



Jefferson Central School District Fund Balances

Report of Examination

Period Covered:

July 1, 2014 — August 6, 2015

2015M-236



Thomas P. DiNapoli

Table of Contents

	Page
AUTHORITY LETTER	1
INTRODUCTION	2
Background	2
Objective	2
Scope and Methodology	2
Comments of District Officials and Corrective Action	2
FUND BALANCES	4
Recommendations	8
APPENDIX A Response From District Officials	9
APPENDIX B Audit Methodology and Standards	12
APPENDIX C How to Obtain Additional Copies of the Report	13
APPENDIX D Local Regional Office Listing	14

State of New York Office of the State Comptroller

Division of Local Government and School Accountability

January 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 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 Jefferson Central School District, entitled Fund Balances. 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 Jefferson Central School District (District) is located in six towns¹ in Delaware and Schoharie counties. The District is governed by a five-member Board of Education (Board). 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 District Treasurer plays a key role in the budget development process along with performing the daily accounting duties.

The District operates one school with 254 students and 50 employees. The District's 2015-16 general fund budgeted appropriations were \$6.4 million, primarily funded through State aid and real property taxes.

Objective

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

- Did the Board and District officials ensure that the fund balances of the general fund and certain reserve funds were reasonable?

Scope and Methodology

We examined the District's financial records for the period July 1, 2014 through August 6, 2015. We extended our scope back to July 1, 2010 and forward through June 30, 2016 to trend and project financial condition, budgeted amounts and fund balance.

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 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 the General Municipal Law, Section 2116-a(3)(c)

¹ Towns of Harpersfield and Kortright in Delaware County and Towns of Blenheim, Gilboa, Jefferson and Summit in Schoharie County

of the 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 should be prepared and provided to our office within 90 days, with a copy forwarded to the Commissioner of Education. 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.

Fund Balances

Fund balance represents resources remaining from prior fiscal years that can be used to lower real property taxes for the ensuing fiscal year. A district may retain a portion of fund balance, referred to as unrestricted fund balance, within the limits established by the New York State Real Property Tax Law. Districts may also establish reserves to restrict a portion of fund balance for a specific purpose, also in compliance with statutory directives. However, reserve balances must be reasonable. Combining a reasonable level of unrestricted fund balance with specific legally established reserve funds provides resources for both unanticipated events and other identified or planned needs. Funding reserves at greater than reasonable levels contributes to real property tax levies that are higher than necessary because the excessive reserve balances are not being used to fund operations. The Board is responsible for developing a formal plan for the use of its reserves, including optimal or targeted funding levels and why these levels are justified, and ensuring that District officials are maintaining appropriate documentation to account for and monitor reserve activity and balances.

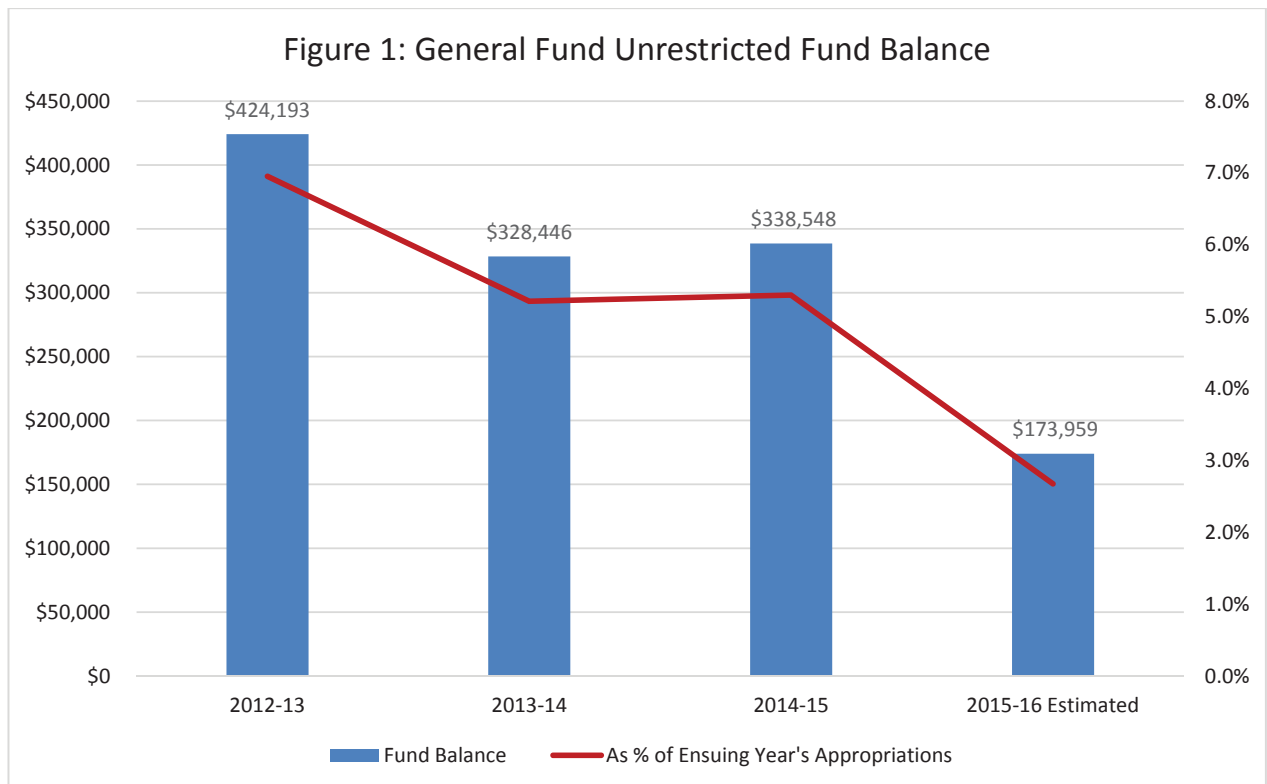
Accurate budget development, as well as budget monitoring and control, are effective ways to ensure fund balances are reasonable. Accordingly, it is essential that District officials develop reasonable, structurally balanced budgets to balance recurring expenditure needs with recurring revenue sources while providing desired services on a continuing basis and manage fund balance responsibly.

