.

The District operates three schools¹ with approximately 920 students and 300 employees. The District's budgeted general fund appropriations for the 2016-17 fiscal year are \$20.76 million and are funded primarily with State aid and real property taxes.

Objective

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

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

Scope and Methodology

We examined the District's financial condition for the period July 1, 2012 through June 9, 2016. We extended our scope through September 28, 2016 to include preliminary² financial results for 2015-16.

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 findings and indicated they plan to initiate corrective action.

¹ An elementary, middle and high school, which are all located on the same campus

² Unaudited financial information

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 Condition

The responsibility for accurate and effective financial planning rests with the Board and Superintendent. It is essential that the Board adopt structurally balanced budgets in which reasonable levels of fund balance are maintained. A district may retain a portion of fund balance, referred to as unrestricted, unappropriated funds, but must do so within the legal limit established by New York State Real Property Tax Law (RPTL).

Prudent fiscal management also includes maintaining sufficient and appropriate balances in reserves to address long-term obligations or planned future expenditures. In doing so, District officials should adopt a detailed policy or plan governing the establishment, use and funding levels or goals of reserve funds. Funding reserves at greater than reasonable levels contributes to real property tax levies that are higher than necessary. Finally, District officials should develop detailed multiyear financial and capital plans to allow them to set long-term priorities and work toward specific goals.

The Board appropriated \$678,000 of fund balance in each budget for fiscal years 2013-14 through 2015-16. However, actual operations resulted in 71 percent of the appropriated fund balance remaining unused because of overestimated expenditures. When adding back unused appropriated fund balance, the District's recalculated unrestricted fund balance was between 4.9 and 7.3 percent of the next year's budget in fiscal years 2012-13 through 2014-15, exceeding the statutory limit. Additionally, two of the District's reserves, totaling \$900,000, may be overfunded and potentially unnecessary.

Fund Balance

Fund balance represents the cumulative residual resources from prior fiscal years. Fund balance can be used in several ways, including to lower real property taxes for the next fiscal year or to help with cash flow to pay for unexpected expenditures, or can be set aside and reserved to finance future costs for a variety of specified purposes. RPTL allows the District to retain up to 4 percent of the next fiscal year's budgeted appropriations for unexpected events and to provide for cash flow. Fund balance in excess of that amount must be used to fund a portion of the next year's appropriations, thereby reducing the tax levy, or used to fund legally established reserves or pay down existing debt.

The District reported year-end unrestricted fund balance at levels that were close to the 4 percent limit for the 2012-13 through 2014-15 fiscal years (Figure 1). The Board accomplished this, in part, by appropriating fund balance and budgeting for a planned operating

deficit in the ensuing year's budget. However, the Board consistently overestimated expenditures in its adopted budgets, resulting in operating deficits that were less than budgeted in fiscal years 2013-14 and 2015-16, and an operating surplus in fiscal year 2014-15. Therefore, actual operating results for fiscal years 2013-14 through 2015-16 resulted in the District using approximately \$585,000 (29 percent) of the \$2.03 million of appropriated fund balance to finance operations.

Figure 1: Unrestricted Fund Balance at Year-End				
	2012-13	2013-14	2014-15	2015-16^d
Total Beginning Fund Balance ^a	\$6,151,719	\$6,101,617	\$5,602,875	\$5,674,209
Plus: Operating Surplus/(Deficit) ^b	(\$50,102)	(\$498,757)	\$71,334	(\$85,961)
Total Ending Fund Balance	\$6,101,617	\$5,602,860	\$5,674,209	\$5,588,248
Less: Restricted Fund Balance ^c	\$3,870,554	\$3,564,604	\$3,626,515	\$3,084,455
Less: Nonspendable Fund Balance	\$357,731	\$357,731	\$420,730	\$420,730
Less: Appropriated Fund Balance for the Ensuing Year	\$678,000	\$678,000	\$678,000	\$678,000
Less: Encumbrances	\$434,781	\$247,801	\$156,859	\$72,891
Unrestricted Fund Balance at Year-End	\$760,551	\$754,724	\$792,105	\$1,332,172
Ensuing Year's Budget	\$19,350,000	\$19,600,000	\$19,995,000	\$20,766,000
Unrestricted Fund Balance as a Percentage of Ensuing Year's Budget	3.93%	3.85%	3.96%	6.42% ^e
^a Balances net of prior period adjustments and other minor adjustments ^b Includes interfund transfers ^c Consists of the following reserves: unemployment insurance, liability, insurance, tax certiorari, employee benefit accrued liability, capital, bus purchase and retirement ^d Based on unaudited information ^e Prior to any transfers to reserves being made. Historically, the District has made transfers to reserves to reduce unrestricted fund balance to be within the statutory limit.				

