



Clifton-Fine Central School District Financial Condition and Transportation Aid Claims

Report of Examination

Period Covered:

July 1, 2008 — June 30, 2010

2011M-213



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

January 2012

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 Clifton-Fine Central School District, entitled Financial Condition and Transportation Aid Claims. 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*



State of New York Office of the State Comptroller

EXECUTIVE SUMMARY

The Clifton-Fine Central School District (District) is governed by the Board of Education (Board) which comprises 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 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.

There is one school in operation within the District, with approximately 335 students and 90 employees. The District's budgeted expenditures for each of the 2008-09 and 2009-10 fiscal years were \$9.1 million, which were funded primarily with State aid and real property taxes.

Scope and Objectives

The objectives of our audit were to examine the District's financial condition and to review the procedures for claiming transportation aid from the State Education Department for the period July 1, 2008 to June 30, 2010. For trend analysis purposes, we examined financial statements and budget reports back to the 2005-06 fiscal year. Our audit addressed the following related questions:

- Does the Board properly manage District finances by preparing realistic budgets and by properly establishing and maintaining reserve funds with reasonable balances?
- Do District officials correctly report school bus mileage to the State Education Department for the purpose of calculating State transportation aid?

Audit Results

The Board needs to ensure that budget estimates are reasonable and that it establishes and maintains reserves in accordance with a comprehensive policy or plan. The Board should also provide District residents with the information they need to understand how their tax dollars are being used. District officials consistently overestimated expenditures for the past five years, by a total of \$4.5 million.¹ As a result, the District had operating surpluses totaling \$2.3 million in four of the last five years, and did not need to use the majority of the \$1.2 million of fund balance which the Board appropriated as a revenue source in the general fund budgets over the last five years. Despite its budgetary surpluses, the District also increased its real property tax levy by approximately \$300,000 – a total of 8 percent – over the last five years.

¹ 2005-06 through 2009-10 fiscal years

The District used its annual surpluses to increase various reserves' account balances. As of June 30, 2010, the District reported seven general fund reserves with balances totaling \$3.5 million. District officials did not adequately inform taxpayers about how the reserves were funded. The District overfunded four of these reserves.²

The District also needs to review its processes and procedures for filing its transportation State aid claims. We found that the District was not claiming all of its eligible miles for State aid. Therefore, the District was not collecting all of the transportation aid that it was eligible to receive. During the State aid years³ 2009-10 and 2010-11, the District potentially lost revenue of \$26,500 and \$23,000, respectively.

Comments of District Officials

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. Except as specified in Appendix A, District officials generally agreed with our recommendations and indicated they planned to take corrective action. Appendix B includes our comments on the issues raised in the District's response letter.

² The four overfunded reserves were the Workers' Compensation Reserve, Unemployment Reserve, Retirement Reserve and the Repair Reserve. All together, the balances in these reserves totaled \$2.4 million.

³ The State aid year covers services provided in the previous fiscal year (2009-10 State aid year includes the actual data from the District's 2008-09 fiscal year).

Introduction

Background

The Clifton-Fine Central School District (District) is located in the Towns of Clifton, Fine, Pitcairn and Russell in St. Lawrence County. The District is governed by the Board of Education (Board) which comprises 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 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 District contracts with the St. Lawrence-Lewis BOCES (BOCES) for finance related services through a shared services agreement. The BOCES shared Business Office provides the District with an Assistant Business Manager and two clerks to process business transactions.

There is one school in operation in the District, with approximately 335 students and 90 employees. The District's budgeted expenditures for each of the 2008-09 and 2009-10 fiscal years were \$9.1 million, which were funded primarily with State aid and real property taxes.

Objectives

The objectives of our audit were to examine the District's financial condition and the District's procedures for reporting transportation miles to the State Education Department for the period July 1, 2008 to June 30, 2010. Our audit addressed the following related questions:

- Does the Board properly manage District finances by preparing realistic budgets and by properly establishing and maintaining reserve funds with reasonable balances?
- Did District officials correctly report school bus mileage to the State Education Department for the purpose of calculating State transportation aid?

Scope and Methodology

We examined internal controls over financial condition as well as the processes and procedures for claiming transportation aid for the period July 1, 2008 to June 30, 2010. For trend analysis purposes, we examined financial statements and budget reports back to the 2005-06 fiscal year.

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 C 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. Except as specified in Appendix A, District officials generally agreed with our recommendations and indicated they planned to take corrective action. Appendix B 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 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

A school district's financial condition is a factor in determining its ability to provide educational services to students. The responsibility for accurate and effective financial planning rests with the Board, the Superintendent and the Assistant Business Manager. One of the most important tools for managing a district's financial condition is the budget process. District officials must ensure that budgets are prepared, adopted and modified in a prudent manner, accurately depicting the district's financial activity while also using available resources to benefit district taxpayers. Prudent fiscal management also includes maintaining sufficient balances in reserves that are needed to address long-term obligations or planned future expenditures. In doing so, district officials should adopt a policy or plan governing the use of reserve funds and ensure that residents are fully informed of all reserve funding and activity.

