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July 15, 2010

Dr. Charles S. DEDRICK, District Superintendent
Members of the Board of Education
Capital Region BOCES
900 Watervliet – Shaker Road, Suite 102
Albany, New York 12205

Report Number: S9-9-66

Dear Superintendent DEDRICK and Members of the Board of Education:

A top priority of the Office of the State Comptroller is to help officials manage their resources efficiently and effectively and, by so doing, provide accountability for tax dollars spent to support operations. The Comptroller oversees the fiscal affairs of local governments statewide, as well as 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 governance. Audits also can identify strategies to reduce costs and to strengthen controls intended to safeguard assets.

In accordance with these goals, we conducted an audit of six BOCES throughout New York State. The objective of our audit was to determine if these BOCES have been reserving excessive funds without informing their component and participating school districts. We included the Capital Region BOCES in this audit. Within the scope of this audit, we examined the policies and procedures of the Capital Region BOCES, the documentation to support reserve balances, and the reporting to component school districts for the period July 1, 2007 to June 30, 2009. For historical reserve fund activity, we reviewed reserve fund data for the period July 1, 2005 through June 30, 2007.

This report of examination letter contains our findings and recommendations specific to the Capital Region BOCES. We discussed the findings and recommendations with BOCES officials and considered their comments in preparing this report. At the completion of our audit of the six BOCES, we will prepare a global report that summarizes the significant issues we identified at all BOCES audited.

Summary of Findings

Our audit found that the Capital Region BOCES (BOCES) retained \$5 million¹ in reserve funds for which BOCES lacks specific authority to have or that BOCES inappropriately used. These funds were allocated from school district moneys. During our audit period, BOCES used approximately \$6.1 million in budgetary appropriations and surplus to fund six of its seven reserves² – an employee benefit accrued liability reserve, an unemployment insurance reserve, a workers' compensation reserve, career and technical education (CTE) equipment reserve, Employees' Retirement System (ERS) contribution reserve³ and a property loss and liability reserve – without indicating to its districts that these appropriations were allocated to reserves, instead, including them within budgeted expenditures. In addition, BOCES officials established an employee benefit accrued liability reserve, having a balance of \$4 million, as of June 30, 2009, and improperly used it to defray the cost of retiree health insurance and to provide cash flow relief to the general fund. Further, BOCES officials established a workers' compensation reserve, having a balance of \$1 million, as of June 30, 2009, and used this reserve to pay workers' compensation claims without clear statutory authority for this type of reserve.

BOCES officials also did not establish policies and procedures, or develop specific documented plans, for the funding and use of the reserves. In addition, the ERS Contribution Reserve Fund was not properly established by board resolution, and the career educational instructional equipment reserve was inappropriately funded in 2008-09 with \$250,000 of surplus funds. Finally, BOCES did not allocate interest to the unemployment insurance or ERS contribution reserves during our audit period.

The failure of BOCES officials to ensure that all reserves were properly established and reasonably funded has increased the risk of the school districts', and therefore taxpayer, moneys not being used in a productive manner and/or in accordance with legal requirements. Further, BOCES' failure to clearly report reserve allocations to the component and participating school districts has compromised the transparency of BOCES operations and denies the school districts complete knowledge of how BOCES is ultimately using money paid by districts for BOCES services.

Background and Methodology

BOCES serves 23 component school districts, in Albany, Schoharie, Schenectady, and Saratoga Counties and the Albany City School District. BOCES is governed by a 10-member Board of Education (Board) whose members are elected by the 23 component school districts. BOCES' operating expenditures totaled \$102.2 million in the 2007-08 fiscal year. These costs are funded primarily by charges to school districts for services, federal grants, and tuition fees from adult education classes. New York State Law and the Office of the State Comptroller provide guidance with respect to the establishment, funding, and use of BOCES reserves.

¹ Includes the Workers' Compensation Reserve of \$1 million, and the inappropriately used Employee Benefit Accrued Liability Reserve of \$4 million.

² This excludes Reserve for Encumbrances, which is an accounting designation for funds that are committed for goods or services ordered but not yet received by the end of the fiscal year in which they were ordered.

³ In BOCES records, this reserve is referred to as the Employees' Retirement System Reserve.