Because the District appropriated fund balance to fund operations and funded reserves at year-end, it reported year-end unrestricted fund balance that complied with the statutory limit from fiscal years 2012-13 through 2014-15. However, after adding back unused appropriated fund balance, the District's recalculated unrestricted fund balance ranged from 4.9 to 7.3 percent of the ensuing year's budget during this time, which exceeded the statutory limit each year (Figure 2).

Figure 2: Unused Fund Balance			
	2012-13	2013-14	2014-15
Unrestricted Funds at Year-End	\$760,551	\$754,724	\$792,105
Add: Appropriated Fund Balance Not Used to Fund Ensuing Year's Budget	\$179,243	\$678,000	\$592,039 ^a
Recalculated Unrestricted Funds	\$939,794	\$1,432,724	\$1,384,144
Recalculated Unrestricted Funds as a Percentage of Ensuing Year's Budget	4.9%	7.3%	6.9%
^a Based on preliminary unaudited figures, the District generated an operating deficit of \$85,961 in 2015-16.			

The District continued this practice in 2015-16 and 2016-17 by appropriating fund balance of \$678,000 in each fiscal year. In addition, the District increased the tax levy from \$4 million in 2012-13 to \$4.3 million in 2016-17, for an average annual increase of 1.96 percent and a total increase of 8 percent. Based on historical operating results, it is unlikely that the District will use all of the fund balance appropriated for fiscal year 2016-17, resulting in continued excess fund balance.

The combination of the District's practice of overestimating expenditures and increasing taxes resulted in the accumulation of excess fund balance and reduced transparency to District residents. Instead of decreasing the unrestricted fund balance as planned, the practice further increased the amount of accumulated fund balance. By lowering taxes and realizing budgeted operating deficits, District officials could have avoided accumulating excess fund balance.

Reserves

Reserves may be established by the Board in accordance with applicable laws. Money set aside in reserves must be used in compliance with statutory provisions which determine how reserves are established and how they may be funded, expended and discontinued. Generally, school districts are not limited as to how much money can be held in reserves. However, reserve balances must be reasonable. Funding reserves at greater than reasonable levels contributes to real property tax levies that are higher than necessary. The Board is responsible for developing a formal plan for the funding and use of reserves, including how and when disbursements should be made and optimal or targeted funding levels.

The Board adopted a reserve fund policy that authorizes the District to establish reserve funds in accordance with applicable laws and regulations. The policy requires that District officials provide the Board with an annual report of all reserve funds that includes the type and description of each reserve, the date the reserve was established, the amount of the sum paid into the reserve, the interest earned by the reserve and the total amount and date of withdrawal from the reserve. The report also should include an analysis of the projected needs for the reserve fund in the upcoming fiscal year and a recommendation for funding those projected needs.

The Assistant Superintendent provided the Board with a reserve plan report as of June 30, 2015 that includes a description of the reserve, date established, activity for the most recent fiscal year ended and the general intended long-range funding goal. However, this plan does not include the District's specific long-term intentions for the funding, use and maintenance of reserve funds, including a detailed analysis of the District's projected future needs.

As of June 30, 2016, the District had seven general fund reserves totaling approximately \$3 million. We analyzed these reserves for reasonableness and determined that the unemployment insurance reserve and capital bus purchase reserve totaling \$900,000 were overfunded and potentially unnecessary.

Capital Bus Purchase Reserve – The reserve was established and approved by voters on March 6, 2003, with a 10-year term and \$1 million maximum funding limit. The reserve was created for the purpose of financing the purchase of vehicles for student transportation. As of June 30, 2016, the balance of this reserve was \$544,482. On average, the District purchases two buses per year. Based on the 2014-15 cost of a 65-passenger bus totaling \$113,743 and a State aid reimbursement rate of 90 percent, the local share to the District to replace a bus is approximately \$11,375. For two of the four fiscal years reviewed, the District did not use this reserve and instead included bus purchases in the general fund budget and levied taxes to pay for them. While the District expended \$232,341 from the reserve in 2015-16 to purchase two buses, the reserve balance is sufficient to fund the District’s share of 48 bus purchases, or 24 years’ of purchases based on the average purchase activity.