District officials consistently overestimated expenditures for the past five years by a total of \$4.5 million. As a result, the District had operating surpluses totaling \$2.3 million in four of the last five years. Therefore, the District did not need to use the majority of the \$1.2 million of fund balance that the Board had appropriated as a revenue source in the general fund budgets. District officials used most of these annual surpluses to fund reserves. District officials made transfers to reserves at the end of each fiscal year, rather than including the transfers in voter-approved operating budgets. Furthermore, while District officials did include moneys from certain reserve funds as financing sources in the operating budgets, they did not actually use any of the designated amounts. As of June 30, 2010, the District reported seven general fund reserves with balances totaling \$3.5 million.

Budgeting and Fund Balance

The Board is responsible for preparing and presenting the District budget to the public for vote. In preparing the budget, the Board is responsible for estimating what the District will receive in revenue (e.g., State aid), how much fund balance will be available at fiscal year-end (some or all of which may be used to fund the ensuing year's appropriations) and, to balance the budget, what the expected tax levy will be. Accurate estimates help ensure that the levy of real property taxes is not greater than necessary.

There are three components of fund balance. Reserved fund balance represents moneys that the District has set aside and may only use for specific purposes, as authorized by statute. Unreserved fund balance represents uncommitted funds and therefore may be used

(appropriated) to fund the ensuing year’s expenditures, thereby reducing the tax levy. The portion of the unreserved fund balance that the District retains, which can be used for cash flow purposes and unanticipated expenditures, is referred to as unreserved, unappropriated fund balance. Real Property Tax Law currently limits the amount of unreserved, unappropriated fund balance to no more than 4 percent⁴ of the ensuing fiscal year’s budget. Any fund balance over this percentage should be used in a manner that benefits District taxpayers.

We compared the District’s budgeted revenues and expenditures with actual results of operations for the last five fiscal years and found that the District has overestimated expenditures by a total of \$4.5 million, as shown on the following table.

Table 1: Budget to Actual						
	FY 2005-06	FY 2006-07	FY 2007-08	FY 2008-09	FY 2009-10	Total
Appropriations ^(a)	\$8,211,728	\$8,420,281	\$8,850,992	\$9,143,342	\$9,124,556	\$43,750,899
Actual Expenditures	\$7,592,313	\$7,728,386	\$8,145,429	\$7,598,737	\$8,137,152	\$39,202,017
Over-Budgeted Expenditures	\$619,415	\$691,895	\$705,563	\$1,544,605	\$987,404	\$4,548,882
^a Does not include encumbrances. (Encumbrances are commitments for payments related to unperformed contracts for goods or services.)						

District officials were unable to provide reasonable justification for some of these unrealistic estimates. For example:

- District officials consistently overestimated expenditures including electricity and transportation over the last two completed fiscal years by an average of 39 percent and 27 percent, respectively.
- District officials significantly overestimated costs for payments to the employee and teachers retirement systems over the last two completed fiscal years by an average of 39 percent and 43 percent, respectively. The Assistant Business Manager stated that she based her estimates on prior year budgeted numbers rather than actual results.

⁴ In July 2007, legislation was enacted to change the Real Property Tax Law statutory limit of unappropriated, unreserved fund balance to 3 percent of the 2007-08 fiscal year’s budget and 4 percent of the 2008-09 fiscal year’s budget and for years after. Prior to this, the limit was 2 percent.

- District officials significantly overestimated costs for interest on debt service payments for the last two completed fiscal years by 58 percent and 43 percent, respectively, even though annual interest on debt service is established per debt service schedules and is a fixed amount. The Assistant Business Manager said that she does not get the debt schedule from the financial advisors before the budget is prepared.

The District has appropriated fund balance in four of the last five years to reduce the tax levy, which should have resulted in planned operating deficits. However, because the District has consistently overestimated expenditures, the District has instead experienced operating surpluses in four of the last five years, with actual revenues exceeding actual expenditures by \$2.3 million.

