OFFICE OF THE NEW YORK STATE COMPTROLLER

DIVISION OF LOCAL GOVERNMENT
& SCHOOL ACCOUNTABILITY

Monticello Central School District

Budgeting

Report of Examination

Period Covered:

July 1, 2012 — October 2, 2013

2014M-97

Thomas P. DiNapoli

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State of New York
Office of the State Comptroller

Division of Local Government
and School Accountability

September 2014

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 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 Monticello Central School District, entitled Budgeting. 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 Monticello Central School District (District) is located in the Towns of Bethel, Fallsburgh, Forestburgh, Mamakating and Thompson in Sullivan County. The District is governed by the Board of Education (Board) which comprises nine elected members. The Board is responsible for the general management and control of the District's financial and educational affairs and adopting the annual budget, which is prepared by various District officials, including the District Business Administrator (Business Administrator). The Superintendent of Schools (Superintendent) is the chief executive officer of the District and is responsible, along with other administrative staff, for the day-to-day management of the District under the direction of the Board. The current Superintendent started with the District in August 2011, and the current Business Administrator started with the District in September 2011.

The District's general fund budgeted appropriations for the 2013-14 school year totaled $80,186,419, which were funded primarily with real property taxes and State aid. The District operates five schools, with approximately 3,100 students and 600 employees. The District's employees are represented under nine collective bargaining agreements. Two agreements expired as of June 30, 2011 and remained unsettled until July 2012 and November 2013, respectively.

Objective

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

- Did the Board and District officials adopt reasonable budgets?

Scope and Methodology

We examined the financial condition of the District for the period July 1, 2012 through October 2, 2013. To analyze the District's historical financial condition and reserves, we extended our audit scope period back to July 1, 2009 and projected forward through June 30, 2014.

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 is included in Appendix D 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 B, have been considered in preparing this report. Except as specified in Appendix B, District officials generally agreed with our recommendations and indicated that they plan to initiate corrective action. Appendix C includes our comments on the issues 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 forwarded 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.

Budgeting

The Board and District officials are responsible for adopting budgets that contain realistic estimates of expenditures and the resources available to fund them and for ensuring that fund balance does not exceed the amount allowed by law. Estimates of expenditures (i.e., appropriations) should be based on known needs as well as historical trends. Similarly, revenue estimates should be based on known sources of revenue reflective of any identified trends. The surplus accumulated over time by District operations (i.e., unexpended surplus fund balance[1]) due to revenues exceeding expenditures is not allowed to exceed 4 percent of the ensuing year's appropriations, which is the legal limit established by New York State Real Property Tax Law. Excess unexpended surplus fund balance may be used to reduce tax levies or establish various legal reserves to finance certain future expenditures (as defined by each reserve). The Board should establish policies relating to reserves, defining which reserves would be established along with the reasonable funding amounts.

The Board and District officials could have adopted more reasonable budgets. The budget estimates for revenues and expenditures have not been aligned with historical or actual needs of the District. This resulted in putting an unnecessary burden on taxpayers. From 2009-10 to 2012-13, the District spent an average of $6 million less than budgeted and received $2.3 million more in revenue than budgeted.

Table 1: Budget Variances

	2009-10	2010-11	2011-12	2012-13[a]	Average
Revenue Variance (Budget vs. Actual)	$1,602,386	$2,140,887	$2,523,544	$2,919,864	$2,296,670
Expenditure Variance (Budget vs. Actual)	$7,550,837	$7,197,087	$5,935,161	$3,284,899	$5,991,996
Total Variance	**$9,153,223**	**$9,337,974**	**$8,458,705**	**$6,204,763**	**$8,288,666**

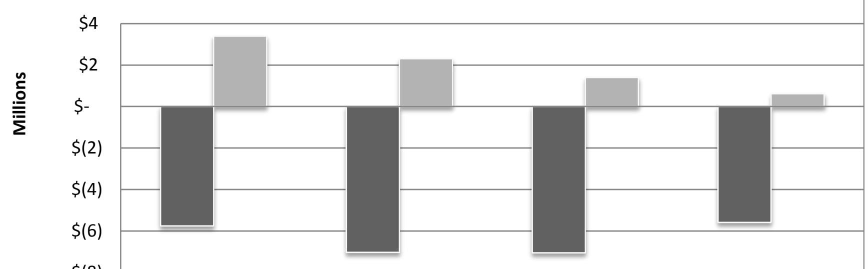
[a] The first budget prepared by the current Superintendent and Business Administrator was for fiscal year 2012-13.

[1] 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).

These revenue variances were primarily caused by consistently underestimating BOCES refunds (average of $1.7 million variance). The expenditure variances were caused by overestimating expenditures related to teaching-regular school (average of $1.4 million variance), program for students with disabilities services (average of $1.4 million variance), transportation services (average of $584,000 variance) and plant operation (average of $497,000 variance).

