



Schroon Lake Central School District Financial Condition

Report of Examination

Period Covered:

July 1, 2010 – July 31, 2013

2014M-145



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

February 2015

Dear District Officials:

A top priority of the Office of the State Comptroller is to help school district officials manage their district resources efficiently and effectively and, by so doing, provide accountability for tax dollars spent to support district operations. The Comptroller oversees the fiscal affairs of districts statewide, as well as districts' compliance with relevant statutes and observance of good business practices. This fiscal oversight is accomplished, in part, through our audits, which identify opportunities for improving operations and Board of Education governance. Audits also can identify strategies to reduce costs and to strengthen controls intended to safeguard district assets.

Following is a report of our audit of the Schroon Lake 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*



State of New York Office of the State Comptroller

EXECUTIVE SUMMARY

The Schroon Lake Central School District (District) is located in the Towns of Schroon Lake and North Hudson in Essex County and the Town of Chester in Warren County. The District is governed by the Board of Education (Board), which comprises 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 (Superintendent) is the District's chief executive officer and is responsible for the District's day-to-day management under the Board's direction. The Superintendent was also appointed by the Board to serve as the District's purchasing agent.

The District's general fund budget appropriations for the 2013-14 fiscal year were approximately \$7.4 million, which were funded primarily with real property taxes and State aid.

Scope and Objective

The objective of our audit was to review the District's financial condition for the period July 1, 2010 through July 31, 2013. To obtain additional financial information and provide updated results of operations for the 2013-14 fiscal year, we extended our scope through June 30, 2014. Our audit addressed the following related question:

- Does the Board adopt realistic budgets, routinely monitor financial operations and take appropriate action to maintain the District's financial stability?

Audit Results

The Board-adopted budgets during our audit period included overestimated expenditures and appropriated fund balance that was not actually used to finance operations. As a result, in 2011-12 and 2012-13 the District accumulated fund balance that exceeded the amount that may be carried over into the next school year.¹ The excess fund balance was more than 16 percent of the next year's budgeted appropriations for both years and District officials did not use any of this excess to reduce the real property tax levy for the 2012-13 or 2013-14 fiscal years. Additionally, for fiscal years 2010-11 through 2012-13, the Board-adopted budgets included about \$1.45 million of appropriated fund balance. However, about \$30,000, or 2 percent, was actually used to finance District operations.

Further, although District officials reserved money to prepare for future contingencies, funding of reserve funds was not included as an appropriation in the budgets voted on by taxpayers. Instead,

¹ New York State Real Property Tax Law allows a district to retain a limited amount of unexpended surplus funds (up to 4 percent of the amount of the budget for the upcoming school year, not including funds properly retained under law).

District reserve funds were funded by unrestricted fund balance determined by the Board at the end of each fiscal year. The taxpayers did approve the establishment of a building repair reserve. Although the Board prepared its budgets without using a multiyear financial plan, District officials initiated preliminary work on such a plan before we completed our audit fieldwork.

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. District officials generally agreed with our recommendations and indicated they planned to initiate corrective action.

Introduction

Background

The Schroon Lake Central School District (District) is located in the Towns of Schroon Lake and North Hudson in Essex County and the Town of Chester in Warren County. The District is governed by the Board of Education (Board) which comprises five elected members. The District operates one school building with 224 students and 51 employees.

The Board is responsible for the general management and control of the District's financial and educational affairs. The Superintendent of Schools (Superintendent) is the District's chief executive officer and is responsible for the District's day-to-day management under the Board's direction. The Board also appointed the Superintendent to serve as the District's purchasing agent. A Board-appointed Treasurer is responsible for managing the District's financial affairs.

The District's general fund budget appropriations for the 2013-14 fiscal year were approximately \$7.4 million, which were funded primarily with real property taxes and State aid. The 2013-14 budget included a tax levy of about \$6 million, which was under the property tax cap limit.²

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 realistic budgets, routinely monitor financial operations and take appropriate action to maintain the District's financial stability?

