



Van Hornesville- Owen D. Young Central School District Financial Condition

Report of Examination

Period Covered:

July 1, 2013 – September 30, 2015

2016M-63



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

July 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 Van Hornesville-Owen D. Young 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 Van Hornesville-Owen D. Young Central School District (District) is located in the Towns of Stark, Columbia, Danube, German Flats, Little Falls and Warren in Herkimer County; Minden in Montgomery County; and Springfield in Otsego County. The District is governed by the Board of Education (Board), which is composed of five elected members. The Board is responsible for the general management and control of the District's financial and educational affairs. The Superintendent of Schools 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 operates one school with approximately 200 students in kindergarten through 12th grade and 40 full-time employees. The District's budgeted expenditures for the 2015-16 fiscal year were \$5.4 million, funded primarily with State aid and real property taxes.

Objective

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

- Does the Board adopt budgets with realistic estimates and maintain an appropriate level of fund balance?

Scope and Methodology

We examined the District's budgeting process for the period July 1, 2013 through September 30, 2015.

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. Unless otherwise indicated in this report, samples for testing were selected based on professional judgment, as it was not the intent to project the results onto the entire population. Where applicable, information is presented concerning the value and/or size of the relevant population and the sample selected for examination.

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 initiate 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 Condition

The Board is responsible for making sound financial decisions that are in the best interest of the District, the students it serves and the taxpayers who fund the District's programs and operations. Sound budgeting practices, based on accurate estimates, along with prudent fund balance management are essential to maintaining a healthy financial condition. Proper budget development begins with identifying and estimating the necessary expenditures to carry out the District's programs. The Board must next identify and estimate the revenues, other than real property taxes, that should be available to finance the planned expenditures. The Board must also estimate the amount of unrestricted fund balance (resources remaining from prior fiscal years) that will be available at year-end, some or all of which may be used to pay for unexpected expenditures or fund the ensuing year's appropriations. After taking these factors into account, the Board establishes the expected tax levy necessary to fund operations. Accurate budgetary estimates help ensure that the real property tax levy is not greater than necessary.

Estimates for revenues and expenditures should be developed based on prior years' operating results and trends, anticipated future needs and available information related to projected changes in significant revenues or expenditures. Unrealistic budget estimates can mislead District taxpayers and significantly affect the District's year-end unrestricted fund balance and financial condition.

Unrestricted fund balance that exceeds the 4 percent statutory limit set by New York State Real Property Tax Law should be used to lower real property taxes, fund existing reserves or pay for one-time expenditures. When fund balance is appropriated as a funding source, it reduces the fund balance included in the 4 percent calculation, and a planned operating deficit is expected in the ensuing fiscal year, with the difference to be financed by appropriated fund balance. Conversely, an operating surplus (when budgeted appropriations are not fully spent, revenues are greater than expected or both) increases the total year-end fund balance and can indicate that budgets are not realistic.

The Board and District officials did not effectively manage the District's financial condition by ensuring budget estimates were reasonable and based on historical costs and trends and that fund balance was maintained at the statutory limit. In 2013-14 and 2014-15 the District adopted budgets that projected planned operating deficits (appropriated fund balance) of \$103,272 and \$218,440, respectively. However, the District instead experienced operating surpluses of

\$173,105 in 2013-14 and \$37,382 in 2014-15 and, in fact, did not need to use the appropriated fund balance. Furthermore, the District has accumulated unrestricted fund balance that exceeds the statutory limit for the ensuing year's budgeted appropriations. As of June 30, 2015, the District's reported unrestricted fund balance was 19 percent of the 2015-16 budgeted appropriations.

Budgetary Estimates

We compared the District's budgeted general fund revenues and appropriations with operating results for fiscal years 2013-14 and 2014-15. Despite budgeting for operating deficits both years by appropriating fund balance to finance operations, the District realized operating surpluses each year (Figure 1).

Figure 1: Budget Estimates and Results of Operations

| | Budget | Actual | Variance |
|---|--------------------|------------------|------------------|
| Fiscal Year 2013-14 | | | |
| Revenues | \$5,452,871 | \$5,513,250 | \$60,379 |
| Less: Appropriations/Expenditures | \$5,556,143 | \$5,340,145 | \$215,998 |
| (Planned Deficit)/Actual Surplus | (\$103,272) | \$173,105 | \$276,377 |
| Fiscal Year 2014-15 | | | |
| Revenues | \$5,564,694 | \$5,665,381 | \$100,687 |
| Less: Appropriations/Expenditures | \$5,783,134 | \$5,627,999 | \$155,135 |
| (Planned Deficit)/Actual Surplus | (\$218,440) | \$37,382 | \$255,822 |
| Two-Year Total (Planned Deficits)/Actual Surpluses | (\$321,712) | \$210,487 | \$532,199 |

While the variances between budget estimates and actual results are not significant in either of the two years reviewed, they have contributed to an excessive and growing level of fund balance as discussed in the next section, "Fund Balance." From our review of the District's estimates and actual results, we did note certain accounts for which the Board did not adopt realistic estimates.