BOCES' primary function is to provide educational programs and services to component and participating⁴ school districts. The Board is responsible for establishing policies and procedures including documented plans for the funding and use of reserves. BOCES has approximately 1,200 employees working at campuses and in schools throughout the region. We examined the minutes of Board proceedings, accounting ledgers, financial statements, BOCES policies and procedures, and other reserve support materials and documentation.

BOCES can legally reserve funds for specific future uses, helping reduce its reliance on operating funds or borrowed moneys. Reserves must be established by Board resolution and in some instances⁵ require approval by a majority of the component school districts' Boards of Education. BOCES officials are responsible for developing policies and procedures to ensure that reserves comply with applicable laws, regulations, and good management practices concerning reserve establishment, funding, use, and reporting to the school districts. These policies and procedures should clearly indicate BOCES' plans for reserve funds, including the specific purpose for each reserve and the Board's intended method and level of funding.

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.

Established Reserves

Education Law and General Municipal Law (GML) define the types of reserves that can be established by a BOCES. Additionally, the law requires reserves to be established by Board resolution and in some instances requires approval by a majority of the component school districts' Boards of Education.

Most reserve funds are established to provide resources for an intended future use. An important concept to remember is that a reserve fund should be established with a clear intent or plan in mind regarding the future purpose, use and, when appropriate, replenishment of funds from the reserve. Reserve funds should not be merely a "parking lot" for excess cash or fund balance. Local governments, school districts and BOCES should balance the desirability of accumulating reserves for future needs with the obligation to make sure taxpayers are not overburdened by these practices. There should be a clear purpose or intent for reserve funds that aligns with statutory requirements.

During the audit period, BOCES maintained six reserve funds that totaled approximately \$6.9 million at June 30, 2009 (prior to year-end adjustments):⁶

⁴ Component school districts (BOCES members) provide most of the funding for BOCES facilities and services. BOCES also serves "participating" school districts which elect to participate in one or more selected BOCES programs and are billed accordingly.

⁵ For example, a career and technical equipment reserve

⁶ This excludes Reserve for Encumbrances, which is an accounting designation for funds that are committed for goods or services ordered but not yet received by the end of the fiscal year in which they were ordered.

| Reserve Title | June 30, 2006 | June 30, 2007 | June 30, 2008 | June 30, 2009⁷ |
|---|----------------------|----------------------|----------------------|----------------------------------|
| Employee Benefit Accrued Liability Reserve | \$1,089,192 | \$2,457,313 | \$3,863,610 | \$3,971,854 |
| Workers' Compensation Reserve | \$389,293 | \$620,327 | \$816,298 | \$1,092,321 |
| Unemployment Reserve | \$356,130 | \$356,343 | \$435,515 | \$489,914 |
| Career and Technical Education (CTE) Equipment Reserve | - | \$50,239 | \$52,060 | \$302,869 |
| Employees' Retirement System (ERS) Contribution Reserve | \$790,042 | \$790,042 | \$1,421,639 | \$1,421,639 |
| Property Loss and Liability Reserve | - | - | - | \$1,019,813 |
| Total Reserves | \$2,624,657 | \$4,274,264 | \$6,589,122 | \$8,298,410 |

BOCES officials properly established four⁸ of the six reserve funds by Board resolution and properly accounted for these reserve funds separately. The ERS Contribution Reserve was established without board resolution, as required by statute. In addition, although it was established by Board resolution, BOCES does not have clear legal authority to establish a workers' compensation reserve. Our findings regarding BOCES' funding of reserves, disclosure of reserve allocations to the school districts, maintenance of reserve fund balances and use of the reserve funds, and the workers' compensation reserve are detailed below.

Funding Reserves and Disclosure to School Districts

Any governing board, including a BOCES Board, that is planning to establish and finance reserve funds on a regular basis should develop a detailed written policy that communicates to taxpayers why the money is being set aside, the board's financial objectives for the reserves, optimal funding levels, and conditions under which the assets will be utilized. All 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. By making provisions to raise resources for reserve funds explicit in the proposed budget, the BOCES board gives its school districts and those districts' voters and residents an opportunity to know the board's plan for funding its reserves.

Operating surpluses and/or budgetary appropriations used to fund reserves should be labeled as such and clearly communicated to BOCES' component and participating school districts, and consequently those districts' taxpayers. Although there is no statutory limit on the amount in most reserves, the balances in statutorily authorized reserves should be reasonable and based on intended

⁷ June 30, 2009 data was unaudited and does not include year-end adjustments and transfers to reserves.