Scope and Methodology

We examined the District's financial records and budgets for the period July 1, 2010 through July 31, 2013. To obtain additional financial information and provide updated results of operations for the 2013-14 fiscal year, we extended our scope through June 30, 2014.

We conducted our audit in accordance with generally accepted government auditing standards (GAGAS). More information on such standards and the methodology used in performing this audit are included in Appendix B of this report.

² Chapter 97 of the Laws of 2011 established a tax levy limit on all local governments (including school districts) in New York State, effective January 1, 2012. This law requires that school districts maintain any property tax levy increase to no more than 2 percent with adjustments for various factors, or the rate of inflation, whichever is less.

**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 the General Municipal Law, Section 2116-a (3)(c) of the New York State Education Law and Section 170.12 of the New York State 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 interests 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, coupled with prudent fund balance management ensure that sufficient funding will be available to sustain operations, address unexpected occurrences and satisfy long-term obligations or future expenditures. Accurate budget estimates also help ensure that the real property tax levy is not greater than necessary. Additionally, the Board should prepare a multiyear financial plan that projects future revenues and expenditures and prepares the District for any future year fiscal challenges.

The Board-adopted budgets during our audit period included overestimated expenditures and appropriated fund balance that was not actually used to finance operations. As a result, in 2011-12 and 2012-13 the District accumulated fund balance that exceeded the amount that may be carried over into the next school year. The excess fund balance was more than 16 percent of the next year's budgeted expenditures for both years³ and District officials did not use any of this excess to reduce the real property tax levy for either the 2012-13 or 2013-14 fiscal years. Additionally, for fiscal years 2010-11 through 2012-13, the Board-adopted budgets included about \$1.45 million of appropriated fund balance. However, about \$30,000, or 2 percent, was actually used to finance District operations.

Further, although District officials reserved money to prepare for future contingencies, funding of reserve funds was not always included as an appropriation in the budgets voted on by taxpayers. Instead, District reserve funds were funded by unrestricted fund balance determined by the Board at the end of each fiscal year, which diminishes the transparency District finances to the taxpayers. The taxpayers did, however, approve establishing a building repair reserve. Finally, although the Board prepared its budgets without using a multiyear financial plan, District officials initiated preliminary work on such a plan before we completed our audit fieldwork. By developing a multiyear financial plan, District officials will have a roadmap to assist in developing more accurate budgetary estimates as well as help manage future District costs and resources.

³ New York State Real Property Tax Law allows a district to retain a limited amount of unexpended surplus funds (up to 4 percent of the amount of the budget for the upcoming school year, not including funds properly retained under law).

Fund Balance and Budgeting

The District's financial condition depends on the Board's ability to develop realistic budgets and monitor the District's financial operations throughout the fiscal year. Further, the Board is required to obtain voter approval for its budgets. If the voters reject a proposed budget, the District has to operate under the spending restrictions of a contingency budget.

When preparing the budget, the Board is responsible for estimating how much the District will spend, how much it will receive in revenue (e.g., State aid), how much fund balance will be available at fiscal year-end as well as determining the expected real property tax levy. Accurate estimates help ensure that the real property tax levy is not greater than necessary. Fund balance in excess of the statutory limit, to the extent not properly retained in reserve funds under law, must be used to fund a portion of next year's budgeted appropriations, thereby reducing the tax levy or used to fund legally-established reserve funds.