Over the past three years, the Board and District officials have adopted budgets that used fund balance of the general fund and certain reserve funds for operating expenditures. We commend the Board and officials for bringing the unrestricted fund balance closer to the 4 percent statutory limit, from 7 percent to 5.3 percent for fiscal years 2012-13 through 2014-15, and using reserve funds appropriately. As expenditures outpaced revenues, the Board and officials used unrestricted fund balance and certain reserve funds to offset the variance. However, continued reliance on unrestricted fund balance and reserve funds to finance recurring expenditures will put the District in a precarious financial position. If District officials use over \$164,000 (33 percent of the June 30, 2015 fund balance) to fund 2015-16 operations as planned, it will be the third consecutive year with an operating deficit. If District officials continue to appropriate and use fund balance at this rate, we estimate the unrestricted fund

balance will drop to 2.7 percent of the ensuing year's appropriations by the end of 2015-16.²

The continued use of fund balance and reserve funds to finance operations has also led to the real property tax levy being artificially low. If expenditures remain steady and District officials do not identify other significant revenues to offset the use of fund balance, the real property tax levy would need to increase approximately 6 percent to make up the shortfall in the 2015-16 budget. Moreover, having significant balances set aside for specific purposes in reserves limits the ability to finance expenditures for other purposes including capital needs.

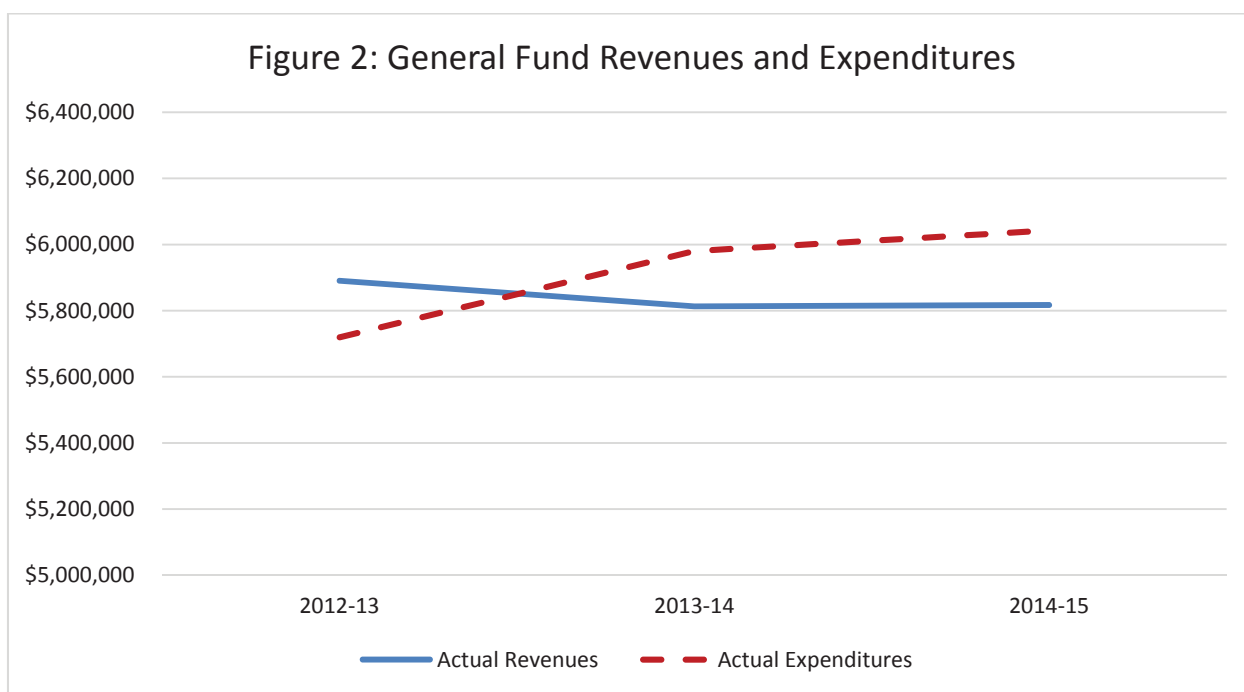
Unrestricted Fund Balance – The District's unrestricted fund balance as of June 30, 2015 exceeded the statutory maximum of 4 percent of the ensuing year's appropriations. However, from 2012-13 through 2014-15, the unrestricted fund balance declined from \$424,193 (7 percent of the ensuing year's appropriations) to \$338,548 (5.3 percent of the ensuing year's appropriations). Moreover, if District officials continue to appropriate funds at this rate, we estimate the unrestricted fund balance will decrease even further, especially as reserve funds are depleted.³