While District officials planned for operating deficits from 2009-10 through 2012-13 averaging $6.4 million, to be funded by unexpended surplus funds, the budgets have provided surpluses. Therefore, these funds were not needed. Although District officials have taken steps and have lessened operating surpluses from $3.4 million in 2009-10 to less than $615,000 in 2012-13, unexpended surplus fund balance has continued to grow.

Table 2: Results of Operations - Planned vs. Actual



	2009-10	2010-11	2011-12	2012-13
■ Planned Results of Operations - Surplus/(Deficit)	$(5,757,225)	$(7,030,000)	$(7,052,000)	$(5,590,000)
■ Actual Results of Operations - Surplus/(Deficit)	$3,395,898	$2,307,481	$1,406,486	$614,763

The 2013-14 budget had a planned operating deficit of $5.5 million, but the District will end the year with a projected operating surplus of $2.5 million, further increasing the surplus. Currently, there are no Board policies relating to reserves and reasonable balances.

Though District officials reviewed and adjusted the funding levels of some of the District's reserves, others remained funded at levels that were higher than necessary. The adopted budgets since the 2009-10 fiscal year included appropriations relating to the purposes of two of those reserves: workers' compensation claims and unemployment insurance. For example, as of June 30, 2013, the workers' compensation reserve had a balance of approximately $2.6 million, which would be enough to fund three years of expenditures based on the District's four-year average annual expenditures. In addition, the unemployment insurance reserve had a balance of approximately $1.1 million as of June 30, 2013, which would be enough to fund seven years of expenditures based on the District's four-year average annual expenditures.

Our analysis comparing historical actual expenditures to adopted budgets identified that previous budgets were not prepared based on prior years' actual results. Moreover, while the budget for fiscal year 2012-13 was the first budget prepared by the current Superintendent and Business Administrator and budgeted amounts were closer to actual results than in prior years, the budgeted amounts still varied from actual amounts by more than $6.2 million. The Superintendent and Business Administrator stated that, while they identified the significance of the accumulated unexpended surplus fund balance, they intended to decrease the balance through gradual changes in order to avoid any negative effects caused by over-adjusting budgeted amounts, including future restrictions relating to the tax cap.[2] A Board member told us the Board was conservative in budgeting because of the perceived likelihood of a new local casino. She stated the Board anticipated future costs due to increased enrollment. Furthermore, according to the Business Administrator, the workers' compensation reserve is being maintained in case there is a substantial employee injury as the District's workers' compensation expenditures are direct payment of claims from the result of work-related injuries. However, she did state that she has not yet had the opportunity to review the funding of the unemployment insurance reserve.

As a result of poor budgeting practices, unexpended surplus fund balance as a percentage of the ensuing year's budgeted appropriations has grown from 8.4 percent as of June 30, 2010 to 17.6 percent as of June 30, 2013 and is likely to continue to rise. Adding the overfunded amount of the reserve balances would further increase this percentage. Furthermore, due to another unexpected operating surplus in 2013-14, this percentage will likely be even greater, and the $5.5 million of appropriated fund balance in the 2013-14 budget would not be needed. If this appropriated fund balance had been included in the unexpended surplus fund balance, the percentage would be 24.5 percent. District officials indicated they plan to create additional reserve funds, such as a capital reserve and an equipment reserve, which will decrease the amount of unexpended surplus fund balance.

We conclude that the increases in the District's real property tax levy between the fiscal years ended 2010 through 2013 were unnecessary.

[2] In 2011, the State Legislature enacted a law establishing a property tax levy limit, generally referred to as the property tax cap. Under this legislation, the property tax levied annually generally cannot increase more than 2 percent, or the rate of inflation, whichever is lower, with some exceptions. School districts may override the tax levy limit by presenting the voters a budget that requires a tax levy that exceeds the statutory limit. However, that budget must be approved by 60 percent of the votes cast.

Table 3: Change in Real Property Tax Levy vs. Surplus Results of Operations					
	2010	2011	2012	2013	Total
Change in Tax Levy (including STAR)	$1,007,043	$705,747	$2,612,323	$859,349	$5,184,462
Results of operations	$3,395,898	$2,307,481	$1,406,486	$614,763	$7,724,628

The aggregate operational surpluses were more than $2.5 million over the increases in the real property tax levies for the same years. If real property taxes were reduced by just 80 percent of the amount of appropriated fund balance, an average taxpayer in the District would have saved $558 on their real property tax bill, assuming a home with an assessed value of $179,000.[3] These unnecessary real property tax levies are particularly disconcerting given the District's demographic profile, where 30.5 percent of children in the District are living in poverty as compared to the statewide average of 21.3 percent.[4]

Recommendations

1. The Board and District officials should develop realistic budgets that are consistent with the District's actual revenues and expenditures to avoid raising more real property taxes than necessary.

