



Croton-Harmon Union Free School District

Budgeting Practices

Report of Examination

Period Covered:

July 1, 2010 — August 31, 2011

2011M-269



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

February 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 Croton-Harmon Union Free School District, entitled Budgeting Practices. This audit was conducted pursuant to Article V, Section 1 of the State Constitution and the State Comptroller's authority as set forth in Article 3 of the General Municipal Law.

This audit's results and recommendations are resources for district officials to use in effectively managing operations and in meeting the expectations of their constituents. If you have questions about this report, please feel free to contact the local regional office for your county, as listed at the end of this report.

Respectfully submitted,

*Office of the State Comptroller
Division of Local Government
and School Accountability*

Introduction

Background

The Croton-Harmon Union Free School District (District) is located in the Village of Croton-on-Hudson, Westchester County, and serves students in parts of the Towns of Yorktown and Cortlandt. 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 is the District's chief executive officer and is responsible, along with other administrative staff, for the day-to-day management of the District under the direction of the Board.

There are three schools in operation in the District, with approximately 1,760 students and 270 employees. The District's budgeted expenditures for each of the 2010-11 and 2011-12 fiscal years were \$43.86 million, funded primarily with State aid, real property taxes, and grants.

Objective

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

- Did the Board accumulate excessive fund balance by overestimating expenditures?

Scope and Methodology

We previously audited the District in 2008 (Report 2008M-94) and followed up on purchasing, information technology and fund balance issues which were addressed in that audit. The District has implemented corrective action relating to purchasing and information technology and we found those areas to be of limited risk. Also, due to the District's size and comparatively small number of employees in the Business office we examined internal controls and found them to be operating effectively. We therefore concentrated on the District's fund balance and related budgeting practices for the period July 1, 2010 to August 31, 2011. We extended our scope to the 2008-09 fiscal year to analyze budgeting and fund balance trends.

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 B of this report.

Comments of District Officials and Corrective Action

The results of our audit and recommendations have been discussed with District officials and their comments, which appear in Appendix A, have been considered in preparing this report. District officials

generally agreed with our recommendations and indicated that 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) 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.

Budgeting Practices

The Board and District officials are accountable to District taxpayers for the use of District resources, and are responsible for effective financial planning and management of District operations. The Board and Superintendent are also responsible for ensuring that budgets are prepared, adopted, and amended based on reasonable estimates of expenditures and revenues. Real property tax law (RPTL) requires unassigned¹ fund balance to be no more than 4 percent of the next fiscal year's budget.

In 2008, the Office of the State Comptroller audited the District and found that the District had more than double the unassigned fund balance permitted by law.² Although the report recommended keeping the unassigned fund balance within legal limits, the Board has failed to do so. Since then, the Board and District officials repeatedly overestimated expenditure items, which resulted in the continued accumulation of unassigned fund balance at year-end in excess of what is permitted by the RPTL.

Expenditure Projections

The Superintendent and Board must ensure that budgets are prepared based on realistic projections/estimates and on the most current and accurate information available. Budgeting practices which result in the retention of fund balance in excess of the amount allowed by law places an unnecessary burden on District taxpayers.

The Board routinely overestimated expenditures in the District's annual budget. During the 2008-09 to 2010-11 fiscal years, expenditures were over estimated by a total of approximately \$12.3 million. We found numerous examples of overestimated appropriations. Although the Board and District officials knew that certain expenditures had been overestimated in previous budgets, they continued to allocate excessive funds to these line items in the 2011-12 budget. Table 1 shows four budget line items: employee health benefits, social security payments, teacher retirement contributions, and BOCES services that indicate a trend in overestimating budget line items annually.

¹ Prior to June 2011, unassigned fund balance was referred to as unappropriated fund balance. This change occurred after implementation of GASB 54.

² During the previous audit, RPTL permitted 3 percent of the ensuing year's budgetary appropriations to be retained.

Table 1: Overestimated Budget Items			
Employee Health Benefits			
Fiscal Year	Budget	Actual	Excess
2008-09	\$2,313,660	\$1,737,189	\$576,471
2009-10	\$2,964,117	\$2,584,597	\$379,520
2010-11	\$2,806,076	\$2,726,137	\$79,939
2011-12	\$2,915,454		
Employee Social Security			
Fiscal Year	Budget	Actual	Excess
2008-09	\$1,504,740	\$1,504,700	\$40
2009-10	\$1,655,729	\$1,469,478	\$186,251
2010-11	\$1,994,538	\$1,511,293	\$483,245
2011-12	\$2,228,210		
Teachers' Retirement			
Fiscal Year	Budget	Actual	Excess
2008-09	\$1,125,670	\$1,097,962	\$27,708
2009-10	\$1,147,699	\$893,705	\$253,994
2010-11	\$1,832,706	\$1,291,431	\$541,275
2011-12	\$2,193,975		
BOCES Services			
Fiscal Year	Budget	Actual	Excess
2008-09	\$1,866,700	\$1,654,669	\$212,031
2009-10	\$1,905,000	\$1,263,452	\$641,548
2010-11	\$1,865,508	\$822,456	\$1,043,052
2011-12	\$1,383,112		