² In order to estimate the ensuing year's appropriations for 2016-17, we calculated the average increase in appropriations from 2013-14 to 2015-16 and applied this average increase to the 2015-16 appropriations.

³ The 2015-16 estimate of unrestricted fund balance assumes that the District will appropriate the same amount of fund balance for the 2016-17 fiscal year.

Although the budget estimates for general fund revenues and expenditures were within a few percentage points from actual amounts,⁴ expenditures increased at a faster rate than revenues over the last two fiscal years (see Figure 2).



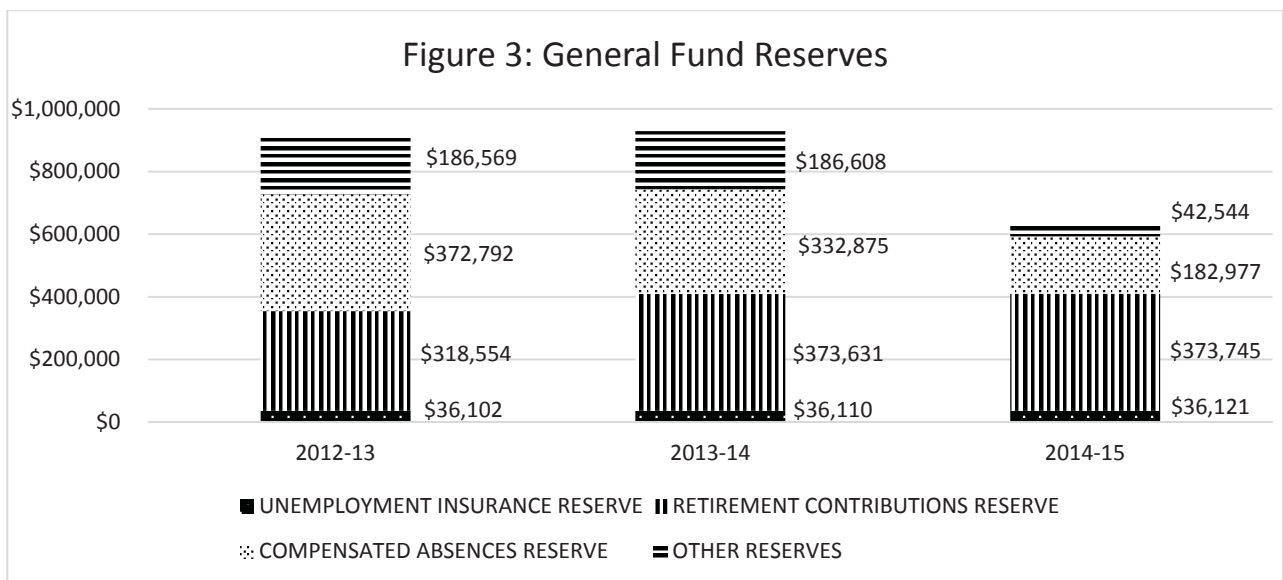
In addition, District officials have raised taxes close to the New York State Real Property Tax Cap limit, barring override.⁵ As a result, District officials have used non-recurring financing sources (i.e., unrestricted and reserved fund balances) to finance the variance. Further, the District recently lost their largest real property taxpayer to tax-exempt status.⁶ While this loss does not necessarily impact the total levy raised, it will impact the property tax rate paid by the remaining taxable properties in the District.

