

Wells Central School District

Financial Condition Management

JULY 2017



OFFICE OF THE NEW YORK STATE COMPTROLLER
Thomas P. DiNapoli, State Comptroller

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Report Highlights

Wells Central School District

Audit Objective

Determine whether District officials effectively managed general fund balance.

Key Findings

- The District's adopted budgets were unrealistic and included appropriated fund balance not used as planned to fund operations. The budgets overestimated appropriations by almost \$1.2 million or 7.7 percent from 2013-14 through 2015-16.
- Unrestricted fund balance increased to almost \$854,000 or 15 percent of the ensuing year's budgeted appropriations, exceeding the statutory limit by 11.1 percentage points as of June 30, 2016.
- Retirement contribution reserve and unemployment insurance reserves appear overfunded.

Key Recommendations

- Adopt realistic annual budgets based on historical trends or other known trends and use appropriated fund balance to fund operations.
- Use surplus funds as a financing source to fund one-time expenditures and needed reserves or reduce District property taxes.
- Review all reserves to determine whether the amounts retained are necessary and reasonable.

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

Background

The Wells Central School District is located in the Towns of Arietta, Lake Pleasant, Hope and Wells in Hamilton County.

The Board of Education is responsible for managing and controlling the District's financial and educational affairs. The Superintendent of Schools (Superintendent) is responsible for the District's day-to-day management. The Superintendent is also responsible for budget development and administration assisted by the District Treasurer.

Quick Facts

Employees	49
Enrollment	150
2016-17 Appropriations	\$5.7 million

Audit Period

July 1, 2013 – November 30, 2016

Financial Condition Management

What is Effective Financial Condition Management?

To effectively manage a district's financial condition, a board of education must adopt realistic and structurally balanced budgets based on historical data or known trends, in which recurring revenues finance recurring expenditures and reasonable levels of fund balance are maintained. A district may retain a portion of fund balance, referred to as unrestricted fund balance.

Districts should ensure that unrestricted fund balance does not exceed the amount allowed by New York State Real Property Tax Law, which currently limits unrestricted fund balance to no more than 4 percent of the following year's appropriations. Any unrestricted fund balance over this percentage must be used to reduce the real property tax levy by appropriating fund balance to lower the unrestricted fund balance.

Districts are legally allowed to reserve portions of fund balance to finance future costs (e.g., capital projects or retirement expenditures). District officials should ensure that reserve balances do not exceed the amount necessary to address long-term obligations or planned expenditures. The Board should adopt a formal written plan that indicates how the reserves will be funded, how much should be accumulated in the reserves and when the money will be used to finance related costs.

While school districts are generally not limited as to how much money can be held in reserves, the balances should be reasonable. The Board should balance the intent for accumulating money for future identified needs with the obligation to ensure that the District's real property tax levy is not greater than necessary.

Unrestricted Fund Balance Exceeded the Statutory Limit

District officials need to improve budgeting practices to more effectively manage the District's fund balance. The District has accumulated unrestricted fund balance that exceeded the statutory limit by \$627,940 or 11.1 percentage points as of June 30, 2016. While District officials appropriated fund balance annually none of the appropriated fund balance was actually used to finance operations from 2013-14 through 2015-16.

For example, District officials appropriated \$200,000 of fund balance for the 2015-16 fiscal year. However, because the District incurred an operating surplus of \$671,690 that year, none of the amount appropriated was used to finance operations. When unused appropriated fund balance was added back, the District's recalculated unrestricted fund balance as a percentage of the subsequent year's budget ranged from 7 to 19 percent.

The District's practice of appropriating fund balance each year that was not needed to finance operations is, in effect, a reservation of fund balance that is

not provided for by statute and a circumvention of the statutory limit. Adopting budgets that result in the appropriation of fund balance that will not be used causes the District to retain more fund balance and levy more real property taxes than needed. As a result, the District accumulated unrestricted fund balance in excess of the statutory limit and continued to accumulate additional amounts during our audit period in both reserved and unreserved fund balance.

Figure 1: Unrestricted Fund Balance at Year-End

	2013-14	2014-15	2015-16
Total Beginning Fund Balance	\$1,626,886	\$1,821,661	\$1,864,652
Add: Operating Surplus	\$194,763	\$42,992	\$671,685
Total Year-End Fund Balance	\$1,821,649	\$1,864,653	\$2,536,337
Less: Restricted and Assigned Funds	\$950,793	\$1,442,466	\$1,482,372
Less: Appropriated Fund Balance for the Ensuing Year	\$677,800 ^a	\$200,000	\$200,000
Total Unrestricted Funds at Year-End	\$193,056	\$222,187	\$853,965
Ensuing Year's Budgeted Appropriations	\$5,426,898	\$5,554,621	\$5,650,626
Unrestricted Funds as Percentage of the Ensuing Year's Budget	3.6%	4.0%	15.1%
Unrestricted Funds as Percentage of Ensuing Year's Budget when unused Appropriated Fund Balance is added back	7%	8%	19%

^a Includes \$477,800 appropriated for reserves.