⁸ These four reserves included the Employee Benefit Accrued Liability Reserve, the Unemployment Insurance Reserve, the Property Loss and Liability Reserve, and the CTE Equipment Reserve. The CTE Equipment Reserve was also appropriately established subsequent to a favorable majority vote of the component school districts' Boards of Education.

future expenditures or estimable liabilities. Withdrawals from the reserves should comply with statute and be directly related to the purpose of the reserve.

BOCES allocated \$6.1 million⁹ to reserves during our audit period. However, we found that BOCES officials did not clearly report these reserve allocations to its districts during this time or for the prior two-year period July 1, 2005 to June 30, 2007. In addition, BOCES does not have any policies, procedures, or written plans for the funding and use of moneys allocated to reserves. Further, BOCES does not report on any surplus or refund due and payable to each district, when refund payments are made. Therefore, these reserve fund allocations were potentially made without the knowledge of component and participating school districts, and consequently those districts' taxpayers.

BOCES officials stated that transfers to most reserves are included as budgeted expenditures in each detailed Cooperative Services (CoSer)¹⁰ budget and the Central Administration budget, which they provide to the component and participating school districts¹¹ prior to the start of the fiscal year. These program budgets are prepared by committees made up of component school district superintendents.¹² Allocations to the Unemployment Reserve, the Workers' Compensation Reserve (which was established without specific statutory authority), and the ERS Contribution Reserve are shown as a budgeted expenditure for employee benefits in the individual CoSer budgets, and allocations to the Employee Benefit Accrued Liability Reserve are shown as a post-employment benefits expenditure in the Central Administration budget. The Property Loss and Liability Reserve was originally established and funded as an accounts payable liability in the 2004-05 fiscal year. The funding for such was shown as budgeted expenditures for telecommunications in NERIC¹³ CoSer budgets.¹⁴ This practice does not clearly indicate that these moneys are allocated to reserves; rather, they appear as budgeted expenditures. Such lack of disclosure compromises the transparency of BOCES operations and denies the school districts complete knowledge of how BOCES is ultimately using money paid by districts for BOCES services.

In addition, BOCES officials transferred \$250,000 of surplus to the CTE Equipment Reserve in 2008-09, without clearly indicating such to the component and participating districts. BOCES does not provide a surplus report indicating the cost allocated to that district in the past year's budget, the actual expenditures associated with providing shared services to the district during the year, and any surplus or refund due and payable to that district. Therefore, money allocated to this reserve was not clearly identified.

⁹ Includes funding of the following reserves: Employee Benefit Accrued Liability Reserve of \$3 million, Unemployment Insurance Reserve of \$250,000, Workers' Compensation Reserve of \$1 million, CTE Equipment Reserve of \$250,000, ERS Contribution Reserve of \$630,000 and Property Loss Reserve of \$1 million.

¹⁰ The main vehicle for BOCES services provided to its school districts. CoSers programs must be approved by the State Education Department (SED).

¹¹ For the CoSers in which they participate

¹² Participation in budget preparation committees is voluntary.

¹³ Northeastern Regional Information Center

¹⁴ The Property Loss and Liability Reserve was established in May 2009 for potential estimated losses due to a dispute with a telecommunications provider related to services provided for NERIC. Reserve funding came from a previously created account payable liability for the telecommunications provider. The reserve balance was supported with a statement from the vendor.

Although some Board members, who represent the 23 component school districts,¹⁵ told us that BOCES business officials provide monthly Treasurer's reports¹⁶ including the balance of reserve bank accounts to the Board, and that BOCES officials are verbally communicating with the Board regarding reserve funding, there was no written documentation of this communication.

Reserve Balances and Use of Funds

Although there is no statutory limit on the amount in most reserves, the balances in statutorily authorized reserves should be reasonable and based on intended future expenditures or estimable liabilities. In addition, reserve funds should be accounted for separately and interest earnings should be allocated to the reserves. Also, withdrawals from the reserves should comply with statute and be directly related to the purpose of the reserve.

