

Victor Central School District

Financial Management

JUNE 2019



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

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Report Highlights

Victor Central School District

Audit Objective

Determine whether the Board and District officials adopted realistic budgets and effectively managed fund balance and reserves.

Key Findings

The Board and District officials:

- Adopted conservative budgets that resulted in circumventing the statutory limit on surplus fund balance by making \$2.4 million in unbudgeted year-end transfers to reserves and appropriating \$1.6 million in fund balance that was not used.
- Annually increased meal prices, despite repeated warnings from its external auditor that the school food service surplus fund balance was excessive.
- Overfunded two general fund reserves with balances totaling more than \$1.3 million as of June 30, 2018.

Key Recommendations

- Develop and adopt budgets that include more realistic estimates for revenues and appropriations and the amount of fund balance and reserves that will be used to fund operations.
- Develop a plan to continue reducing the school food service fund balance to a reasonable level.
- Review and fund reserve balances to reasonable levels in accordance with applicable statutes.

District officials generally disagreed with our findings and recommendations. Appendix B includes our comments on issues raised in the District's response letter.

Background

The Victor Central School District (District) serves the Towns of Victor, East Bloomfield and Farmington in Ontario County, the Town of Perinton in Monroe County and the Town of Macedon in Wayne County.

The District is governed by an elected seven-member Board. The Superintendent of Schools is responsible, along with other administrative staff, for managing day-to-day operations under the Board's direction. The Assistant Superintendent for Business is responsible for the administration and supervision of financial activities. The Board, Superintendent and Assistant Superintendent for Business are responsible for developing the budget.

The current Assistant Superintendent for Business began in February 2018.

Quick Facts

2018-19 Appropriations	\$69.2 million
Enrollment	4,400
Total Reserves as of June 30, 2018	\$8.5 million

Audit Period

July 1, 2015 – February 7, 2019

Financial Management

What Is Effective Financial Management?

To effectively manage financial condition, the board should 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. To provide for cash flow and unanticipated events, a district may retain a portion of fund balance, referred to as surplus fund balance.

District officials should ensure that fund balance does not exceed the amount allowed by New York State Real Property Tax Law,¹ (RPTL) which currently limits surplus fund balance² to no more than 4 percent of the next year's appropriations. Any surplus fund balance that exceeds the statutory limit should be used to pay for one-time purchases, fund needed reserves, pay down debt or reduce the next year's real property tax levy. When fund balance is appropriated to finance operations, the district is budgeting for a planned operating deficit equal to the amount of fund balance appropriated.

The school food service fund is used to account for and report transactions of the school district breakfast, lunch and milk programs. In addition to direct program costs, such as food purchases and food service workers' salaries and benefits, this fund can be charged, to the extent funds are available, indirect costs such as utilities, custodial and administrative expenditures, using a cost allocation that must be approved by the New York State Education Department (SED). While the budget is not submitted to the voters for approval, appropriations must balance with estimated revenues. District officials should limit year-end fund balance to a reasonable level to manage cash-flow and unanticipated costs and ensure students are not charged higher meal prices than necessary.

Districts are legally allowed to establish reserves for certain future purposes (e.g., capital projects, retirement expenditures). To be transparent, the Board should include the amounts to be reserved in its annual budget to give taxpayers the opportunity to know and approve the board's plans for funding reserves.³ District officials should plan for the funding and use of reserves by balancing the desire to accumulate funds for future needs with the obligation to make sure real property taxes are not higher than necessary.

It also is important for district officials to develop a comprehensive multiyear financial plan to estimate the future costs of ongoing services and future needs and plan for various methods or resources to finance them.

¹ New York State Real Property Tax Law, Section 1318

² Surplus fund balance is defined as unrestricted fund balance minus appropriated fund balance and encumbrances included in committed and assigned fund balance. See our accounting bulletin at www.osc.state.ny.us/localgov/pubs/releases/gasb54.pdf

³ Refer to our publication Reserve Funds available at www.osc.state.ny.us/localgov/pubs/lmg/reservefunds.pdf

The Board Overestimated Expenditures and Appropriated Fund Balance That Was Not Needed

We compared appropriations and estimated revenues with actual operating results for 2015-16 through 2017-18 and found that the total budget variance exceeded \$5 million during that period (Figure 1). While estimated revenues appeared reasonable, appropriations were overestimated by a total of \$4.2 million over three years. Although appropriations were more reasonable in 2017-18, there were still significant variances in certain line items.