Reserves – District officials have accumulated significant balances in three of the District’s reserves. As of June 30, 2015, the District had six reserves in the general fund totaling \$635,387.

⁴ From 2012-13 through 2014-15, the average variance between appropriations and expenditures was 3.8 percent and the average variance between budgeted revenues and actual revenues was 2.9 percent.

⁵ The law precludes a school district from adopting a budget that requires a tax levy that exceeds the prior year’s tax levy by more than 2 percent or the rate of inflation, whichever is less, and certain exclusions permitted by law, unless 60 percent of District voters approve a budget that requires a tax levy that exceeds the statutory limit.

⁶ Real property taxes totaling \$251,300 were withheld from the District upon the resolution of a tax certiorari case. District officials properly used \$122,100 from the tax certiorari reserve and anticipate receiving \$125,000 in 2015-16 from a grant to offset this burden.



We analyzed these reserves for reasonableness and adherence to statutory requirements and found the funding of the capital, insurance and tax certiorari reserves to be reasonable. However, the reserves for retirement contributions, compensated absences and unemployment insurance, with balances totaling \$592,843, appeared to be overfunded when compared to the amounts necessary for their stated purposes.

- **Retirement Contributions Reserve** – This reserve is used to pay the District’s retirement contribution to the New York State and Local Retirement System (NYSLRS). The District’s 2014-15 NYSLRS expenditure was approximately \$84,300. The reserve balance as of June 30, 2015, was \$373,700⁷ – more than four times higher than the 2014-15 annual contribution. However, the 2015-16 adopted budget plans for the use of \$90,000 from this reserve.
- **Compensated Absences Reserve** – This reserve must be used only for cash payments of accrued and unused sick, vacation and certain other leave time owed to employees when they leave District employment. As of June 30, 2015, we determined the District’s liability for compensated absences was approximately \$122,800. However, the reserve balance was \$183,000. Therefore, the reserve was overfunded by approximately \$60,200.
- **Unemployment Insurance Reserve** – This reserve is used to pay unemployment insurance claims under the “benefit reimbursement” method. The District’s average annual

⁷ Over the past five years, this reserve was used to fund \$45,000 of the District’s retirement contribution expenditures, which totaled \$439,717 during that period.

unemployment insurance expenditure for the past five years was \$2,000. However, the \$36,100⁸ reserve balance as of June 30, 2015 was more than 18 times higher than the average annual expenditure.

Reserve balances accumulated to significant levels because District officials were historically transferring funds to them without using them. Moreover, District officials do not have long-term plans for reserve balance levels or usage.

Cost Savings – District officials have indicated they have taken several steps to curtail expenditures in 2014-15, such as eliminating an unnecessary bus route, enforcing a spending freeze, finding a less expensive bus maintenance vendor and bringing students back to the District from the District’s Board of Cooperative Educational Services (BOCES) programs and enrolling them in District programs that are less expensive. District officials told us that they estimate that they will save \$58,000 per year by changing the bus maintenance vendor. The District is also in the process of having an energy-efficiency audit conducted by the New York State Energy Research and Development Authority (NYSERDA) to determine if it can save on energy costs.

Recommendations

The Board should:

1. Establish formal spending levels and long-term plans for the District’s unrestricted fund balance and reserves.
2. Review all reserve balances and transfer excess funds to unrestricted fund balance, where allowed by law, or use the reserve funds for their designated purposes.

District officials should:

3. Closely monitor the level of unrestricted fund balance and reduce reliance on fund balance as a financing source, while continuing to evaluate and explore ways to reduce expenditures and increase revenues.

⁸ This reserve has not been used to fund any of the District’s unemployment insurance expenditures in the past five years.

APPENDIX A

RESPONSE FROM DISTRICT OFFICIALS

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



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January 1, 2016

Mr. H. Todd Eames, Chief Examiner
Office of the State Comptroller
Binghamton Regional Office
44 Hawley Street - Suite 1702
Binghamton, NY 13901-4417

Dear Mr. Eames:

I am writing this letter in response to the findings identified by the Office of the State Comptroller Division of Local Government and School Accountability. We are in receipt of the draft report your office recently issued detailing your audit of our district's finances. Our Board of Education takes its fiduciary responsibilities very seriously. Beyond that, we rely heavily upon the scrutiny of our external auditors and the Comptroller's Office, both of whom periodically review our district's finances.