2. The Board should ensure that the amount of the District's unexpended surplus fund balance is in compliance with Real Property Tax Law statutory limits and reduce the amount of unexpended surplus fund balance in a manner that benefits District taxpayers. Such uses could include, but are not limited to, using surplus funds as a financing source, funding one-time expenditures or funding appropriate reserves.

3. The Board should review all reserve balances and transfer excess funds to unrestricted fund balance, where allowed by law, or other reserves established and maintained in compliance with statutory directives. Also, the Board should establish policies relating to reserves, defining which reserves would be established along with the reasonable funding amounts.

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3 In order to distribute school district taxes among multiple municipalities, the level of assessment of each municipality must be equalized to full market value. This value reported would be the full assessed value after adjusting for equalization rates in the different towns and villages. Therefore, actual savings would vary depending on which town the taxpayer lived in.

4 United States Census Bureau 2012 small area income and poverty estimates *(SAIPE) Program* – www.census.gov. For additional demographics relating to Sullivan County, see Appendix A.

APPENDIX A

RELEVANT DEMOGRAPHICS

The following data has been included in this report to further detail the demographic and economic profile of the District and surrounding area located in Sullivan County.[5]

- The total rate of persons below the poverty level was 17.2 percent, compared to 14.9 percent for New York State.

- 11.7 percent of households received Supplemental Nutrition Assistance Program/food stamp benefits within the prior 12 months, compared to 13.5 percent for New York State. However, other indicators indicate a higher poverty level in the County than the rest of the State.

- The median household income (from 2008-2012) was $48,050, compared to $57,683 for New York State.

- 51.7 percent of households earn less than $50,000 of annual income, compared to 44 percent for New York State.

- The homeownership rate was 66.5 percent, compared to 54.5 percent for New York State. However, the median value is lower.

- The median value of owner-occupied housing units was $179,500, compared to $295,300 for New York State.

[5] Sullivan County demographic information as per *United States Census Bureau* located at www.census.gov

APPENDIX B

RESPONSE FROM DISTRICT OFFICIALS

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

Monticello Central School District
237 Forestburgh Road, Monticello, NY 12701
Tel: 845-794-7700 Fax: 845-794-7710
Daniel A. Teplesky, *Superintendent of Schools*
Mrs. Stacey Sharoff, *President - Board of Education*

"Building Excellence Through Trust" www.monticelloschools.net

July 24, 2014

H. Todd Eames, Chief Examiner
Office of the State Comptroller
Division of Local Government & School Accountability
44 Hawley Street
Suite 1702
Binghamton, NY 13901-4417

RE: Financial Condition - 2014M-97

Dear Chief Examiner Eames:

The Monticello Central School District accepts and acknowledges the Financial Condition Report of Examination 2014M-97. The scope of the work was for the time period of July 1, 2012 through October 2, 2013. The District response to the audit will include the corrective action plan. See Note 1 Page 13

The district would like to acknowledge that the current Superintendent and School Business Administrator came into the district in August 2011 and September 2011 respectively. And in three (3) out of the four (4) years that were under review, three (3) of the four (4) budgets developed were developed under the previous administration. See Note 2 Patge13

The report states revenue variances were primarily caused by consistently underestimated BOCES refunds. The revenue budget is built on an estimation with the previous year's actual revenues received and taken into consideration. The BOCES refund is a cultivated approach especially when estimating the exact number of special education students who will move in to the district yearly. The price to educate a student with special needs is particularly costly and the majority of the BOCES refund relates to special education costs.

Monticello disagrees with the State's poor budgeting practices statements. As previously stated the current administration started in the District in August and September 2011 and the 2011-2012 school budget was approved by taxpayers and adopted by the Board of Education in May/June 2011. The 2013-2014 school budget was the first budget prepared by the new Superintendent and School Business Administrator and dealt with the new Tax Cap. Another discrepancy to be noted is the Tax Cap did not allow the district to replicate the $5.5 million dollars that had been used to offset the revenue budget. As a result the district will need to decrease the appropriated $5.5 million fund balance and begin using surplus funds above the allowed 4%. The district also needs to use any additional allotment coming in from State Aid to further reduce the tax levy. The district received additional State Aid funds for the 2104-2015 school year. The idea was discussed with the Board of Education to use the additional funds to lower the levy; however, because an announcement by New York State on Casino placement will not occur until the fall of 2014, the District decided not to move forward in this direction. See Note 3 Page 13 See Note 2 Page 13 See Note 4 Page 13

As noted in my previous paragraph there is a strong possibility for up to two (2) Casinos to be located in Sullivan County, with one placed directly within the Monticello Central School District boundaries. Should this come to fruition and the District be required to re-open the former Duggan Elementary School (closed June 2010), the current fund balance permits the district to do so.