Unemployment Insurance Reserve – This reserve is for reimbursing the New York State Unemployment Insurance Fund (SUIF) for payments to claimants where the school district has elected to use the “benefit reimbursement” method based on actual unemployment claims. If, at the end of any fiscal year, the money in this reserve exceeds amounts required to be paid into the SUIF, plus any additional amounts required to pay all pending claims, the Board may, within 60 days of the close of the fiscal year, elect to transfer excess funds to certain other reserve funds or apply the excess to the budgeted appropriations of the next succeeding fiscal year. As of June 30, 2016, the balance of this reserve was \$352,830. This balance could fund 32 employees for the maximum benefit amount,³ or 29 years of claims based on the District’s three-year claim average of approximately \$12,000.⁴ Ultimately, this reserve should be used to fund unplanned spikes in unemployment insurance expenditures.

Because the District has not developed an adequate reserve plan that projects anticipated long-term future needs, certain reserves may be overfunded and unnecessary. Further, the allocation of funds in the District’s reserves may be inappropriate for its needs.

Multiyear Planning

It is important for District officials to develop comprehensive multiyear financial and capital plans to estimate the future costs of

³ Effective October 5, 2015, the maximum benefit is \$425 a week for up to 26 weeks, or a maximum of \$11,050.

⁴ Based on expenditures in the 2012-13 through 2014-15 fiscal years

ongoing services and capital needs. Effective multiyear plans project operating and capital needs and financing sources over a three- to five-year period and allow District officials to identify revenue and expenditure trends, set long-term priorities and goals and avoid large fluctuations in tax rates. Multiyear plans also allow District officials to assess the effect and merits of alternative approaches to address financial issues, such as the use of unrestricted fund balance to finance operations and the accumulation of money in reserve funds. 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 the Board. Also, the Board must monitor and update long-term plans on an ongoing basis to ensure that decisions are guided by the most accurate information available.

The Board and District officials have not developed formal, written multiyear financial or capital plans. The failure to develop and adopt adequate multiyear plans which include specific estimates for revenues, expenditures, reserves, the use of debt service funds and fund balance and long-term capital needs inhibits officials' abilities to effectively manage District finances and address future needs. A multiyear plan can establish future needs and the methods of financing so that appropriate amounts can be accumulated in reserves, while keeping the unappropriated fund balance within limits and the tax levy at appropriate levels.

Recommendations

The Board and District officials should:

1. Discontinue the practice of adopting budgets that result in the appropriation of fund balance and reserve funds that will not be used.
2. Adopt an adequate reserve plan which includes the District's intentions for the long-term accumulation and use of reserve funds, analyze existing reserve fund levels against the plan and, if necessary, make statutorily allowed transfers between reserve funds to better align reserves with long-term needs, provide tax relief or both.
3. Develop and adopt comprehensive multiyear financial and capital plans for a three- to five-year period that address any economic or environmental factors which could affect the plans.

APPENDIX A

RESPONSE FROM DISTRICT OFFICIALS

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

RED CREEK CENTRAL SCHOOL DISTRICT

ADMINISTRATION CENTER, P.O. BOX 190, RED CREEK, NEW YORK 13143

Telephone (315) 754-2010
Fax (315) 754-8169



DAVID G. SHOLES
Superintendent of Schools

December 5, 2016

Edward V. Grant, Jr., Chief Examiner
Office of the State Comptroller
The Powers Building
16 West Main Street, Suite 522
Rochester, New York 14614-1608

Dear Mr. Grant:

This letter will serve as the official response from the Red Creek Central School District to the initial draft audit report prepared by your office for the period July 1, 2012 through June 9, 2016. First, I would like to commend your staff, [REDACTED], [REDACTED], and [REDACTED] for conducting this audit in a very thorough, professional and courteous manner. They were very respectful of the business office and other district staff. The district appreciates the recommendations, both written and verbal, that were offered as part of the audit.