Table 2: Operating Surplus						
	FY 2005-06	FY 2006-07	FY 2007-08	FY 2008-09	FY 2009-10	Total
Actual Revenues	\$7,582,302	\$8,369,350	\$8,208,705	\$8,679,599	\$8,687,012	\$41,526,968
Actual Expenditures	\$7,592,313	\$7,728,386	\$8,145,429	\$7,598,737	\$8,137,152	\$39,202,017
Operating Surplus/ (Deficit)	(\$10,011)	\$640,964	\$63,276	\$1,080,862	\$549,860	\$2,324,951
Appropriated Fund Balance at Year End	\$400,000	\$400,000	\$267,521	\$0	\$145,681	\$1,213,202
Unreserved, Unappropriated Fund Balance at June 30	\$317,257	\$498,879	\$991,088	\$1,744,491	\$700,938	
Percentage of Fund Balance Over Statutory Limit	1.76%	3.62%	7.84%	15.12%	3.87%	

During the same period, although revenues exceeded expenditures in four of the last five fiscal years, the Board increased the tax levy each year from \$3.5 million in 2005-06 to \$3.8 million in 2009-10, a total increase of over 8 percent. Although the District’s adopted budget for 2010-11 – in contrast to the previous five years – indicates no increase in the tax levy, the District’s budgeting practices are still likely to result in withholding excess moneys that could be used productively – for example, to pay off debt, finance one-time expenses, reduce property taxes or increase necessary reserves.

These increases occurred even though the District’s last five independent audit reports contained a finding related to the District’s unreserved, unappropriated fund balance being in excess of the statutory limit. Budgeting practices which produce operating surpluses that are retained in excess of the amount allowed by law do

not provide adequate accountability to taxpayers regarding the use of their resources.

Reserves

Reserve funds may be established by Board action, pursuant to various laws, and are used to provide financing only for specific purposes, such as unemployment insurance and workers compensation payments. The statutes under which the reserves are established determine how the reserves may be funded, expended or discontinued. Generally, school districts are not limited as to how much money can be held in reserves. However, it is important that school districts maintain reserve balances that are reasonable. To do otherwise, that is, funding reserves at greater than reasonable levels, essentially results in real property tax levies that are higher than necessary.

A governing board that establishes and funds reserves on a regular basis should adopt a written policy that communicates its rationale for establishing reserve funds, objectives for each reserve established, optimal or targeted funding levels, and conditions under which the funds' assets will be used or replenished. Reserve fund transactions should be transparent to the public. Reserve funds are typically funded from amounts raised through the annual budget process, transfers from unexpended balances of existing appropriations, and surplus moneys. Ideally, amounts to be placed in reserve funds should be included in the annual budget and they should not routinely be funded at year-end through excess fund balance.

Making provisions to raise resources for reserve funds explicit in the proposed budget gives voters the opportunity to know the Board's plan for funding reserves, which increases transparency. When appropriations for transfers to reserves are not anticipated in the annual budget, a Board resolution is generally necessary to authorize the transfer of unexpended balances or surplus money into a reserve fund. The resolution should include specifics about the amount to be transferred and the reserve fund to be credited. These resolutions help promote visibility of the Board's actions to taxpayers. The Board has not adopted any written policies regarding the establishment and use of reserve funds.

District officials have used a portion of their annual operating surpluses to fund various reserves.⁵ As of June 30, 2010, the District had seven reserves in the general fund with reported balances totaling approximately \$3.5 million. The District's reserve account balances

⁵ These reserves and balances were a retirement contribution reserve for \$1,002,492, a reserve for Tax Certiorari for \$933,421, a repair reserve for \$514,000, a workers' compensation reserve for \$450,579, an unemployment reserve for \$438,885, a reserve for compensated absences for \$143,720, and a reserve for tax reduction for \$20,333.

nearly tripled from 2005-06 to 2009-10, going from \$1.2 million as of June 30, 2006 to \$3.5 million as of June 30, 2010.

The Board's resolution lacked adequate specific direction to the Superintendent. The resolution stated that the "Board of Education authorizes the funding of appropriated reserves with excess fund balance that exceeds 4 percent." It is the Board's responsibility to identify specific amounts or maximum amounts of excess fund balance that it is authorizing the Superintendent and/or Assistant Business Manager to transfer into specifically named reserve funds, rather than to provide for an open-ended delegation to the Superintendent to make transfers of excess fund balance in his or her discretion. As a result, four of the District reserves are overfunded.

Unemployment Insurance Reserve – General Municipal Law (GML) authorizes districts to create this type of reserve to reimburse the State Unemployment Insurance Fund for payments made to claimants. While the Board authorized increasing this reserve, District officials were unable to provide us with the Board resolution establishing this reserve.⁶ This reserve had a reported balance at June 30, 2010 of \$438,885,⁷ which is much larger than necessary. While the District incurred unemployment expenses of \$12,600 in fiscal year 2008-09 and \$5,606 in 2009-10, they did not charge this expense to this reserve. Instead, these expenses were paid out of the general fund. Furthermore, the average annual expense for the last five years was only \$6,543. Based on this cost level, the District's current reserve balance would cover unemployment insurance claims for approximately 67 years.