Corrective Action Plan

Recommendation 1 – District officials should develop realistic budgets that are consistent with the District's actual revenues and expenditures to avoid raising more real property taxes than necessary.

Corrective Action: The district has and continues to develop realistic budgets that are consistent with the District's actual revenues and expenditures. With the Tax Levy Cap in place and the Gap Elimination Adjustment the district, through use of a multiyear financial spreadsheet, projects that the district will be using its excess fund balance over the next five to six years.

See Note 3 Page 13

Recommendation 2 – The Board should ensure that the amount of the District's unexpended surplus fund balance is in compliance with Real Property Tax Law statutory limits and reduce the amount of unexpended surplus fund balance in a manner that benefits District Taxpayers. Such uses could include, but not limited to, using surplus funds as a financing source, funding one-time expenditures, or funding appropriate reserves.

Corrective Action: The Superintendent, in collaboration with the School Business Administrator and the Board of Education, will ensure that the amount of the District's unexpended fund balance is in compliance with Real Property Tax Law statutory limits. The Board approved, and subsequently approved on May 20, 2014 by District taxpayers, a onetime payment of $750,000 for security upgrades. The Superintendent and School District Administrator will propose to the Board of Education to place a resolution on the May 2015 ballot to fund a $1,500,000 Capital Reserve for future repairs on district buildings.

Recommendation 3 – The Board should review all reserve balances and transfer excess funds to unrestricted fund balance, where allowed by law, or other reserves established and maintained in compliance with statutory directives. Also, the Board should establish policies relating to reserves, defining which reserves would be established along with the reasonable funding amounts.

Corrective Action: The Superintendent, School Business Administrator and Board of Education will review all reserve balance and transfer excess funds to unrestricted fund balance. The District is working with its Third Party Administrator (TPA) to review the Workers' Compensation Reserve Fund to ensure the district has the appropriate amount reserved for all open cases. The Superintendent, in conjunction with the Board of Education Policy Committee, will begin the process of establishing policies relating to reserves and defining which reserves need to be established including a reasonable funding amount.

Respectfully,

Mr. Daniel A. Teplesky
Superintendent of Schools

Cc: Board of Education
Denise S. Cedeira, School Business Administrator

APPENDIX C

OSC COMMENTS ON THE DISTRICT'S RESPONSE

Note 1

As stated in the report, to analyze the District's historical financial condition and reserves, we extended our audit scope period back to July 1, 2009 and forward through June 30, 2014.

Note 2

Our audit reviewed five fiscal years from 2009-10 through 2013-14, and the first budget prepared by the current Superintendent and Business Administrator was for fiscal year 2012-13.

Note 3

From 2009-10 to 2012-13, the District spent an average of $6 million less than budgeted and received $2.3 million more in revenue than budgeted. Additionally, the 2013-14 budget had a planned operating deficit of $5.5 million, but the District ended the year with an operating surplus of $2.5 million. These significantly large budgeting variances and resulting operating surpluses do not demonstrate a pattern of realistic budgeting practices.

Note 4

Considering that the District did not need to use any appropriated fund balance during any of our scope period, more realistic budget estimates may have enabled a better use of fund balance to fund operations instead of increasing real property taxes every year.

APPENDIX D

AUDIT METHODOLOGY AND STANDARDS

To accomplish our audit objective, we interviewed appropriate District officials and employees, tested selected records and examined pertinent documents for the period July 1, 2012 through October 2, 2013. To analyze the District's historical financial condition and reserves, we extended our audit scope period back to July 1, 2009 and projected forward through June 30, 2014. Our examination included the following:

- We identified and documented relevant background and demographic information related to the District and Sullivan County.

- We reviewed and assessed the effectiveness of the District's budget development process from 2009-10 through 2012-13.

- We compared budgeted revenues and expenditures to actual results from 2009-10 through 2012-13.

- We used the District's 2013-14 fund balance projection report to determine the projected results of operations for the year in order to quantify the expected operating surplus or deficit as of June 30, 2014.

- We calculated the District's results of operations from 2009-10 through 2012-13 and identified all relevant trends.

- We documented the reported unexpended surplus fund balances from 2009-10 through 2012-13 and calculated those balances as a percentage of the ensuing years' appropriations.

- We assessed the appropriation and use of unexpended surplus funds from 2009-10 through 2012-13.

- We determined and assessed the reasonableness of funding levels of the District's reserves as of June 30, 2013.

- We identified trends in the District's real property tax levies from 2009-10 through 2012-13 and calculated the potential effect of using unexpended surplus funds to lower tax levy amounts.

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 E

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