Our review of expenditure trends and current year costs shows that the District will likely spend significantly less than was budgeted for these four expenditure categories in 2011-12. For example, our review of employee health insurance invoices and annualized payments shows that the District's 2011-12 contribution will be approximately \$377,000 less than the \$2.91 million budgeted. The District's social security contributions for employees based on the 2011-12 salaries will likely be approximately \$1.72 million, or \$500,000 less than what the Board budgeted for 2011-12. The District's teachers' retirement contribution for 2011-12 will likely be about \$400,000 less than the District's budget appropriation. Finally, the District's 2011-12 appropriation for BOCES special educational services is over \$560,000 more than was expended in 2010-11.

More accurate projections for the above expenditures could easily have been calculated by District officials and provided to the Board when developing the budget. By not using realistic estimates,

the Board is creating annual operating surpluses, resulting in the accumulation of excessive fund balance. Although the District's tax levy has remained fairly consistent, by overestimating budget expenditures the Board is placing a higher tax burden on District taxpayers than is necessary to provide educational services for District students, within the District.

Fund Balance

Fund balance is the difference between revenues and expenditures accumulated over a given period of time. Assigned fund balance represents moneys that the District has set aside and may use only for specific purposes and, therefore, these moneys are not available for the District to use in any other manner. Between 2008-09 and 2010-11, the District established three new reserves and added funds to two existing reserves,³ totaling approximately \$4.5 million. The Board also appropriated approximately \$6.2 million for subsequent years' expenditures. Unassigned fund balance represents uncommitted funds and may be used for cash flow purposes and unanticipated expenditures and/or revenue shortfalls. RPTL currently limits the amount of unassigned fund balance that the District can retain to no more than 4 percent of the ensuing fiscal year's budget.

As Table 2 indicates, the District has not reduced unassigned fund balance to within the legal limits.

Fiscal Year	Unassigned Fund Balance at Previous Year End	Percentage of Ensuing Year's Budget	Amount Over Legal Limit
2008-09	\$3,560,999	8.51%	\$1,887,047
2009-10	\$3,520,671	8.21%	\$1,805,150
2010-11	\$4,699,310	10.71%	\$2,944,877
2011-12	\$3,394,424	7.74%	\$1,639,991

The Director of Finance and Administration told us that Board members are aware of the excess unassigned fund balance and that they believe the four percent limitation is unfair, as other government units (towns, villages, and counties) are not limited as to the amount of unassigned fund balance they may retain.

By retaining unassigned fund balance that exceeds the 4 percent threshold, the Board is not adhering to the RPTL and is placing an unnecessary tax burden on District taxpayers.

³ The Board properly established a retirement, unemployment and compensated absence reserve and added additional funds to the capital and tax certiorari reserves.

Recommendations

1. The Board should adopt realistic budgets, using actual financial results from prior years to project expenditures.
2. The Board should maintain unassigned fund balance within the legal limits permitted.
3. District officials should develop a plan to use the surplus fund balance in a manner that benefits District taxpayers. In order to provide appropriate transparency, the use of this surplus should be done through the budget process with public disclosure. Such uses could include, but are not limited to:
 - Reducing District property taxes
 - Funding necessary reserves
 - Paying off debt
 - Funding one-time expenditures.

APPENDIX A

RESPONSE FROM DISTRICT OFFICIALS

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



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February 7, 2012

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Christopher J. Ellis
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Re: Croton-Harmon School District

Dear Mr. Ellis,

Please be advised that we had our exit interview with [REDACTED] from the Office of the State Comptroller on January 17, 2012. At that time we reviewed the draft *Report of Examination* and would now like to submit our Response and Corrective Action Plan to the draft. We appreciate the examiners' efforts and believe that the recommendations will help our school district continue to strengthen our fiscal controls. The recommendations related to issues that we were already aware of and working upon. The report supports our continuing efforts to protect the district's fiscal assets.

The first recommendation: *"The Board should adopt realistic budgets, using actual financial results from prior years to project expenditures."*
Response: The Board of Education has a fiduciary responsibility to the taxpayers of the district. This responsibility covers budgeting, maintaining the physical plant, and educating our students. Since the district had additional unexpended funds available, the Board, with the approval from the community, has been able to establish and fund two Capital Reserve Funds. The district was then able to repair and replace the roofs on all three of the school buildings without having the additional cost of borrowing funds. Additional funds in the Capital Reserve Funds will be used to reconfigure bus lanes and resurface parking areas as well as upgrade the high school auditorium stage area and HVAC system and upgrade the Transportation Facility which was the only building in the district to be deemed inadequate on the Five Year Building Condition Survey. The district has also funded an Employee Benefits Accrued Liabilities Reserve. This reserve has been used to pay out accumulated sick and vacation pay for retirees which was not budgeted for in the general fund budget.

With the additional fund balance, the Croton-Harmon School District has also avoided the expense of borrowing on tax anticipation notes since there have been available funds for cash flow. Maintaining a positive cash flow is vital to a district.