District officials' practice of overestimating operating expenditures contributed to annual operating surpluses and increasing amounts of unrestricted fund balance. We compared the District's budgeted revenues and appropriations with actual results of operations from 2013-14 through 2015-16 to determine whether the estimates were reasonable. While revenue estimates were reasonable, District officials presented, and the Board approved, budgets that overestimated appropriations by a total of approximately \$1.2 million or 7.7 percent.

Figure 2: Overestimated Appropriations

	2013-14	2014-15	2015-16	Totals
Appropriations	\$5,357,840	\$5,426,898	\$5,554,621	\$16,339,359
Actual Expenditures	\$4,997,049	\$5,329,334	\$4,843,447	\$15,169,830
Overestimated Appropriations	\$360,791	\$97,564	\$711,174	\$1,169,529
Percentage Overestimated	7.2%	1.8% ^a	14.7%	7.7%

^a The Board approved a \$477,000 transfer from the general fund to the capital project fund that was not originally in the 2014-15 budget, resulting in a smaller operating surplus in the general fund this year.

We analyzed all expenditure accounts to determine whether the budget estimates were reasonable based on prior years' actual expenditures and the District's current needs. Overestimated appropriations were spread among numerous accounts throughout the budgets. The most significant were in fiscal year 2015-16 appropriations for employee benefits, which were overestimated by \$266,466 (19 percent) and contractual costs which were overestimated by \$213,937 (26 percent). The Superintendent indicated that when developing the budgets, he wanted to ensure that costs were not underestimated (especially medical insurance) and added an extra 3 percent over the prior year's budget each year to the appropriation for medical insurance. This increase occurred even though prior year budgets overestimated health insurance costs.

We also reviewed the District's adopted 2016-17 budget totaling approximately \$5.7 million and found while estimated revenues are reasonable, appropriations continue to be overestimated. We project that the District will realize an unplanned operating surplus of approximately \$550,000. As a result, fund balance will increase by approximately \$550,000, rather than decrease as budgeted by District officials based on the \$200,000 appropriation of fund balance. As with prior year budgets, we projected overestimated appropriations will continue to be spread among numerous accounts. The most significant projected variance overestimates employee benefits by more than \$368,000 or 26 percent.

For 2013-14 and 2014-15, the overall budget to actual variances for expenditures were reasonable. However, by overestimating expenditures and appropriating fund balance that was not actually used to finance annual operations led to the District maintaining an excessive and increasing level of unrestricted fund balance.

The Board was aware of the excess amount of unrestricted fund balance the District accumulated but has not adopted a written plan to reduce this excess. However, the Superintendent indicated that there is an informal plan to use a portion of the excess to finance a future building capital project to repair the school roof, install new energy efficient boilers, replace all electrical panels and replace a water main.

Two Reserves Appear Overfunded

As of June 30, 2016, the District reported four general fund reserves (retirement contribution, unemployment insurance, capital and employee benefit accrued liability) with balances totaling approximately \$1.5 million. We examined the District's plans for funding and using these reserves. We did not find any significant concerns with the capital and employee benefit accrued liability reserves. However, we had the following concerns with the retirement contribution and unemployment reserves:

-
- The Board established a retirement contribution reserve in August 2006 to fund future payments to the New York State and Local Retirement System. The balance as of June 30, 2016 was \$410,000, sufficient to cover over eight years of retirement costs, which averaged \$48,980 over the last three years. However, the District has not used any reserve funds to pay for these expenditures over the last three years because appropriations were included in the annual budgets.
 - The Board established an unemployment reserve in March 2013 to fund reimbursement to the New York State Unemployment Insurance Fund for claims filed. The balance as of June 30, 2016 was \$50,000, sufficient to cover nearly eight years of unemployment costs which average \$6,477 over the last three years. However, the District has not used any reserve funds to pay for these expenditures over the past three years.

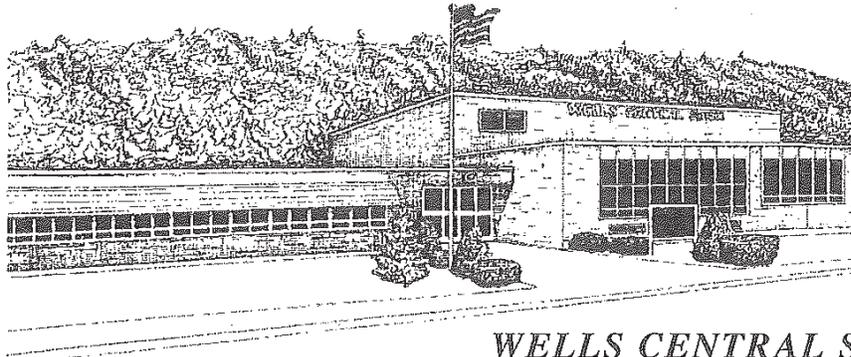
Further, the District has not developed a written reserve fund policy that describes a maximum funding level and the planned use of these reserves. As a result, these two reserves appear overfunded.