By the end of the 2013-14 fiscal year, the unrestricted fund balance increased from about \$295,000 to over \$1.4 million in just four years. This increase occurred despite the Board using \$700,000 of fund balance in August 2012 to increase reserves (see Reserve Funds section of this report).⁴

	2010-11	2011-12	2012-13	2013-14
Beginning Fund Balance	\$1,962,671	\$1,947,655	\$2,146,974	\$2,746,521
Revenues	\$6,914,386	\$6,876,173	\$7,031,894	\$7,141,385
Expenditures	\$6,944,553	\$6,677,158	\$6,360,455	\$6,686,140
Operating Surplus (Deficit)	(\$30,167)	\$199,015	\$671,439	\$455,245
Prior Period Adjustments	\$15,151	\$304	(\$71,892)	\$0
Year-End Fund Balance	\$1,947,655	\$2,146,974	\$2,746,521	\$3,201,766
Less: Restricted Fund Balance	\$1,027,321	\$639,068	\$1,170,724	\$1,402,129
Less: Unrestricted Fund Balance Appropriated for the next Fiscal Year	\$625,000	\$300,000	\$350,000	\$380,000
Unrestricted Fund Balance at Year-End	\$295,334	\$1,207,906	\$1,225,797	\$1,419,637

Additionally, the Board overestimated expenditures and appropriated unrestricted fund balance that was not actually used to fund operations.⁵

Appropriating fund balance to finance operations should result in a planned operating deficit in the year of appropriation. For example, the District's budget for the 2010-11 fiscal year included an appropriation

⁴ Unrestricted fund balance exceeded the statutory limit for the 2011-12, 2012-13, and 2013-14 fiscal years, despite the reserve fund transfer and because of operating surpluses generated those years.

⁵ District officials again appropriated \$350,000 of fund balance in the 2013-14 budget and \$380,000 in the 2014-15 budget.

of \$525,000 of fund balance to aid in financing operations. Thus, if revenues and expenditures realized were in line with their budgetary estimates, the District would then incur a planned operating deficit of \$525,000. However, the District used \$30,167 of fund balance to finance 2010-11 operations because it actually incurred an operating deficit of that amount.

Furthermore, although the Board appropriated \$625,000 of fund balance to help finance the 2011-12 fiscal year's operations, the District did not use any of these funds because it generated a surplus of about \$199,000.

Similarly, for the 2012-13 fiscal year, the Board appropriated \$300,000 of fund balance to finance operations. However, the District did not use any of the fund balance because it actually generated a surplus of about \$671,000. Finally, the Board appropriated \$350,000 of fund balance to finance operations for the 2013-14 fiscal year. However, the District actually generated a surplus of about \$455,000 and did not use any of the fund balance. These surpluses occurred because the District overestimated expenditures in each year, by about \$725,000 for 2011-12, \$883,000 for 2012-13 and \$714,000 for 2013-14.

From fiscal years 2010-11 through 2012-13 the Board-adopted budgets included appropriated fund balance of about \$1.45 million to finance operations. However, due to a very small operating deficit in 2010-11 and operating surpluses in both 2011-12 and 2012-13, the District actually used about \$30,000, or about 2 percent, of total appropriated fund balance.

General fund actual expenditures were well below the budgeted appropriations for each year we reviewed. From fiscal years 2010-11 through 2013-14, District officials overestimated expenditures by about \$2.66 million, or 9 percent of these fiscal year's combined budget appropriations.

Figure 2: Overestimated Expenditures and Appropriated Fund Balance				
	2010-11	2011-12	2012-13	2013-14
Estimated Expenditures	\$7,286,413	\$7,042,379	\$7,243,314	\$7,400,244
Actual Expenditures	\$6,944,553	\$6,677,158	\$6,360,455	\$6,686,140
Variance	\$341,860	\$725,221	\$882,859	\$714,104
Appropriated Fund Balance	\$525,000	\$625,000	\$300,000	\$350,000
Operating Surplus (Deficit)	(\$30,167)	\$199,015	\$671,439	\$455,245
Actual Unrestricted Fund Balance Used	\$30,167	\$0	\$0	\$0

Our review of the District's budgets from 2010-11 through 2013-14 disclosed that estimated revenues were reasonable. However,

certain expenditure items were consistently overestimated each year. For example, the amounts budgeted for programs for children with disabilities were the highest overestimated expenditures each year. The District overestimated these expenditures by more than \$226,000 in 2010-11, \$378,000 in 2011-12, \$395,000 in 2012-13 and \$405,000 in 2013-14.