Expenditures from BOCES reserves¹⁷ were in compliance with statute and directly related to the purpose of the reserve, with the exception of withdrawals from the employee benefit accrued liability reserve. In addition, BOCES properly accounted for each reserve separately. However, the balances of the reserve funds were not adequately supported with intended future expenditures or related liability calculations. We also found that BOCES officials did not deposit interest earnings to two of BOCES' six legally established reserves - the Unemployment Insurance Reserve and the ERS Contribution Reserve.

Employee Benefits Accrued Liability Reserve (EBALR) – The BOCES established this reserve in March 2007, by board resolution, for the purpose of paying accrued benefit liabilities for retirees. An EBALR, per statute, is used to make cash payments of the monetary value of accrued or accumulated but unused sick leave, holiday leave, vacation leave, etc. due to employees upon separation of service. BOCES officials stated that the EBALR that BOCES created was intended to be used to pay retiree health insurance payments and that these payments are not related to compensated absences earned and payable at the time of retirement. This is not a legally permissible use of this type of reserve. During our audit period, BOCES officials allocated \$3,034,128 to this inappropriately used reserve without clearly identifying these allocations as reserve funding.¹⁸ Payments made from this reserve during our audit period totaled \$1,646,904. Of these payments, we were able to trace one payment for \$158,737 to a compensated absence payment; the remaining \$1,488,167 could not be traced to any specific payments and appeared to be used for general fund cash flow purposes. At the conclusion of fieldwork, the balance of this reserve was almost \$4 million. EBALR moneys in excess of the fund's liabilities can be transferred only to specific reserve funds. They cannot be used to pay for operating expenses other than those associated with compensated absences.

Unemployment Reserve – The Board established this reserve in 1978 for funding payments to reimburse the State Unemployment Insurance Fund for actual claims filed. The balance as of June

¹⁵ Although the ten Board members represent all 23 component school districts, each originates from one of the component school districts.

¹⁶ We reviewed the Treasurer reports to verify that they included reserve fund balances.

¹⁷ Refers to spending from the Unemployment Reserve, averaging \$59,000 annually; BOCES did not use funds from the CTE Equipment Reserve or the ERS Contribution Reserve during our audit period. In addition, although BOCES used the Worker's Compensation Reserve for related expenses, there is no clear statutory authority for them to have such a reserve.

¹⁸ BOCES has deposited into this reserve account approximately 3 percent of actual salary expenditures from the general and Federal funds, and budgeted these allocations as expenditures for retiree health insurance without identifying these moneys as reserve allocations.

2009 (prior to year-end adjustments) was approximately \$489,000. BOCES has deposited into the reserve approximately 0.25 percent of actual salary expenditures from the general and Federal funds, and budgeted the added amounts as expenditures for unemployment insurance without identifying these moneys as reserve allocations. These allocations totaled \$250,000 during the audit period. Payments made from this reserve during our audit period (averaging \$59,000 a year) were in compliance with statute and directly related to the purpose of the reserve. However, BOCES does not have a specific documented plan for funding and use of moneys in this reserve. In addition, BOCES officials maintain this reserve fund in a non-interest bearing account. We estimate that the additional interest earnings which should have been deposited to the reserve during our audit period alone totaled approximately \$18,509.

CTE Equipment Reserve – This reserve was established by the BOCES board in April 2005 to be operated in accordance with Education Law and the Commissioner’s Regulations. While the resolution establishing this reserve does not define its purpose, BOCES officials indicated that it was created to buy future equipment for career and technical education programs. As of June 30, 2009 (prior to final year-end adjustments), the balance in this reserve was \$302,869. Education Law allows two methods of funding such a reserve: 1) proceeds from the sale of career education instructional equipment no longer needed by BOCES, and 2) a depreciation allowance for equipment used in career and technology instruction. However, instead of using one of the methods prescribed by law, BOCES officials inappropriately transferred \$250,000 of surplus funds to this reserve in the 2008-09 fiscal year. This transfer could not be linked to depreciation schedules or sales of equipment. The reserve has not been otherwise funded or used during the period July 1 2005 through June 30, 2009. Furthermore, BOCES is statutorily required to maintain accurate records of user contributions to the CTE equipment reserve fund on a CoSer level; and to submit reports of the financial status of their CTE equipment reserve to the New York State Education Department (NYSED). However, BOCES officials were unable to provide records of user contributions and they informed us that they have not submitted reports on the CTE equipment reserve to NYSED. Lastly, BOCES officials have not established a specific documented plan for the CTE Equipment Reserve’s funding and use.