The most significant variances for the three years were for health insurance (\$2.4 million, 8 percent), retirement contributions (\$1.6 million, 13 percent), fuel and gasoline (\$1.2 million, 49 percent) and principal and interest on debt (\$800,000, 4 percent). While overall revenue variances were \$922,730 over three years, the favorable variance contributed to total budget variances and resulting operating surpluses, instead of the planned operating deficits that should have resulted from the Board's appropriation of fund balance.

Figure 1: Budget Variances

	2015-16	2016-17	2017-18	Totals
Appropriations	\$63,969,683	\$65,102,872	\$66,352,887	\$195,425,442
Actual Expenditures	\$62,070,976	\$63,402,859	\$65,792,862	\$191,266,697
Overestimated Appropriations	\$1,898,707	\$1,700,013	\$560,025	\$4,158,745
Percentage Overestimated	3%	3%	1%	
Estimated Revenues	\$62,777,159	\$64,292,191	\$65,534,206	\$192,603,556
Actual Revenues	\$63,187,614	\$64,161,051	\$66,177,621	\$193,526,286
Under/(Over) Estimated Revenues	\$410,455	(\$131,140)	\$643,415	\$922,730
Percentage Underestimated	1%	0%	1%	
Total Budget Variance	\$2,309,162	\$1,568,873	\$1,203,440	\$5,081,475
Operating Surplus	\$1,116,638	\$758,192	\$384,759	\$2,259,589
Increase in Real Property Tax Levy	\$1,209,230	\$1,572,254 ^a	\$2,224,214	\$5,005,698

^a The District overrode the tax cap by \$812,481 in 2016-17.

By adopting overly conservative budgets, the Board gave taxpayers the impression that it needed to both increase taxes and use appropriated fund balance and reserves to close projected budget gaps. The Board annually appropriated \$529,000 of fund balance as a financing source in the 2015-16 through 2017-18 budgets, which should have resulted in \$529,000 in planned operating deficits each year. However, due to budget variances, the District realized operating surpluses and did not use any of the \$1.6 million in appropriated fund balance to fund operations.

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

for by statute and is a circumvention of the statutory limit imposed on the level of surplus fund balance.

District officials indicated in their reserve plan that they intentionally budget conservatively. However, budgeting practices that annually overestimate appropriations and underestimate revenue can result in real property tax levies that are higher than necessary and budgets that are not an effective tool for financial management.

Based on our analysis of the 2018-19 adopted budget, officials budgeted similarly to previous years. The Board increased overall appropriations even though actual expenditures were less than budgeted the previous years. As a result, it is likely that the District will end 2018-19 with an operating surplus, appropriated fund balance will be unused and fund balance will continue to increase.

The Board Was Not Transparent When Funding Reserves

The District reported surplus fund balance at 4 percent in compliance with RPTL (Figure 2) in 2015-16 through 2017-18. However, this was achieved, in part, by making year-end unbudgeted transfers totaling approximately \$2.4 million to reserves (capital reserve – \$2.2 million and tax certiorari reserve – \$150,000) to reduce the amount of reported surplus fund balance. Prior to these decisions, year-end surplus fund balance exceeded the allowed fund balance level.

Figure 2: Effect of Unbudgeted Transfers on Reported Surplus Fund Balance

	2015-16	2016-17	2017-18
Surplus Fund Balance Before Transfers	\$3,472,266	\$3,445,901	\$3,489,234
Fund Balance as a Percentage of the Next Year's Budget	5%	5%	5%
Less: Unbudgeted Transfers to Reserves	\$868,153	\$791,784	\$720,319
Reported Surplus Fund Balance at Year-End	\$2,604,113	\$2,654,117	\$2,768,915
Next Year's Budget	\$65,102,872	\$66,352,887	\$69,222,879
Fund Balance as a Percentage of the Next Year's Budget	4%	4%	4%

Instead of including funding for reserves in the annual budget, District officials transferred money, at the end of the fiscal year, to the capital and tax certiorari reserves from operating surpluses generated by their conservative budgets, to stay within the statutory surplus fund balance limit.