Workers' Compensation Reserve – GML authorizes the District to establish a reserve fund to pay for workers' compensation benefits, medical, hospital or other expenses, and the expenses to administer a self-insurance program. The Board established this reserve in May 2010 for \$450,579. We determined that this reserve balance is larger than necessary. The District incurred average workers' compensation expenses of approximately \$36,000 over the last five years. Based on this cost level, the District's current reserve balance will cover workers' compensation claims for approximately 12.5 years.

⁶ The moneys already in the reserves may constitute de facto reserves. De facto reserve is a legal concept where the courts have said that public policy behind the statute is to protect taxpayers from public officials who would shift funds away from an approved purpose and misuse them as an unlawful accumulated surplus to hide deficit spending or to reap political profit. The courts have indicated that a persistent course of conduct in treating and characterizing these funds as reserves is sufficient to keep anyone from trying to say there are not reserves at this point.

⁷ In addition to interest earned, the District increased this reserve by \$325,359 during 2009 and 2010.

Retirement Contribution Reserve – GML restricts the use of this reserve to payments to the New York State and Local Retirement System. In May 2010 the Board passed a resolution increasing the balance in this reserve from approximately \$506,000 to \$535,000. However, the Assistant Business Manager and Interim Superintendent increased the reserve balance to \$1 million and thus exceeded the delegation of authority given by the Board’s May 2010 resolution. Furthermore, the Board consistently budgeted for these contributions each fiscal year but paid contributions directly from the general fund. In effect, the Board levied real property taxes to make these annual contributions while increasing the reserve. Over the last two years, no moneys were used from the retirement contribution reserve to pay for the District’s contributions. Furthermore, this level of funding will cover the District’s retirement expense for approximately 10 years.

Building Repair Reserve – GML authorizes the District to establish a reserve fund to pay for certain repairs to capital improvements or equipment. The type of repairs must not recur annually or at shorter intervals. The Board passed a resolution in June 2010 establishing and funding a Repair Reserve with fund balance above 4 percent. At year end the District ultimately funded this reserve with \$514,000. District officials developed a list of repairs to provide support for the reserve. However, the list predominately included items that constituted capital improvements rather than repairs. This has resulted in the over funding of the repair reserve by \$274,300. The Assistant Business Manager told us that the District decided to create the repair reserve rather than a capital reserve because they could do so by a Board resolution rather than a public vote. However, this is incorrect. The State Education Department advises school districts to present repair reserves to a public vote.

Tax Certiorari Reserve – Education Law authorizes districts to establish a reserve fund for the payment of judgments and claims for tax certiorari proceedings for the tax roll in the specific year in which the money was deposited in the reserve. Education Law further provides that moneys held in such a reserve fund may not exceed the amount which might reasonably be deemed necessary to meet anticipated judgments and claims arising out of tax certiorari proceedings. This law also requires that moneys not used as intended to pay judgments and claims must be returned to the general fund within four years of the day that they were deposited into the reserve.

The District funded this reserve with two Board resolutions. The first resolution established the reserve for \$125,000. The second resolution was a blanket statement authorizing the funding of reserves with excess fund balances that exceed 4 percent. This resolution lacked adequate direction to the Superintendent and Assistant Business

Manager. It is the responsibility of the Board to identify specific amounts of fund balance to transfer into specifically named reserve funds rather than provide for an open ended delegation. The District does not appear to have any reasonable basis for how it funded the tax certiorari reserve account.

In addition, the majority of all transfers of unappropriated fund balance to reserves were completed in June, instead of being included in the adopted budget. Therefore, these unbudgeted transfers to fund reserves were made without prior communication to and approval by the voters. Failure to plan ahead for the use of reserve funds and to clearly and accurately communicate both those plans and the actual use of reserve funds, to Board members and voters alike, raises concerns about the due diligence exercised by the Board and District officials in managing District resources.

The failure to adopt realistic budgets and properly establish and maintain only necessary reserves has resulted in the accumulation of a significant amount of resources. During our audit period the District transferred \$1.8 million of the District's annual tax levy into reserve funds without transparency to the voters. It is clear that the District was funding reserves in an attempt to keep fund balance within the statutory limit. Had the District reported these moneys as general fund unreserved balance, real property taxes could have been reduced. The Board should clearly state how it plans to use these significant resources in a Board Policy or Plan, and the Board should clearly inform District taxpayers about these plans during the budget adoption and voting process.

Recommendations

1. The Board and District officials should develop realistic expenditure and fund balance estimates for the annual budget.
2. District officials should develop comprehensive policies related to the establishment and use of reserve funds. These policies should outline the optimal or targeted funding levels and the conditions under which the funds will be used or replenished.
3. When establishing or funding reserves, the Board should adopt resolutions identifying specific amounts to be transferred into specific reserve funds.
4. The Board and District officials should review all reserves and determine if the amounts reserved are necessary, reasonable and in compliance with statutory requirements.