ERS Contribution Reserve – BOCES officials created this reserve without the statutorily required BOCES board approval and did not have a specific documented plan for the funding and use of the reserve. The reserve had a balance of \$1,421,639 as of June 30, 2009 (prior to year-end adjustments). No payments have been made from the reserve during our audit period. BOCES’ annual ERS expenditures are budgeted for in its CoSer budgets; if the budgeted amount exceeds the amount actually billed and paid, the excess budgeted amount is transferred to the reserve for future ERS payments. These allocations totaled \$631,597, during our audit period. BOCES is not clearly indicating to its districts that such surplus funds are being used to fund this reserve. In addition, BOCES officials do not allocate interest earned to this reserve. We estimate that the additional interest earnings which should have been deposited to the reserve during the audit period alone totaled approximately \$28,433.¹⁹

BOCES officials believe that the ERS reserve is not truly a reserve, but rather an accounting treatment used to set aside funds for future ERS payments. However, there is no such method for BOCES to set aside funds for future ERS payments other than a retirement contribution reserve. For

¹⁹ For this calculation, we used a conservative interest rate of 2 percent, compounding annually. This interest rate was used to reflect the average interest rates for three-month certificates of deposit during the audit period; we obtained interest rate information from the Federal Reserve Statistical Release.

all intents and purposes, the funds that BOCES has set aside for the payment of future ERS expenses is a retirement contribution reserve.

The BOCES' lack of a documented plan for the use of these reserve funds – combined with the failure to report the allocations made to reserves, or adequately justify the reserve balance – demonstrates inadequate planning and a lack of transparency in BOCES' reporting to the school districts.

Workers' Compensation Reserve

Currently there is no clear statutory authority for a BOCES to create a Workers' Compensation Reserve. However, BOCES established a Workers' Compensation Reserve by Board resolution in April 2002 to pay for BOCES workers' compensation claims. During our audit period, BOCES officials allocated over \$1 million to this reserve without clearly identifying these allocations as reserve funding.

BOCES' expenditures averaged \$364,000 a year during our audit period. At the conclusion of our fieldwork, the balance in this reserve was over \$1 million. In the absence of clear statutory authority and in view of the amount accumulated, BOCES officials should return the moneys in this reserve to operating funds and apportion the excess funds to the component and participating school districts.

Recommendations

1. The Board and BOCES officials should develop written policies and procedures to ensure that reserve funds are clearly authorized by law and properly established by Board vote in compliance with statutory requirements. These policies and procedures should include a specific documented plan for the funding and use of reserve funds.
2. The Board should ensure that participating and component districts are properly notified of BOCES' intent to fund reserves. Amounts budgeted for the purpose of funding reserves should be clearly identified.
3. BOCES officials should ensure that reserve fund moneys are maintained in interest-bearing accounts and that interest earnings are appropriately allocated to reserve funds according to statutory requirements.
4. BOCES management should discontinue the inappropriate use of the Employee Benefits Accrued Liability Reserve (EBALR). Funds in excess of the amounts necessary to satisfy genuine EBALR liabilities can only be transferred to certain other reserves authorized by law.
5. The Board should review BOCES' legally established reserves and determine if the balances are necessary and reasonable. To the extent that they are not, BOCES officials should reduce the reserves to reasonable levels in compliance with statutory restrictions.
6. BOCES management should discontinue the use of its Workers' Compensation Reserve. The funds in this reserve should be returned to operating funds and properly apportioned to the component and participating school districts.

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 Clerk's office.

Our Office is available to assist you upon request. If you have any further questions, please contact Ann Singer, Chief of Regional and Statewide Projects, at (607) 721-8310.

Sincerely,

Steven J. Hancox
Deputy Comptroller
Office of the State Comptroller
Division of Local Government
and School Accountability

APPENDIX A

RESPONSE FROM BOCES OFFICIALS

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



Board of Cooperative Educational Services
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Leaders for Educational Excellence

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April 15, 2010

Mr. Steven J. Hancox
Deputy Comptroller
Office of the State Comptroller
Division of Local Government
and School Accountability
110 State Street
Albany, New York 12236

Re: Audit Report #59-9-66

Dear Mr. Hancox:

This letter represents the response of the Albany-Schoharie-Schenectady-Saratoga BOCES (hereinafter referred to as Capital Region BOCES or BOCES) to your draft audit report concerning the policies and procedures in place to support reserve balances.