General Fund Surplus Fund Balance Exceeded the Statutory Limit

Because the District did not use its appropriated fund balance, actual surplus fund balance exceeded the statutory limit. The District further circumvented the statutory limit by maintaining unnecessary or overfunded reserves.⁴ We recalculated the District's surplus fund balance, which in total exceeded the statutory fund balance limit by 4 percentage points as of June 30, 2018.

Figure 3: Recalculated Fund Balance as of June 30, 2018

Surplus Fund Balance	\$2,768,915
Add: Unused Appropriated Fund Balance	\$529,000
Add: Unused Debt Service Funds	\$2,520,304
Recalculated Surplus Fund Balance	\$5,818,219
2018-19 Budget Appropriations	\$69,222,879
Percentage	8%

Despite its budgetary surpluses⁵ and excess fund balance and reserves,⁶ the Board continued to increase the tax levy by 3 to 5 percent each year. The Board increased the tax levy by \$5 million (13 percent) over the last three years (Figure 1). The Board unnecessarily overrode the tax cap limit⁷ by \$812,481 when adopting its 2016-17 budget, despite having excess available funds that could have been used to reduce the tax levy. The Board increased the tax levy again by \$1.9 million (4 percent) in adopting its 2018-19 budget.

School Food Service Fund Balance Was Excessive

As of June 30, 2018, the school food service fund reported surplus fund balance of \$808,388, approximately 50 percent of annual expenditures. The fund balance has been close to \$800,000 since 2012, and could have been reduced to fund the budget and reduce student meal costs.

Although there was a small operating deficit in 2015-16, this fund generated small operating surpluses in the last two years resulting in increases to the already excessive fund balance. District officials did not implement any corrective action

4 Refer to The Board Overfunded and Did Not Use Reserves.

5 Refer to The Board Overestimated Expenditures and Appropriated Fund Balance That Was Not Needed.

6 Refer to The Board Overfunded and Did Not Use Reserves.

7 In 2011, the New York State Legislature enacted a law establishing a property tax levy limit, generally referred to as the property tax cap. Under this legislation, the property tax levied annually generally cannot increase by more than 2 percent or the rate of inflation, whichever is lower, with some exceptions. School districts may override the tax levy limit by presenting to the voters a budget that requires a tax levy that exceeds the statutory limit, provided the budget is approved by 60 percent of the votes cast.

to reduce the surplus fund balance despite the fact that the District's external auditors cited the excessive balance in at least the last four annual audit reports they issued. Instead, officials increased meal prices each year, by an average of 4 percent in 2016-17 and 2017-18 and 9 percent for 2018-19.

The Board may consider the need for and reasonableness of establishing and funding a capital reserve for food service equipment. By appropriating remaining surplus fund balance in future budgets, the Board could reduce meal prices and gradually reduce the excess fund balance accumulated from prior years' student meal purchases, then charge prices currently necessary to provide meals to students.

After our audit fieldwork,⁸ District officials provided us with documentation of certain actions they have recently taken to reduce fund balance, including installing new coolers and a freezer (\$38,000), and hiring a nutritionist and allocating salaries and benefits for an additional cleaner to the fund (approximately \$85,000 additional salary and benefits). They are also in the process of purchasing a new food delivery truck.

The Board Did Not Adopt a Multiyear Financial Plan

The Board has not adopted a comprehensive written multiyear financial plan to help officials address and plan for the use of fund balance, including reserve funds, and prioritize and plan for future capital needs.

At the beginning of our audit fieldwork,⁹ the Assistant Superintendent for Business told us that the business office was working on a plan. In December 2018, he provided us with a multiyear financial plan for the 2019-20 through 2023-24 fiscal years. However, he told us that this was a new internal business office document and was not provided to the Board for review or approval.

As the District moves forward, using the multiyear plan can assist the Board in making timely, informed and documented decisions about programs and operations and help effectively manage fund balance in the best interest of taxpayers.