- The estimate for the "refund of BOCES services"¹ was \$6,000 for both 2013-14 and 2014-15. However, in 2013-14 the District received a refund of \$103,687 and in 2014-15 it received a refund \$119,601. The District again budgeted \$6,000 of revenue in the 2015-16 budget. The Business Administrator stated she budgeted for such a low refund amount because she was under the impression that budgeting at realistic levels may adversely affect BOCES aid, and the amount of the refund is difficult to estimate. She also stated that greater communication with BOCES is needed during

¹ The District receives a refund in the following year of the difference between the District's payments to Board of Cooperative Educational Services (BOCES) and BOCES' expenditures to provide the programs in the prior school year.

budget preparation to obtain more realistic estimates of the refund to be received in the coming year.

- The District's appropriation for diesel fuel for the Transportation Department was based on an expected usage of 14,000 gallons in 2013-14 and 13,500 gallons in 2014-15 at a cost of \$4.50 per gallon. We examined the diesel fuel invoices during our audit period and found the usage estimate was reasonable. However, the average cost during our audit period was \$3.00 per gallon, or 33 percent less than budgeted. Although the estimate for diesel fuel for both years totaled \$123,750, actual expenditures were \$61,969 during the two years. The Business Administrator stated that the \$4.50 per-gallon estimate was used so the District can readily absorb any increases in cost. For 2015-16 the District again budgeted its gallon cost for diesel fuel at \$4.50 per gallon. However, at the outset of the 2015-16 year and prior to the end of our audit period, the District was paying \$1.70 per gallon, or 62 percent less than budgeted.
- The District's appropriation for a BOCES prekindergarten program was \$24,000 in both 2013-14 and 2014-15. However, the District's actual cost for the program was \$9,437 in 2013-14 and \$9,406 in 2014-15. The Business Administrator stated that the District's cost for this service is based on grant funding to BOCES, and the District is billed the difference between the grant money BOCES receives and BOCES' cost to provide the program. BOCES does not provide the District with cost projections at budget preparation time. The Business Administrator further stated that she kept the budget at \$24,000 to deal with potential decreases in grant funding to BOCES. For 2015-16 the District budgeted \$24,000 for the program and expects to spend \$12,600.

A conservative approach to budgetary estimates is understandable; however, some District estimates were not in line with prior years' actual results or with the actual revenues realized or costs incurred. In addition, the District has more than ample fund balance to absorb unforeseen events, so a realistic budget could be adopted and the District would still be prepared for fluctuations. As a result, the District did not use any of the fund balance it had appropriated to finance operations in both 2014-15 and 2015-16, increasing an already excessive level of fund balance.

Fund Balance

The unrestricted fund balance was 13 percent and 19 percent of subsequent year's appropriations for the fiscal years ended June 30, 2014 and 2015, respectively, and, therefore, was in excess of the

statutory limit. Figure 2 shows the District's unrestricted funds, as reported.

| Figure 2: Unrestricted Fund Balance | | |
|---|-----------------------|-------------|
| | 2013-14 | 2014-15 |
| Total Beginning Fund Balance | \$1,360,626 | \$1,510,913 |
| Less: Prior Period Adjustment | \$22,818 ^a | \$0 |
| Plus: Operating Surplus | \$173,105 | \$37,382 |
| Total Ending Fund Balance | \$1,510,913 | \$1,548,295 |
| Less: Restricted Funds ^b | \$509,384 | \$459,384 |
| Less: Encumbrances | \$10,672 | \$5,806 |
| Less: Appropriated Fund Balance for the Ensuing Year | \$218,440 | \$60,000 |
| Total Unrestricted Funds at Year-End | \$772,417 | \$1,023,105 |
| Ensuing Year's Budgeted Appropriations | \$5,783,134 | \$5,424,054 |
| Unrestricted Funds as Percentage of Ensuing Year's Budget | 13% | 19% |
| ^a This adjustment was due to an authorized move of \$20,515 to the capital projects fund and an adjustment to write off \$2,303 of uncollected revenue from the previous year. ^b Restricted fund balance is composed of an unemployment insurance reserve of \$95,000, a reserve for compensated absences of \$164,194, a capital reserve of \$200,190 and a repair reserve of \$50,000, as of June 30, 2014. The repair reserve had a zero balance as of June 30, 2015. | | |

The District appropriated a cumulative total of \$278,440 of fund balance as a financing source in the annual budgets for 2014-15 and 2015-16. Due to the District's overly conservative budgetary estimates combined with the operating surplus in 2014-15, none of the appropriated fund balance was used that year. Additionally, based on our review of the 2015-16 budgetary estimates, we anticipate the District will also not use any of the fund balance it appropriated in 2015-16. When the appropriated but unused fund balance is added back, the District's recalculated unrestricted fund balance exceeds the statutory limit by 13 and 16 percentage points, respectively, as indicated in Figure 3.