The Board budgeted about \$706,900 for these expenditures in 2013-14. However, District officials spent about \$301,200 on these programs through the fiscal year. The District's 2014-15 adopted budget includes \$642,630 for the programs for children with disabilities, even though from 2010-11 through 2013-14 the average amount spent for these expenditures totaled about \$422,000.

Further, District officials also consistently overestimated employee insurance and secondary-level teacher salary expenditures. For example, secondary-level teacher salaries were overestimated by \$48,421 in 2013-14, by \$130,641 in 2012-13 and by \$90,077 in 2011-12. Employee medical insurance was overestimated by \$155,828 in 2013-14, by \$114,847 in 2012-13, and by \$265,373 in 2011-12. As these costs are established by contract, they should be predictable and budget estimates should be very close to actual expenditures.

Because District officials consistently overestimated expenditures and used such a small amount of appropriated fund balance to finance operations over the past three fiscal years, the District accumulated fund balance at levels in excess of the amount that may be carried over into the next school year. As a result, real property taxes have been significantly higher than necessary because none of the excess was used to reduce the real property tax levy for either the 2012-13 or 2013-14 fiscal years. Furthermore, the budgetary practice of adopting unrealistic estimates for expenditures and appropriating fund balance that will not actually be used to finance operations diminishes the transparency of the budgeting process.

Reserve Funds

Unrestricted fund balance may be restricted or reserved for particular purposes or appropriated to reduce the real property tax levy. When District officials establish reserve funds for specific purposes, it is important that they develop a plan for funding the reserves, determining how much should be accumulated and how and when funds will be used to finance related costs. Such a plan serves to guide District officials in accumulating and using reserve funds and to inform District residents about how their tax dollars will be used.⁶

⁶ See our publication entitled Reserve Funds available at: <http://www.osc.state.ny.us/localgov/pubs/lmg/reservefunds.pdf>

District officials accumulated an increasing amount of restricted fund balance, or reserve funds. As of June 30, 2012, reserve funds totaled \$364,678.⁷ In August 2012, the Board increased an existing employee benefit and liability reserve by \$500,000. The Board also established two more reserve funds – tax certiorari reserve⁸ and an unemployment insurance reserve and placed \$100,000 into each reserve fund.

The funding of these reserves was not planned nor was it included as an appropriation in the budgets voted on by taxpayers. Instead, these reserve funds were funded by the unrestricted fund balance available at year-end. Had District officials included transfers of unrestricted fund balance to reserve funds in the budgets, they could have achieved the same result, but done it in a way that was more transparent to taxpayers. As a result of the 2014-15 budget vote, the taxpayers approved establishing a building repair reserve, which District officials funded with \$300,000 of unrestricted fund balance.

We reviewed the reserve funds to determine if the balances were maintained at reasonable levels. The employee benefit and liability reserve fund balance at the end of the 2012-13 fiscal year totaled \$804,089. The money held in this reserve is used to compensate employees for unused sick leave upon retirement. The Treasurer's estimated projection for the liability to be paid from this reserve fund was based on the employees' contractual agreement provisions and the value of all District employees' unused sick leave balances. However, our review of unused sick leave balances for District teachers who were eligible or close to being eligible to receive payment for their unused sick leave upon retirement had accumulated sick leave benefits worth approximately \$256,000 as of June 30, 2013. Thus, this reserve fund is funded beyond the District's needs.

According to the Treasurer, the amounts reserved in the tax certiorari and unemployment insurance reserve funds were based on estimates of potential future liabilities. However, District officials provided no evidence supporting any future potential liabilities for either of these reserve funds. Further, the amount reserved for tax certiorari was not based on any actual claims or pending litigation substantiating a reasonable estimate of potential liability. District officials expended about \$11,000 from the tax certiorari reserve during the 2012-13 fiscal year and no expenditures were made from the unemployment insurance reserve.