The Capital Region BOCES believes that its conservative approach to the strategic management of its long term fiscal health has been responsible and prudent, as evidenced in your statement that with but one exception, ***“Expenditures from BOCES reserves were in compliance with statute and directly related to the purpose of the reserve.”***

See
Note 1
Page 16

We also recognize that there are always opportunities to improve the effectiveness of operations and therefore appreciate the general recommendations made in the audit.

Although we generally agree with the findings and recommendations made in the audit, there are several areas where your opinion(s) differ from the professional judgment of the BOCES external auditor, attorney and senior financial staff. These differences will be explained in this response.

1. Recommendation #1

The Board and BOCES officials should develop written policies and procedures to ensure that reserve funds are clearly authorized by law and properly established by Board vote in compliance with statutory requirements. These policies and procedures should include a specific documented plan for the funding and use of reserve funds.

Your audit questions the “appropriate” establishment of the ERS Contribution Reserve and the “alleged” lack of authority for the BOCES to establish a Workers’ Compensation Reserve. Each has a different set of underlying circumstances and therefore our response will deal with each separately.

The BOCES is also cited for not having established “Board Policies” for reserves. However, when we asked for a sample of such a policy for guidance, we were told you did not have such a policy.

See
Note 2
Page 16

a) **ERS Contribution Reserve** - *The BOCES initially established a liability account on its balance sheet for the accrual of the employer's portion of the retirement system contribution. Excess accrued amounts were then transferred to a reserve account based upon the recommendation of our external auditor. At that time, the BOCES Board did not approve the official establishment of the reserve. The BOCES Board has since approved the establishment of the ERS Reserve by resolution.*

b) **Workers' Compensation Reserve** - *During the exit conference we learned that OSC audits across the state have opined that BOCES do not have clear legal authority to establish a Workers' Compensation Reserve. BOCES legal counsel does not agree that the BOCES lacks authority to maintain a reserve fund from which it can pay workers compensation benefits. BOCES, which self-insures for workers' compensation, is granted the requisite authority by General Municipal Law (GML) §6-j.*

See
Note 3
Page 16

Although BOCES acknowledges that GML §6-j, as originally enacted in 1949, did not expressly list BOCES as one of the governmental bodies authorized to create workers' compensation reserve funds, legal counsel believes that the audit report erroneously ignores the Legislature's 1987 addition of a new paragraph five to GML §6-j, which specifically includes BOCES among the governmental entities that are directed to handle year-end workers' compensation reserve fund balances in a particular manner. For the OSC to contend that BOCES does not have authority to maintain a workers' compensation reserve fund when paragraph five of GML §6-j specifically tells a BOCES how such funds should be managed, assigns, in our view, an erroneous construction to the statute. BOCES respectfully disagrees with the audit finding at this time.

See
Note 3
Page 16

2. Recommendation #2

The Board should ensure that participating and component districts are properly notified of BOCES' intent to fund reserves. Amounts budgeted for the purpose of funding reserves should be clearly identified.

Capital Region BOCES Board and staff have worked very hard during the last several years to build the effectiveness, efficiencies and capacity to serve its component districts. Communication, transparency and interaction with component Boards of Education, component district superintendents and other administrators have been at the center of this initiative.

As thoroughly explained to OSC audit staff, Capital Region BOCES uses a Superintendents' Advisory Committee structure in the development of budgets. The committee structure is segregated by functional service areas and is intended to offer a broad array of representation across the districts.

In many ways the underlying operational structure of a cooperative service agency such as the BOCES affects many of its fiduciary and fiscal practices. This is true as it relates to budget development and the funding of reserves which are part of a healthy financial infrastructure.

Because the BOCES is required to develop a budget for each of its more than 100 cooperative programs (Co-Ser), the BOCES budgets for allocations of certain

appropriations to reserves, as suggested and recommend in Page 4 of the audit.¹ This is true for all but two (2) of the BOCES reserves. The only two that have not been funded in this manner are the Career and Technical Equipment Reserve Fund and the Property Loss and Liability Reserve Fund.

See
Note 4
Page 16

Although we are disappointed that OSC auditors did not interview component school personnel (Superintendents/Board of Education members) to our knowledge prior to offering their opinion that Capital Region BOCES has not been transparent in its financial and operational disclosure, we do recognize the need to continually improve communications and transparency of operations.