What Do We Recommend?

The Board and District officials should:

1. Adopt annual budgets which are realistic based on historical trends or other known factors and use appropriated fund balance to fund operations.
2. Use surplus funds as a financing source for:
 - Funding one-time expenditures
 - Funding needed reserves
 - Reducing District property taxes
3. Review all reserves at least annually to determine whether the amounts reserved are necessary and reasonable, and use excess amounts in accordance with applicable statutes in a manner that benefits residents.
4. Adopt a written reserve fund policy that includes how the reserves will be funded, the optimal funding levels for each reserve and the conditions under which reserves will be used to finance related costs.

Appendix A: Response From District Officials



WELLS CENTRAL SCHOOL

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July 12, 2017

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One Broad Street Plaza
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Audit Report Title: Financial Condition Management
Audit Report #: 2017M-70

To Whom It May Concern:

This letter is in response to the draft audit *Financial Condition Management* of the Wells Central School District by the Office of the New York State Comptroller dated July 1, 2013 to November 30, 2016. On behalf of the Board of Education and the District administration and office staff, we would like to thank the Comptroller's staff for their professionalism and courtesy in conducting their auditing duties.

We have reviewed the report on the financial condition of the District and it appears that the findings and recommendations within the report are accurate. Once the final audit report has been issued, the District will respond with a Corrective Action Plan within 90 days. The Corrective Action Plan will be filed with the Office of the State Comptroller and New York State Education Department.

The Wells Central School District is committed to providing the community and the students with sound fiscal health in both the short-term and long-term. As a District, our top priority is to provide the best education in the most cost-effective ways possible. The Board of Education and the administration and office staff are dedicated to ensuring that the District's financial operations are performed at the highest level and in the best interest of the community. Ways to improve the financial operations of the District are of utmost importance to our students and residents.

Once again the District would like to extend its appreciation for the professionalism and courteous manners we experienced with your staff during the audit process.

Sincerely,

Thomas D. Sincavage
Superintendent of Schools

Appendix B: Audit Methodology and Standards

We conducted this audit 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. To achieve the audit objective and obtain valid audit evidence, we performed the following audit procedures:

- We interviewed the Superintendent and other District officials to gain an understanding of the District's financial management policies and procedures and the District's budgeting practices.
- We analyzed the District's general fund financial records from 2013-14 through 2015-16 to determine whether unrestricted fund balance increased or declined. We also evaluated any factors contributing to the increase or decline identified.
- We reviewed the Board adopted general fund budgets to determine whether they were realistic and structurally balanced by comparing the adopted budgets from 2013-14 through 2015-16 with actual results of operations.
- We reviewed the adopted general fund budget for 2016-17 to determine whether budgeted revenues and appropriations were reasonable based on historical data and supporting source documentation.
- We analyzed the general fund's financial condition to determine whether during the audit period fund balance increased or was in excess of statutory limit and whether operating deficits were incurred.

We conducted this performance audit in accordance with GAGAS, generally accepted government auditing standards. 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.

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

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, pursuant to Section 35 of General Municipal Law, Section 2116-1(3) (c) of New York State Education Law and Section 170.12 of the Regulations of the Commissioner of Education. To the extent practicable, implementation of the CAP must begin by the end of the 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. We encourage the Board to make the CAP available for public review in the Clerk's office.

Appendix C: Resources and Services

Regional Office Directory

www.osc.state.ny.us/localgov/regional_directory.pdf

Cost-Saving Ideas – Resources, advice and assistance on cost-saving ideas

www.osc.state.ny.us/localgov/costsavings/index.htm

Fiscal Stress Monitoring – Resources for local government officials experiencing fiscal problems

www.osc.state.ny.us/localgov/fiscalmonitoring/index.htm

Local Government Management Guides – Series of publications that include technical information and suggested practices for local government management

www.osc.state.ny.us/localgov/pubs/listacctg.htm#lmgm

Planning and Budgeting Guides – Resources for developing multiyear financial, capital, strategic and other plans

www.osc.state.ny.us/localgov/planbudget/index.htm

Protecting Sensitive Data and Other Local Government Assets – A non-technical cybersecurity guide for local government leaders

www.osc.state.ny.us/localgov/lgli/pdf/cybersecurityguide.pdf

Required Reporting – Information and resources for reports and forms that are filed with the Office of the State Comptroller

www.osc.state.ny.us/localgov/finreporting/index.htm

Research Reports / Publications – Reports on major policy issues facing local governments and State policy-makers

www.osc.state.ny.us/localgov/researchpubs/index.htm

Training – Resources for local government officials on in-person and online training opportunities on a wide range of topics

www.osc.state.ny.us/localgov/academy/index.htm

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