| Figure 3: Unused Fund Balance | | |
|--|-------------|-------------|
| | 2013-14 | 2014-15 |
| Total Unrestricted Funds at Year-End | \$772,417 | \$1,023,105 |
| Add: Appropriated Fund Balance Not Used to Fund Ensuing Year's Budget | \$218,440 | \$60,000 |
| Total Recalculated Unrestricted Funds | \$990,857 | \$1,083,105 |
| Ensuing Year's Budgeted Appropriations | \$5,783,134 | \$5,424,054 |
| Recalculated Unrestricted Funds as a Percentage of Ensuing Year's Budget | 17% | 20% |

The District's last two independent audit reports contained findings related to the unrestricted fund balance being in excess of the statutory limit. However, District officials have not developed a corrective action plan to reduce the unrestricted fund balance to the allowed level. The Business Administrator provided us with documentation of Board discussions to address the fund balance issue through the

use and funding of reserves in the coming years. The Board adopted a policy on February 3, 2014 that states the District no longer requires fund balance to be maintained within the limits of the law. The Board President told us this was done in case of an emergency situation requiring immediate outlays of money that may take months to be reimbursed, if at all. However, there is no legal provision that allows retaining fund balance above the statutory limit. Additionally, the District is able to legally reserve moneys for various purposes in the event an emergency situation did arise and, as shown in Figure 2, has established and funded various reserves.

Had District officials used more realistic revenue and appropriation estimates, they could have avoided accumulating excess fund balance and reduced the tax levy. The District's practice of appropriating fund balance that is not actually used to finance operations in effect withholds public moneys without legal authorizations and gives the appearance that the District is returning a portion of excess funds to its taxpayers when that is not the case.

Recommendations

The Board should:

1. Adopt budgets that reflect the District's actual needs based on realistic revenue and appropriation estimates, taking into account historical trends and all available information.
2. Ensure that the amount of unrestricted fund balance is in compliance with the statutory limit.
3. Develop a plan to reduce the amount of unrestricted 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;
 - Funding needed reserves; and
 - Reducing District property taxes.

APPENDIX A

RESPONSE FROM DISTRICT OFFICIALS

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



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May 25, 2016

[REDACTED]
NYS Office of the State Comptroller
Division of Local Government and School Accountability
One Broad Street Plaza
Glens Falls, NY 12801

Dear [REDACTED]

The Owen D. Young Central School District is in receipt of the Draft Audit Report titled *Financial Condition* for the period of July 1, 2013 through September 30, 2015, prepared by the office of the State Comptroller. During the course of this audit, the Comptroller's Office conducted a comprehensive examination of the District's financial practices. We are pleased that no fraud, waste or abuse was identified by this examination. 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 Board of Education and District administration strive to maintain the highest standard of fiscal management, balancing the needs of the instructional program with the community's desires, aspirations and ability to pay. The District has been able to maintain an average tax increase of only 1.27% over the past eight years.

During the first year of this audit period the Board declared the District as being in a state of emergency due to the 2013 flood causing \$2 million in damages. It was during that time that the Board adopted a fund balance policy that would help alleviate monetary outlays because we were unsure of the reimbursement timeline. In December of 2015, the Board revised their fund balance policy.

The three budgeting areas cited in the report are all areas that are extremely difficult to predict. The Board and district officials feel that they were being fiscally responsible to the community in providing these estimates. BOCES refunds and net grant funds cannot be easily predicted historically. At any time an unforeseen circumstance could occur beyond the district's control and knowledge. For fuel prices, at any time during a year fuel price could climb without warning. The district will give the historical pricing a closer look at budget time.

Upon further review and analysis we shall develop a corrective action plan, which shall document how we intend to use the report to positively improve our operations, while taking into consideration the ever-increasing constraints that school districts face.

Thank you once again for your valuable feedback concerning our district's finances.

Sincerely,

Brennan Fahey
District Superintendent

APPENDIX B

AUDIT METHODOLOGY AND STANDARDS

Our overall goal was to assess the District's budgeting process. To accomplish our objective and obtain valid evidence, we interviewed District officials and employees, tested selected records and examined pertinent documents. We performed the following procedures:

- We interviewed District officials and employees to gain an understanding of the budget process and determine reasons for large revenue and expenditure variances.
- We examined the entire population of diesel fuel invoices to determine if the per-gallon cost estimate was reasonable.
- We reviewed District policies and procedures.
- We reviewed and analyzed reported fund balance levels in comparison to amounts appropriated in adopted budgets for fiscal years 2013-14 through 2014-15.
- We calculated the unrestricted fund balance as a percentage of the next year's budget.
- We compared budgeted revenues and appropriations to actual revenues and expenditures for the 2013-14 and 2014-15 fiscal years. We also compared the 2014-15 actual revenues and expenditures to the 2015-16 budgeted revenues and appropriations.

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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