⁷ This total included \$303,728 in an employee benefit and liability reserve and \$60,950 in a reserve for debt.

⁸ In general, tax certiorari is a legal proceeding whereby a taxpayer, who has been denied a reduction in real property tax assessment, challenges the assessment on the grounds of excessiveness, inequality, illegality or misclassification.

The District's 2012-13 budget contained a \$13,000 appropriation for unemployment insurance expenditures and officials expended \$6,128 from the general fund in 2012-13 to fund these expenditures. Therefore, no reserve fund money was used to finance these expenditures. The District did not budget for unemployment costs in the general fund in 2013-14 and 2014-15. Considering the annual level of expenditures for tax certiorari and unemployment insurance and because District officials had not determined a specific dollar threshold for the District's potential tax certiorari liability, the amounts placed in these reserve funds appear excessive in comparison with the District's needs.

By maintaining excessive money in reserve funds, the Board and District officials have withheld significant funds from productive use, levied unnecessary taxes and compromised the transparency of District finances to the taxpayers.

Multiyear Financial Plan

Multiyear financial planning is a tool school districts can use to improve the budget development process. Planning on a multiyear basis can enable District officials to identify developing revenue and expenditure trends, establish long-term priorities and goals and consider the impact of near-term budgeting decisions on future fiscal years. It also allows District officials to assess the merits of alternative approaches (such as using unrestricted fund balance or establishing and using reserve funds) to finance District operations.

A well-designed plan can assist the Board in making timely and informed decisions about the District's programs and operations. Multiyear financial planning can also help District officials project the future costs of employee salaries and benefits provided for in collective bargaining agreements. Any long-term financial plan should be monitored and updated on a continuing basis to provide a reliable framework for preparing budgets and to ensure that information used to guide decisions is current and accurate.⁹

The Board did not establish a multiyear financial plan to facilitate development of the annual budgets that were included in our audit period. As a result, District officials did not formulate a plan that considers current economic conditions, recent reductions in State aid and the impact of the tax cap legislation.¹⁰ Further, employee benefit costs, such as medical insurance and required contributions to the retirement systems, continued to increase. The Board also did not evaluate its establishment and future use of reserve fund money.

⁹ See our publication entitled Multiyear Capital Planning available at: http://www.osc.state.ny.us/localgov/pubs/lmg/capital_planning.pdf

¹⁰ By law, the District's annual real property tax levy generally cannot increase more than 2 percent, or the rate of inflation, whichever is less, with some exceptions. Districts may override the tax levy limit if a budget that exceeds the statutory limit is approved by at least 60 percent of District voters.

According to the former Superintendent, the Board directed her to develop a multiyear financial plan that will include using unrestricted fund balance. Before we completed our on-site audit fieldwork, District officials received a building condition survey report that recommended about \$5.7 million in repairs and renovations to the school building. The former Superintendent said that the report will be used to aid in developing a multiyear plan that will also include future projected operational costs and revenues. Such a multiyear financial plan that is reviewed and updated annually will allow District officials to manage the use of unrestricted fund balance and reserve funds and provide a way to solicit public input by establishing practical goals to ensure that such use is in the best interest of District taxpayers.

Recommendations

District officials should:

1. Ensure that unrestricted fund balance accumulated in excess of the limit allowed by law is used to reduce the next year's real property tax levy.
2. Adopt budgets with reasonable expenditure estimates.
3. Develop a plan determining how to fund the reserve funds, specifying the funding levels to be maintained and indicating how and when these funds should be used to avoid placing excessive amounts in the reserve funds.
4. Include the amounts of planned reserve fund transfers in the annual proposed budgets as a means to enhance transparency of reserve funding to the taxpayers.
5. Continue developing a multiyear financial plan.