The BOCES is taking steps to establish clear parameters for funding and communication of reserve balances to component schools, such as presenting reserve balances in our budget documents and at the BOCES Annual Meeting.

See
Note 5
Page 16

3. Recommendation # 3

BOCES officials should ensure that reserve fund monies are maintained in interest-bearing accounts and that interest earnings are appropriately allocated to reserve funds according to statutory requirements.

BOCES acknowledges that the Unemployment Insurance Reserve was not maintained in an interest bearing account. This oversight has been corrected.

4. Recommendation #4

BOCES management should discontinue the inappropriate use of the Employee Benefits Accrued Liability Reserve (EBALR). Funds in excess of the amounts necessary to satisfy genuine EBALR liabilities can only be transferred to certain other reserves authorized by law.

As noted in the audit, the BOCES has funded an accrued benefit liability reserve through a budgetary appropriation that represents approximately 3% of salary, and is applied uniformly across all Co-Ser budgets.

See
Note 6
Page 16

We disagree with the opinion that there was inadequate identification of the funding and use of the reserve to component boards of education and superintendents. Funding and application of reserves has been clearly communicated during budget development and budget communications. In addition, the amount of the reserve is well under the Compensated Absences balance reported annually on the BOCES audited financial statement.

See
Note 7
Page 17

We do agree that adjustments will need to be made to the accounting methodology used to address the significant long-term liability related to these legacy costs. We will be working with our external CPA firm to develop and document a more palatable and transparent solution.

¹ve funds are typically funded from amounts raised through the annual budget process, transfers from unexpended
s of existing appropriations, and surplus monies.

5. Recommendation #5

The Board should review BOCES' legally established reserves and determine if the balances are necessary and reasonable. To the extent that they are not, BOCES officials should reduce the reserves to reasonable levels in compliance with statutory restrictions.

As stated previously, the Capital Region BOCES believes it has acted prudently, responsibly and conspicuously in its action to improve the fiscal health of the organization to the benefit of the districts it serves. This includes but is not limited to many of the processes and procedures related to the establishment of budgets and funding of reserves at reasonable balances.

Although not specifically identifiable in a written protocol or process, we substantiate these actions and process as follows:

| | | <u>Authorization & Establishment</u> | <u>Funding</u> | <u>Application or Use</u> | <u>Substantiation of Reserve Balance</u> |
|-----|--|---|---|--|--|
| (a) | <i>Accrued Benefit Liability Reserve</i> | <i>By Board Resolution - March 2007</i> | <i>Funding by program budgets at 3% of salary via budgetary appropriation and communicated during budget development and in public budget documents</i> | <i>Applied against Administrative budget to mitigate costs of retiree health insurance</i> | <i>As of June 30, 2009 Compensated Absence Balance was \$18,184,794 GASB45 OPEB Liability \$11,084,800</i> |
| (b) | <i>Unemployment Reserve</i> | <i>By Board Resolution in 1978</i> | <i>.25% of salary via budgetary appropriation communicated in budget development and public budget documents</i> | <i>Direct payment to the NYS Unemployment Insurance Fund</i> | <i>Approximate 2008/09 Annual Expense \$73,253 Approximate 2008/09 Annual Funding \$127,651</i> |
| (c) | <i>CTE Equipment Reserve</i> | <i>By Board Resolution April 2005</i> | <i>Transfer from surplus, authorized by superintendents and resolution by BOCES Board. Future funding will be by budgetary appropriation</i> | <i>Finance acquisition and replacement of instructional technology equipment</i> | <i>Total value of "capital asset" depreciation used in the CTE instruction programs</i> |
| (d) | <i>ERS Contribution Reserve</i> | <i>Re-established by Board resolution July 2009</i> | <i>Based on applicable salary paid, ERS trend analysis, and economic conditions</i> | <i>To fund employer portion of amount payable to ERS</i> | <i>The 2008/09 ERS employer liability was \$1,815,374</i> |
| (e) | <i>Workers' Compensation Reserve</i> | <i>By Board resolution April 2002</i> | <i>1% of salary via budgetary appropriation communicated during budget development and in public budget documents</i> | <i>To pay benefits and administrative expenses related to a self-funded workers' compensation plan</i> | <i>2008/09 incurred benefits costs totaled \$855,948. Total benefit and lost time incurred from 2002/03 totaled \$1,573,270.</i> |

| | | | | | |
|-----|-------------------------------------|---|-------------------------|--|---|
| (f) | Property Loss and Liability Reserve | By Board resolution 2004/05 fiscal year | Budgetary appropriation | Based on claims made by Verizon regarding a multi-year dispute over inaccurate invoices. | The Verizon claim currently under dispute is approximately \$640,000. |
|-----|-------------------------------------|---|-------------------------|--|---|