5. District officials should include both the funding and use of all reserves in their adopted budget plan each year to provide increased knowledge and transparency for the District's voters.
6. District officials should present the repair reserve to the public for vote.
7. District officials should transfer excess moneys from the repair reserve to a properly established capital improvement reserve subject to voter approval.
8. District officials should develop a plan for the use of the surplus balances in unreserved, unappropriated fund balance and in the District's reserve funds identified in this report in a manner that benefits District taxpayers. Such uses could include, but are not limited to:
 - Paying off debt
 - Financing one-time expenditures
 - Reducing District property taxes
 - Increasing necessary reserves.

Transportation Aid Claims

In the current economic environment, it is important for school districts to ensure they are collecting all available revenues. State Education Law provides for the reimbursement to school districts of a portion of allowable expenses incurred in transporting students. The law defines which expenses are⁸ and are not⁹ eligible for aid. To assist school districts in determining which costs are allowable, the State Education Department (SED) has prepared a Transportation Aid Guide for their use. One of the factors included in the transportation aid formula is the number of miles traveled by the District's buses. On the aid form, the District's mileage is divided into several categories. The categories include, but are not limited to, miles for regularly scheduled routes, annual mileage for District operated summer school and annual mileage for other purposes excluding summer school. In order for the District to ensure it is optimizing its transportation aid revenue, it must ensure that all of its miles are being properly classified.

District managers have not established processes and procedures for preparing and reviewing State aid claims to ensure that they are properly completed. Consequently, District managers made significant errors in reporting school bus mileage to SED during the two years we audited.¹⁰ Most notably, the District was recording its late bus runs as mileage for other purposes rather than miles for regularly scheduled routes. In the 2009-10 State aid year,¹¹ the District properly reported 129 late bus run miles but incorrectly reported 14,600 late bus run miles. Similarly, in the 2010-11 aid year, the District properly reported 108 late bus run miles but incorrectly reported 16,542 late bus run miles. In total, for the 2009-10 State aid year, the District reported regular route mileage of 86,956 when they were eligible to report 99,122 miles. Similarly, in the 2010-11 State aid year the District originally reported 105,181 regular route miles when they were eligible to report 121,733. As a result, the District received approximately \$26,500 less in transportation aid than they were eligible for in 2009-10 and \$23,000 less in 2010-11.

⁸ Miles that are eligible for aid include but are not limited to regular before- and after-school runs, BOCES, special-education and late bus runs.

⁹ Ineligible miles include but are not limited to field trips and sporting events.

¹⁰ We reviewed the District's aid documentation for the 2007-08 fiscal year and determined that they made the same errors on the transportation aid forms during this year.

¹¹ The State aid year covers services provided in the previous fiscal year (2009-10 State aid year includes the actual data from the District's 2008-09 fiscal year).

Recommendations

9. District management should file an amended transportation aid form for the 2010-11 fiscal year with the correct mileage numbers in order to maximize transportation aid for the District.
10. District management should establish procedures for preparing and reviewing State aid claims to ensure that they are properly completed.

APPENDIX A

RESPONSE FROM DISTRICT OFFICIALS

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



Clifton-Fine Central School – District Office

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January 2, 2012

Office of the State Comptroller
State Office Building, Room 409
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Syracuse, New York 13202-1428

To the Office of the State Comptroller:

Please accept this letter as the official response from the Clifton-Fine Central School District regarding the Draft Audit Report "Financial Condition and Transportation Aid Claims" for the period July 1, 2008 – June 30, 2010 conducted by your office. On behalf of the Board of Education and the District's administration, we would like to thank the local field staff of the Comptroller's office. The exit interview was the only portion where current administration was involved, but that meeting was found to be very congenial and informative. The District welcomes the feedback provided by the Comptroller's office and appreciates the opportunity to strengthen our practices as a result of reflection on that feedback.

The District is pleased that the draft report does not suggest any malfeasance or legal impropriety with respect to the District's general business operations. We have carefully reviewed the findings and recommendations presented both internally as well as with our outside independent financial advisors. To the extent that the Comptroller's audit represents an examination of the District's business operations and statutory and regulatory compliance, we appreciate this opportunity to review our financial management practices and oversight. As will be outlined in our Corrective Action Plan, we will take appropriate corrective action in certain areas.

However, the audit report contains a number of conclusions and broad statements that we believe reflect subjective opinions of the Comptroller's office with respect to the District's financial management specifically as they relate to financial planning, reserve funds, and fund balance management. In reviewing the recommendations, we carefully considered your perspective. That being said, the elected Board of Education and the District's administration firmly believe that our overall approach to financial management is consistent with our legal authority under both the Education and General Municipal laws and accompanying regulations; and is consistent with our fiduciary responsibility to our taxpayers, students, and employees.

Clifton-Fine students will have the skills and confidence necessary to compete in a global society.