As you noted in your report, our district continues to work in the areas of Reserves, Fund Balances and Cost Savings. We are writing to assure you that we will adapt corrective actions as a result of your findings. In the paragraphs that follow, we have attempted to acknowledge and respond to each of your auditors' findings.

Comptroller's Findings:

1. Unrestricted Fund Balance – The District's unrestricted fund balance at June 30, 2015 exceeded the statutory maximum of 4 percent of the ensuing year's appropriations. However, from 2012-13 through 2014-15, the unrestricted fund balance declined from \$424,193 (7.0 percent of the ensuing year's appropriations) to \$338,548 (5.3 percent of the ensuing year's appropriations). Moreover, if **District officials continue to appropriate funds at this rate, we estimate the unrestricted fund balance will decrease even further, especially as reserve funds are depleted.**
2. Reserves – District officials have accumulated significant balances in three of the District's reserves. As of June 30, 2015, the District had six reserves in the general fund totaling \$635,387. We analyzed these reserves for reasonableness and adherence to statutory requirements and found the funding of the capital, insurance and tax certiorari reserves to be reasonable. However, the reserves for retirement contributions, compensated absences and unemployment insurance, with balances totaling \$592,843, appeared to be overfunded when compared to the amounts necessary for their stated purposes. **Reserve balances accumulated to significant levels because District**

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officials were historically transferring funds to them without using them. Moreover, District officials do not have long-term plans for reserve balance levels or usage.

3. Cost Savings – District officials have indicated they have taken several steps to curtail expenditures in 2014-15, such as eliminating an unnecessary bus route, enforcing a spending freeze, finding a less expensive bus maintenance vendor and bringing students back to the District from the District’s Board of Cooperative Educational Services (BOCES) programs and enrolling them in District programs that are less expensive. District officials told us that they estimate that they will save \$58,000 per year by changing the bus maintenance vendor. The District is also in the process of having an energy-efficiency audit conducted by the New York State Energy Research and Development Authority (NYSERDA) to determine if it can save on energy costs.

Comptroller’s Recommendations/ District Response:

The Board should:

1. Establish formal spending levels and long-term plans for the District’s unrestricted fund balance and reserves.

District Response: The Board of Education and the Administration will establish formal levels and long-term plans for the District’s unrestricted fund balance and reserves.

2. Review all reserve balances and transfer excess funds to unrestricted fund balance, where allowed by law, or use the reserve funds for their designated purposes.

District Response: The Board of Education and the Administration will review all reserve balances and transfer excess funds to unrestricted fund balance, where allowed by law, or use the reserve funds for their designated purposes.

3. Closely monitor the level of unrestricted fund balance and reduce reliance on fund balance as a financing source, while continuing to evaluate and explore ways to reduce expenditures and increase revenues.

District Response: The Board of Education and the Administration will closely monitor the level of unrestricted fund balance and reduce reliance on fund balance as a financing source, while continuing to evaluate and explore ways to reduce expenditures and increase revenues.

Respectfully Submitted:

Mr. Brian M. Corey, Superintendent

APPENDIX B

AUDIT METHODOLOGY AND STANDARDS

To achieve our audit objective and obtain valid evidence, we interviewed District officials and employees, tested selected records and examined pertinent documents for the period July 1, 2014 through August 6, 2015. We expanded our scope back to July 1, 2010 and projected forward through June 30, 2016 to analyze the District's financial condition, budgeting trends and fund balance. We performed the following procedures:

- We interviewed District officials and reviewed Board minutes to gain an understanding of the budgeting process for the general fund, including the rationale for determining the amount of unrestricted fund balance available for appropriation and the procedures for monitoring and controlling the budget.
- We calculated the general fund's unrestricted fund balance as a percentage of the ensuing year's appropriations to determine if the District was within the statutory limitation during fiscal years 2012-13 through 2014-15. We also used the 2015-16 adopted budget and calculated the average increase in appropriations from 2013-14 through 2015-16 to calculate an estimated unrestricted fund balance at June 30, 2016 as a percentage of estimated 2016-17 appropriations.
- We analyzed the general fund's reserves to identify the trends and to determine if they were properly supported, reasonably funded and used during the last three fiscal years.
- We compared the budgeted revenues and appropriations to the actual revenues and expenditures for the general fund for 2012-13 through 2014-15 to determine if the District's budget estimates were reasonable.
- We reviewed the District's tax levies, taxable assessments and tax rates for 2012-13 through 2014-15 to determine if the tax levies and rates had been increasing.

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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