Corrective Action Plan: The district will work to produce and adopt realistic budgets. The Director of Finance and Administration will use the available Budget Status reports to show variances in budget lines to show actual expenditures versus budgeted expenditures.

The second recommendation: *“The Board should maintain unassigned fund balance within the legal limits permitted.”*

Response: The Croton-Harmon School District prides itself on being fiscally conservative. One goal of the Board of Education is to create sound budgets which do not cause tax rates to spike in any one year. Monies from the fund balance have helped the district to submit reasonable tax increases to our community over the years. For twenty-four consecutive years, the community has passed our school budgets. In addition, as a small school district, there is always a concern about unanticipated emergencies and being able to fund necessary remedies. For example, a few years ago, during the winter, a boiler in the older section of our high school unexpectedly broke down and had to be replaced. We were able to immediately bring in a temporary boiler with monies from the fund balance. Without this money, the district would have been forced to cancel classes since there would have been no heat in the building. We believe that establishing fund balance limits to which only school districts must adhere to is unfair and causes significant concern, particularly in a small school district with a limited budget. Our ability to respond to unexpected emergencies is compromised by the fund balance cap.

Corrective Action Plan: The Board of Education is aware of the excess funds in the unassigned fund balance and has entered in to discussion on how to utilize the funds to the best advantage of the taxpayer.

The third recommendation: *“District officials should develop a plan to use the surplus fund balance in a manner that benefits District taxpayers. In order to provide appropriate transparency, the use of this surplus should be done through the budget process with public disclosure. Such uses could include, but are not limited to:*

- a. *Reducing District property taxes*
- b. *Funding necessary reserves*
- c. *Paying off debt*
- d. *Funding one-time expenditures*

Response: Both the District administration and the Board feel as if they have managed the taxpayers’ money appropriately and transparently. Each year, the district has used unassigned fund balance to reduce the property taxes and prevent spikes in the tax rates. Reserves, such as tax certiorari, legal liability, capital reserve funds, employee benefit accrued liability, and unemployment insurance, have been properly funded. Reserves are necessary to avoid the need to borrow funds to pay tax refunds or for legal settlements.

Unfortunately, with the new tax cap, it is no longer prudent to pay off debt as this penalizes the district in the calculation of the tax levy. The district has used unassigned fund balance to pay for one-time expenditures such as computers, photography lab and other Operations and Maintenance projects.

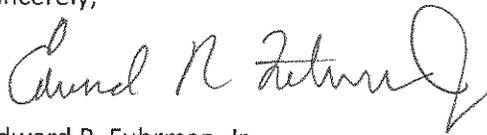
Corrective Action Plan: The Board of Education will continue to ensure that all action relating to funding reserves will be done through board resolution to maintain all transparency. The Board will review the unassigned fund balance

on a regular basis and use the five year projection model created to forecast future unassigned fund balance. When funds are available, the Board will use the funds to: reduce property taxes, fund reserves and fund one-time expenditures.

The Croton-Harmon School District is pleased with the overall *Report of Examination* and its recognition that no pattern of waste, fraud or abuse was found as shared by [REDACTED]. We were told that the district is highly transparent when dealing with financial issues. The report also commends the district on addressing past issues in the areas of information technology and purchasing. According to the report, "The District has implemented corrective action relating to purchasing and information technology and we found those areas to be of limited risk. Also, due to the District's size and comparatively small number of employees in the Business office, we examined internal controls and found them to be operating effectively."

The Croton-Harmon School District wishes also to acknowledge the hard work and the seriousness with which [REDACTED] [REDACTED] approached our audit. Their understanding of the small size of our business office staff and their need to keep our district running smoothly while also fully cooperating with them during the audit was appreciated. We take the responsibility of running an efficient business office and protecting the district's assets on behalf of the Croton-Harmon School District and its community very seriously and will continue to strengthen our efforts by addressing the Recommendations in the *Report of Examination*.

Sincerely,



Edward R. Fuhrman, Jr.
Superintendent of Schools

APPENDIX B

AUDIT METHODOLOGY AND STANDARDS

Our overall goal was to determine if the Board was accumulating excessive fund balance by over budgeting appropriations. To accomplish our objective, we interviewed appropriate District officials and District staff members, tested selected records and examined pertinent documents for the period July 1, 2010 to August 31, 2011. We extended our scope for testing of budgeted appropriations to the 2008-09 fiscal year. Our testing included the following steps:

- We interviewed appropriate District officials and staff members regarding the areas of fund balance and budget appropriations.
- We reviewed Board minutes, adopted budgets for the 2008-09 through 2011-12 fiscal years, contracts, payments, audited financial statements, and budget status reports.
- We reviewed District reserve accounts and supporting documentations to verify appropriateness of funding levels and of proper procedures were adhered to for establishment of those reserves.
- We reviewed salary schedules, health insurance invoices, social security calculations, teacher retirement invoices and BOCES contracts to calculate estimated expenditures for the 2011-12 fiscal year.

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 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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