ADMINISTRATION

Denise Dzikowski, Superintendent • Susan Shene, PK-12 Principal • Patty Smithers, Business Mgr. • Anne Hanley, District Clerk • Tim Redmond, Facilities Director
• Darren Bullard, Transportation Director

BOARD OF EDUCATION

Roxy Silsby, President • Michelle Durham, Vice President • Mary Fraser, Board Clerk • Brian Dolan • Denise Folsom • Richard Hitchman • Robert Tebo, III



Clifton-Fine Central School – District Office

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We are concerned that the overall tone of the audit report seems inconsistent with the philosophy set forth by the Comptroller’s office itself in the guidance document *Local Government Management Guide – Reserves*. (LGMG). That document states:

See Note 1 Page 24

In our personal lives, saving or putting money aside to finance future needs is a common practice. Unquestionably, strong arguments can be advanced for accumulating funds. The disputable policy “live for today and let tomorrow take care of itself” can easily be refuted with many savings slogans such as “prepare for a rainy day”.

These practices are equally important for New York’s local governments. Legally established reserves can provide many benefits to municipalities and their citizens. Available moneys can be set aside to finance all or part of planned projects, thereby reducing the need to issue costly debt. Reserves can provide a degree of financial stability. In certain economic times, reserve funds may give managers options other than cutting services or raising taxes. In good times, moneys not needed for current purposes can often be set aside for future benefit. (LGLG – at p. 1, emphasis added).

The guidance goes on to state the following:

Municipalities, like any other entity, need to accumulate funds for future contingencies. However, if the adopted budget is on the mark total revenues plus appropriated fund balance would equal total expenditures with a zero fund balance remaining at the end of the fiscal year, leaving nothing to accumulate. In accordance with some statutes, many municipalities may include in their budgets an amount for estimated unappropriated, unreserved fund balances for each fund. Such estimate may not exceed a reasonable amount, consistent with prudent budgeting practices, necessary to ensure the orderly operation of the government (see Town Law § 107[1][b], Village Law § 5-506 [1][c], and County Law § 355 [1][g]).

See Note 2 Page 24

Fortunately, municipalities are not precluded from setting aside and accumulating funds. This is accomplished by establishing reserve funds, which provide a means for raising money today, investing it and spending the money and earnings in the future. The decision to establish reserve funds, other than “mandatory” reserves, is left up to the governing board of each municipality. The purpose of the chapter is to offer a reference document on legally authorized reserve funds. Hopefully, it will serve to acquaint officials with legal requirements so that the establishment and use of reserve funds comply with the law. (LGMG – at p. 2, emphasis added).

Clifton-Fine students will have the skills and confidence necessary to compete in a global society.

ADMINISTRATION

Denise Dzikowski, Superintendent • Susan Shene, PK-12 Principal • Patty Smithers, Business Mgr. • Anne Hanley, District Clerk • Tim Redmond, Facilities Director
• Darren Bullard, Transportation Director

BOARD OF EDUCATION

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It is with these principles in mind that we have considered, and now respond to the various recommendations.

Comptroller Recommendation No.1

The budget is the most thoroughly reviewed and most important financial document in the District. Throughout the report the Comptroller suggests that the District be more realistic when estimating fund balance and appropriations when preparing its budget, which would conceivably lower taxes.

The District believes in conservatively estimating revenues and expenses which stabilize taxes, trying to establish a consistently low level of tax increases rather than creating a fluctuating tax rate that would burden our tax payers and consequently impact constituent support and related items such as our bond rating. Through these budgeting practices the District’s goal is to be able to provide its taxpayers a level of consistency and predictability. Over the last five years the District has averaged a tax increase of 1.6% per year. In contrast, the C.P.I. over that same time frame has averaged 2.2%. We also currently, and for the past several years, have the second lowest tax rate in the St. Lawrence-Lewis BOCES.

Insofar as overestimating budgetary appropriations, the Comptroller’s report suggests the Board of Education does not effectively estimate its annual spending plan. Estimates of expenditures are based on facts known at the time of budget planning and adoption. Unfortunately, events occur subsequent to the Board adoption date that results in a decrease in expected expenditures that cannot be adjusted. There are a number of factors during budget planning that impact expenditure estimates. As information becomes available it is incorporated and accurate figures replace estimates.

See
Note 3
Page 24

We have a very transient student population. For example, just this past school year we ended with a total population of 348 students. We opened with 321. The materials and supplies that had been budgeted to be used throughout the course of the year are of course not going to be ordered now for students who are no longer here. There are also great fluctuations in the cost of items such as electricity and fuel that occurs each year depending on the markets. We take a very cautious and conservative approach to estimating appropriations for students with special needs. Just one or two students transferring into the District with specialized needs in transportation, out of District placement, 1:1 aides, etc. can be financially devastating to a District of our size if not prepared and these types of costs typically have no offsetting revenue in the enrollment year to cover the cost of such needs.