6. Recommendation #6

BOCES management should discontinue the use of its workers' compensation reserve. The funds in this reserve should be returned to operating funds and properly apportioned to the component and participating school districts.

As previously discussed under Recommendation #1, BOCES believes that the current GML §6-j authorizes BOCES to maintain a workers' compensation reserve fund. You state numerous times that BOCES lacks the "clear" authority to have a workers' compensation reserve, without fully explaining that this is an unwritten opinion of your legal counsel and not a matter of fact. Further, there is no explanation of the 1987 Amendment to Section 6j of GML, which added a specific reference to BOCES in the statute. However, in order to eliminate any further complications or differences of opinion relative the authority of a BOCES to establish a workers' compensation reserve, Capital Region BOCES is seeking legislative clarification.

In addition, we are also investigating the viability of joining a workers' compensation consortium, which will eliminate the need for the BOCES to hold a reserve for self insurance of its workers' compensation liability.

See
Note 3
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The Capital Region BOCES is committed to providing a stable foundation to effectively continue its mission as an educational service agency. This commitment is rooted in sound fiscal and operational practices and in a participative and transparent relationship with its component districts.

We appreciate the professionalism of your audit staff who conducted the audit and their recommendations to improve the health and welfare of the BOCES operations.


In closing, we thank you for your thoughts and opinions to enhance our operation. We also hope you are equally receptive to our efforts to clarify the legal standing of the workers' compensation reserve.

Sincerely, .

Board of Cooperative Educational Services


Sandra Beloncik - Board President


John T. Phelan - Audit Committee Chair


Charles S. Dedrick, Ed.D. - District Superintendent

APPENDIX B

OSC COMMENTS ON BOCES' RESPONSE

Note 1

We have added a footnote to clarify that this statement referred to BOCES use of funds from one reserve – the Unemployment Reserve - and is not the conclusion of this audit on BOCES overall practices for establishing and funding reserves. Our audit found that BOCES officials have indeed accumulated significant amounts of money in reserves that they are not authorized to have, or have used those reserves for unauthorized purposes without transparently reporting such activity to component and participating school districts.

Note 2

BOCES is responsible for establishing its own policies and procedures.

Note 3

BOCES currently lack specific authority to have a workers' compensation reserve. Historical amendments to General Municipal Law §6-j, specifically that of subsection 5, do not illustrate intent by State policymakers to add BOCES to the entities that are authorized to have such a reserve. BOCES can choose to pursue changes to the statute through the State Legislature.

Note 4

None of BOCES reserves were funded through transparent budget appropriations. The four reserves BOCES officials said were funded as we recommend were actually funded with appropriations labeled as being for current fringe benefit expenditures, not for reserves. This method of funding reserves – without better disclosure of the purpose of the appropriations – is not sufficient to provide transparency.

Note 5

BOCES officials have the responsibility to clearly communicate to their component and participating districts their intention to fund reserves through charges to those districts, whether through budgeted appropriations or through the use of surpluses. Five BOCES Board members told us that they receive monthly treasurer reports that contain reserve fund cash balances, and that reserve issues are discussed verbally at Board meetings. Depending on Board members to relay the results of informal discussions about reserves to their respective school districts does not ensure that all interested parties are adequately informed about BOCES use of district and taxpayer funds. Rather, BOCES officials should document the specific plans for the funding and use of reserve funds.

Note 6

Budgetary appropriations used to fund the employee benefits accrued liability reserve showed that the funds would be used for retiree health insurance, and did not indicate that these appropriations were used to fund a reserve.

Note 7

Reporting reserve fund balances alone does not provide districts and their taxpayers with adequate knowledge of the intended use and ultimate disposition of funds collected from those districts. Budgetary appropriations used to fund reserves should be clearly labeled as such.