FINDINGS

Fund Balance:

As stated in your report, the Red Creek Central School District is proud to note that we have always met the statutory requirements of year-end unrestricted fund balance as stated in the report. There is no statutory limitation for Appropriated Fund Balance limits and/or usage. The report found that the district did not always use the Appropriated Fund Balance and we believe that to be a fortunate outcome. For example, two (2) years ago, the district was forced to reduce its Fund Balance by \$498,757 and three of the four years cited in this report also resulted in the reduction of Fund Balance. These types of financial swings reflect the volatility of educating an ever-changing population of students within a budget. For example, just one (1) additional student with disabilities can increase expenses in excess of \$100,000 of which the district is forced to absorb absent additional revenue in that year. The amount currently appropriated equals approximately 3% of the current year's budget. We believe that working within a 3% budget tolerance is acceptable considering the many variables affecting a budget. Also, if the district were to spend every dollar that is appropriated, that same amount of revenue would need to be generated for the subsequent year and/or expenditures would need to be reduced. The tax cap restricts the district's ability to raise revenue and cuts to our very basic educational program would severely impact students in a negative way.

Through sound fiscal management over the past two (2) decades, the Red Creek CSD has been able to maintain a strong academic program, excellent facilities and one of the lowest tax rates in New York State. The residents of the RCCSD have validated this fiscal approach as evidenced by budget vote passing rates of 83%, 84%, and 86% over the past three (3) years.

The Board of Education and Administration have taken great effort to be transparent to our stakeholders. Our reserve balances have been included in the treasurer's report approved by the Board each month and have been discussed at length during numerous budget and capital project presentations. Our budgets have been developed and debated in open session and have historically been beneficial for both our students and the taxpayers.

Capital Bus Purchase Reserve:

The RCCSD has met the statutory requirements of this reserve and has strategically used the Bus Reserve to reduce the need to borrow money for the purchase of buses. Borrowing monies for bus purchases is expensive due to Bond attorney costs, financial advisor costs and interest expenses. By not borrowing to pay for buses, the district keeps the tax rate lower and can help augment the educational program for students. The District is required to pay the entire amount for school buses at the time of purchase as evidenced by the reduction of the Bus Purchase Reserve by \$231,980 in the 2015-16 school year. The aid on the two (2) buses purchased will not be fully received by the district until 2022.

Unemployment Insurance Reserve:

The RCCSD has met the statutory requirements of this reserve and has strategically used and funded this reserve throughout the years. It is agreed that the district has been fortunate over the past three years and has not needed to dramatically draw down this reserve. However, for a high need district that is dependent on the State for upwards of 72% of its revenue, a reserve such as this can be quite necessary and beneficial should the state reduce aid as it has most recently through the GAP elimination adjustment. The district will review this reserve for reasonableness as part of its reserve analysis.

Multiyear Planning:

The district has had a 3-5 year financial plan in the past. However, given the fact that this District is dependent on New York State for upwards of 72% of its revenue, long term planning can be quite futile if the state does not do the same. Our long term planning has consisted of maintaining adequate reserves and fund balance in order to meet the many State and Federal mandates required of school districts and to protect the district from reductions in state aid that have been a reality in the past. However, in respect to the comptroller, the district will work towards a long term projection of expenditures.

The District will be submitting a separate Corrective Action Plan to address the recommendations outlined in your report. Again, the District would like to thank you and your staff for your time and effort.

Very truly yours,

RED CREEK CENTRAL SCHOOL

David G. Sholes
Superintendent of Schools

DGS/ak

cc: Members, Board of Education
Andrew J. DiBlasi, Business Administrator
Jolean B. Bliss, District Treasurer

APPENDIX B

AUDIT METHODOLOGY AND STANDARDS

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

- We interviewed District officials to gain an understanding of the budget process. We reviewed financial information provided to the Board and reviewed the Board minutes for financial discussions.
- We reviewed relevant policies and plans, including budgeting and reserve policies and the District's adopted reserve plan, for adequacy.
- We compared unrestricted unappropriated funds to the ensuing years' budgeted appropriations to determine if the District was within the statutory limit. We further reviewed the District's operating results and analyzed fund balance based on actual operating results.
- We reviewed District reserve accounts to determine if reserves were properly and legally established.
- We analyzed the District's reserve funds for fiscal years 2012-13 through 2015-16 to determine their funding, use, reasonableness and compliance with applicable statutes.

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.

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