The most volatile and extensive portion of the budget is employee benefits. Health care costs are not finalized until after the budget adoption. In addition, these costs have been very unpredictable over the past few years, causing the District to estimate accordingly. In our recent contract settlement the District has been able to secure a

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contribution toward the cost of the employee’s insurance costs and this should assist us with better controlling the total amount. In addition to the health care costs, the District is challenged to cover pension costs, which we also have no control over. These areas require a conservative approach with their potential for dramatic increases that have significant budgetary impact.

The Comptroller’s report also pointed out the district doesn’t end up using the appropriated fund balance as a revenue source. Although we do not dispute that fact, we feel our budgeting practices are fiscally responsible and as indicated by our tax levy increase history, is in the best interest of the taxpayers. One of the primary reasons this has occurred is due to underestimated revenues from State Aid and interest income. There are solid reasons for our estimates in those two areas. With regard to State Aid, the number reported on various State budget runs is never equal to the actual State Aid received by the District. Actual State Aid is always lower, and is heavily dependent upon enrollment, which has steadily been declining here over the past 10 years. We follow the State Education Department recommended budget calendar, which historically hasn’t allowed for an approved State budget figure for school aid until after our Board has adopted the budget. Furthermore, some State aid revenue, like BOCES and transportation aid is expense driven. Exact aid amounts are difficult to estimate and the District must protect against potential deficits. BOCES aid is traditionally a major discussion item for reduction or freezing during the State budget process.

In light of the extremely turbulent fiscal condition of New York State and the potential for large decreases in State Aid that all school Districts are facing, the budgeting practices exercised by the District appear prudent and fiscally responsible. It is true that these practices have resulted in budgetary surpluses. However, the surplus was utilized to fund reserves and has been and will continue to be used, in even greater amounts based upon an increased need, in subsequent years as budgeted revenue.

Comptroller Recommendation No. 2, No. 3

The District will establish a policy to conduct an annual review of all reserve funds as a part of the budget process. During this review the Audit Committee will review a listing of each reserve and the funds therein, learn of any payments made from each reserve in the recent past, receive a briefing on the status related to each reserve and any limits on funding or spending the amounts, and receive an analysis of the projected needs for the reserves in the upcoming fiscal year in order to make a recommendation on how to fund those needs. All resolutions now identify specific amounts to be transferred to reserves.

Comptroller Recommendation No. 4 & No. 5

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These recommendations seem to imply that the Board of Education and District Administration have not been appropriately overseeing the financial management of the District’s reserves. We can assure that this is not the case at all. The Board of Education and Administration review the reserve amounts on a regular basis and consider the overall financial picture of the District when funding such reserves and setting the tax levy. A five-year plan is now in place that takes into account upcoming retirements as well as projected needs in other areas. A trend analysis has been completed to look at the use of Worker’s Compensation as well as Unemployment and projections for staff reduction have been included in the analysis. A review of our bond prospectus shows that our rating for long term debt financing enjoys an outstanding rating for a school of our size and poverty. A factor in this rating is the existence of our reserve funds. Thus the assertion that we did not think of District taxpayers when we established reserves belies the reality of our actions. Because we have the reserves, the net result is lower borrowing costs to our taxpayers, which has the net effect of reducing property taxes. The District includes all available information in the budget plan. As reserves are a part of the revenue stream and not the expenditure side of the budget, that information isn’t readily available at the time of the budget adoption, but it is reviewed and openly discussed during the Board’s process of establishing the levy.

See
Note 4
Page 24

Comptroller Recommendation No. 6, No. 7

The District believes that all of the reserve funds have been established and maintained as per regulations in General Municipal Law § 6 and Education Law § 3651. As the Repair Reserve is not a funded reserve, there is nothing in regulation that indicates the District is required to present the reserve for a public vote. The Board of Education and District Administration see no upcoming requirement for a Capital project, thus they have chosen to designate the reserve for the purpose of repairs rather than for Capital Improvements.

See
Note 5
Page 24

Comptroller Recommendation No. 8

The District feels as though it does in fact use surplus in ways that are beneficial to taxpayers. Surplus has been used to increase necessary reserves, finance one-time expenditures, and reduce property taxes. In fact, the District’s tax levy has remained flat or experienced modest increases over the past five school years.

Comptroller Recommendation No. 9

The District will ensure any amendments possible have been made to maximize transportation aid.

Comptroller Recommendation No. 10

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The District has established updated procedures and made software adjustments to ensure that the maximum aid possible is claimed.