APPENDIX A

RESPONSE FROM DISTRICT OFFICIALS

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

Schroon Lake Central School District

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Board of Education

Robert Claus, President
Tina Armstrong, Vice President
Dana Shaughnessy, BOE Member
Eric Welch, BOE Member
Anne Durkee, BOE Member



District Officials

James Polunci, Interim Superintendent
David Williams, Pupil Personnel Director
Matthew Dempsey, Guidance Counselor
Lisa DeZalia, District Clerk
Danielle Y. Fosella, District Treasurer

February 4, 2015

Office of the State Comptroller

Division of Local Government

The following is the response from the Schroon Lake Central School District to the recommendations list in your draft audit report covering the period of July 1, 2010 through July 31, 2013.

Recommendation #1- Ensure that unrestricted fund balance accumulated in excess of the limit allowed by law is used to reduce the next year's real property tax levy.

The District is putting together a multi-year revenue and expenditure plan to address the excess unrestricted fund balance noted in the audit. The plan will include estimated increases in annual expenditures over the next several years based on trends and information that we currently have. Funding appropriate reserves as allowed under general municipal law and appropriating fund balance to the upcoming budgets will be used in accordance with the educational plans and goals the District has set forth.

Recommendation #2- Adopt budgets with reasonable expenditures.

The District will review actual expenditures over the past three years and evaluate areas in which there are surplus funds available as well as areas where there were deficits. This will allow the District to more accurately project expenditures in future year's budgets.

Recommendation #3- Develop a plan determining how to fund reserve funds, specifying the funding levels to be maintained and indicating how and when these funds should be used to avoid placing excessive amounts in the reserve funds.

The District is utilizing Reserve fund chart that lists the allowed reserve funds, purpose, legal citation, how it is established and funded, how it is expended, duration of time and any restrictions to move forward with new and existing reserve funds for the District.

Recommendation #4- Include the amounts of planned reserve fund transfers in the annual proposed budgets as a means to enhance transparency of reserve funding to the taxpayers.

We will include this recommendation in our fiscal planning moving forward planning and administering future budgets and tax levies.

Recommendation #5- Continue developing a multiyear financial plan.

We will continue to develop budgets in the future using a multi-year plan in the process.

Sincerely,

James P. Polunci

Interim Superintendent

APPENDIX B

AUDIT METHODOLOGY AND STANDARDS

Our overall goal was to assess the District's financial operations. To accomplish this, we performed an initial assessment of the internal controls put in place by officials to safeguard District assets so that we could design our audit to focus on those areas most at risk. Our initial assessment included evaluations of the following areas: financial oversight, cash receipts and disbursements, purchasing, payroll and personal services and information technology. We determined that controls appeared to be adequate and limited risk existed in most of the financial areas we reviewed. We then decided on the reported objective by selecting the District's financial condition for audit. To accomplish our audit objective and obtain valid audit evidence we performed the following procedures:

- We interviewed officials to gain an understanding of the District's budgeting process.
- We reviewed the results of operations and analyzed changes in fund balance. Subsequent to field work, we obtained additional financial information to provide updated results of operations through June 30, 2014.
- We compared the adopted budgets to the modified budgets and actual operating results to determine if the budget assumptions were reasonable.
- We analyzed the composition of sources of revenue to identify trends.
- We reviewed expenditures based on the District's budget categories to identify significant expenditures and analyze trends.
- We reviewed Board minutes and resolutions to verify the establishment of reserve funds. We reviewed the balances of the reserves for reasonableness.
- We interviewed officials to determine if the District developed a multiyear financial plan.
- We tested the reliability of the data reported on the annual financial report filed with the Office of the State Comptroller and the District's independently audited financial statements by reviewing journal entries, bank statements and cash receipts and disbursements.
- We reviewed budget and revenue status reports.
- We reviewed the District's tax cap calculations for accuracy.
- We reviewed meeting minutes and interviewed officials to determine whether the District's management is involved in financial matters by receiving and reviewing financial reports, analyzing the need for and establishing reserves and otherwise monitoring the District's financial condition.

We conducted this audit in accordance with GAGAS. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

APPENDIX C

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