Conclusion:

In conclusion, the Clifton-Fine Central School District appreciates the feedback provided by the Comptroller’s office and views this as an opportunity to improve upon our financial practices. The Board of Education and new administration is committed to taking appropriate action to correct, clarify, and/or strengthen our operating procedures in those areas of concerns that were noted, and to fully comply with State regulations.

While respectfully acknowledging that the Comptroller has, from a policy perspective, taken issue with certain aspects of the District’s fiscal approach, the District maintains that its primary financial objective is to minimize the cost of delivering a high quality education to our students. The District’s current budgeting practice and management of its fund balance and reserves is conducted in furtherance of this objective and has resulted in, by any measure, a high achieving school District within our region of the state, along with the second lowest tax rate within our BOCES.

The District has already begun to implement the recommendations specified in the audit document. Our Board of Education Audit Committee along with District administration will work to complete the corrective action plan within the given timeline and forward to the appropriate parties. Thank you for the opportunity to review and respond to these recommendations.

Sincerely,

Denise L. Dzikowski
Superintendent of Schools

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APPENDIX B

OSC COMMENTS ON THE DISTRICT'S RESPONSE

Note 1

We disagree that our audit report is inconsistent with the philosophy set forth in the LGMG on reserves. Reserves are important and they play a large role in the District's ability to budget and plan for future contingencies. However, they are meant to be used as a planning tool. The District should have a multi-year financial plan in place that outlines how it plans to fund and use the reserves. It is not appropriate for the District to simply increase reserves through year-end adjustments with minimal communication to taxpayers.

Note 2

Towns, villages, and counties are permitted by law to retain a "reasonable amount" of unappropriated, unreserved fund balance for each fund, consistent with prudent budgeting practices, necessary to ensure the orderly operation of their government. School districts, however, are limited to retaining 4 percent¹² of the current school budget in unreserved, unappropriated fund balance. The District regularly exceeded the statutory limit.

Note 3

Our review of the District's budgeting practices disclosed that the District did not always use available data when developing its budget, which resulted in significant budget variances in certain appropriation accounts. For example, the District developed some budget estimates by reviewing prior year budgeted numbers rather than prior year actual numbers. Using prior year actual numbers typically provides a more accurate guideline. In addition, the District did not utilize debt service schedules when budgeting debt interest costs. We encourage the District to adopt budgets that reflect the District's actual needs.

Note 4

The District has not been incorporating the funding of its reserves or the use of these funds within its annual budget. Instead, the District has been funding its reserves at the end of the fiscal year as a reactionary measure to deal with the annual operating surplus. The District should include both the funding and use of its reserves within its annual budgets as well as its long-range financial management plans.

Note 5

The District indicates in its response that the repair reserve is not a funded reserve. However, the repair reserve had a reported balance of \$514,000 at the end of their 2009-10 fiscal year, so the District has funded this reserve. The District also indicates that it is not required to present such a reserve

¹² Real Property Tax Law limits school districts' unappropriated, unreserved fund balance to 3 percent of the 2007-08 fiscal year's budget and 4 percent of the 2008-09 fiscal year's budget and for years after. Prior to this, the limit was 2 percent.

for public vote. Our Office has previously expressed the opinion that the use of surplus moneys by a school district to fund a repair reserve fund would not constitute an ordinary contingent expense and, therefore, would require voter approval (Op St Comp No. 81-401).

APPENDIX C

AUDIT METHODOLOGY AND STANDARDS

The objectives of this audit were to review the financial condition of the District and to identify transportation revenue enhancements. To achieve our audit objective and obtain valid audit evidence, we performed the following audit procedures:

- We interviewed District officials to obtain an understanding of the District's internal controls over financial condition, budgeting, use of reserve funds, and the District's processes and procedures for submitting for transportation aid.
- We compared budgets with actual results for the two fiscal years 2008-09 and 2009-10, to assess whether the budgets were realistic and supported. We also reviewed the fiscal years 2005-06 through 2007-08 to determine the District's budgeting trends.
- We reviewed Board minutes, Board resolutions, accounting records, audited financial statements, applicable statutes, and activity within the reserves to determine if reserves were properly established, funded and used.
- We evaluated the method of funding the reserves currently in place, as well as the level of fund balance remaining as unreserved and unappropriated in the general fund, to determine whether the District complied with applicable statutes.
- We contacted SED and reviewed their transportation guide to obtain an understanding of the transportation aid process.
- We examined 15 bus routes to determine the reasonableness of the transportation mileage submitted by the District for transportation aid. Our sample included some long routes, some short routes, some regular runs and some sports runs from both fiscal years under review.
- We compared the number of miles the District submitted to SED for transportation aid to the number of miles they were eligible to report.
- We entered the number of eligible miles into the transportation formula aid output report calculation to determine the amount of revenue the District lost by incorrectly submitting transportation miles.

We conducted this performance audit in accordance with generally accepted government auditing standards (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 objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

APPENDIX D

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