How Should the Board Establish, Fund and Use Reserves?

A board may establish various reserves in accordance with applicable laws to provide financing for specific purposes. Money set aside in reserves must be used in compliance with statutory provisions, which determine how reserves are established and how they may be funded, expended and discontinued. Generally,

⁸ At a March 28, 2019 meeting

⁹ November 14, 2018

school districts are not limited as to how much money can be held in reserves. However, reserve balances should be reasonable and necessary.

The board should periodically analyze the reasonableness of the balances in its reserves. When conditions warrant (subject to legal requirements), the board should reduce reserve funds to reasonable levels or liquidate and discontinue a reserve fund that is no longer needed or whose purpose has been achieved.

Any interest earned on reserve fund money must accrue proportionately to each reserve fund. When reserve funds are commingled with other District money for investment purposes, each reserve fund must receive its share of interest.

A debt service reserve must be established if unexpended bond proceeds remain on a capital improvement financed with debt, or if State or federal aid is received for a capital improvement for which there is outstanding debt.¹⁰ The balance and any interest earned on this money must be used to help finance related debt service costs. This money must be set aside and accounted for in the debt service fund.

It is important that the board adopt a written plan that states its rationale for establishing reserve funds, objectives and optimum funding levels for each reserve and conditions under which reserves will be used or replenished.

The Board Overfunded and Did Not Use Reserves

As of June 30, 2018, the District had eight general fund reserves,¹¹ with balances totaling \$6 million, and a debt service reserve totaling \$2.5 million.

The Board annually budgeted for the use of the workers' compensation, unemployment, employee benefit accrued liabilities (EBALR) and liability reserves. However, the information provided to the public listed a total appropriated reserve amount and did not break down the amount to be used from each reserve.

Further, the District did not use \$811,897 (63 percent)¹² of the \$1.3 million in reserves appropriated from 2015-16 through 2017-18, because related costs were covered by operating surpluses generated by conservative budgets.¹³ For example, the District did not use any of the amounts appropriated from the unemployment (\$89,681) and liability (\$528,205) reserves for all three years.

10 New York State Local Finance Law (LFL), Section 165.00 and General Municipal Law (GML), Section 6-I

11 Unemployment insurance, tax certiorari, retirement contribution, liability, workers compensation, employee benefit accrued liability, repair and capital

12 All of the appropriated liability (\$528,205) and unemployment insurance (\$89,681) reserves and a portion of the EBALR (\$144,011, 33 percent) and workers compensation (\$50,000, 20 percent) reserves.

13 Refer to The Board Overestimated Expenditures and Appropriated Fund Balance That Was Not Needed.

Furthermore, funds from the liability reserve should not have been appropriated because an eligible liability was not known when the budget was approved.

In addition, with the exception of the capital reserve, District officials have not allocated interest to any of the reserves recorded in the general fund in at least ten years. Instead, all interest earned on reserve balances was added to unrestricted general fund cash because reserve fund money was in the same bank accounts as other general fund money. Therefore, officials inappropriately used reserve money for unauthorized purposes. For perspective, during 2017-18, reserve cash balances averaged 19 percent of the total general fund cash balances, and should have been increased by approximately \$52,000 of the \$282,000 in general fund interest earnings.

We analyzed the reserve balances and activity for reasonableness and adherence to statutory requirements and found that two general fund reserves totaling more than \$1.3 million are overfunded and potentially unnecessary. The Board can discontinue these reserves if it determines they are unnecessary, but must reallocate the money in conformance with applicable statutes.

Unemployment Insurance Reserve – This reserve is to reimburse the State Unemployment Insurance Fund for payments made to claimants where the municipality has elected to use the “benefit reimbursement” method. The \$510,149 balance in this reserve as of June 30, 2018 has remained unchanged over the last 10 years and could cover annual costs for 67 years, based on average annual expenditures totaling \$7,646 for the past three-years. Therefore, this reserve is significantly overfunded. Further, because District officials did not use this reserve to pay for unemployment insurance expenditures in the previous ten years, we question the need for this reserve.

Liability Reserve – This reserve may be funded in an amount not to exceed 3 percent of the annual budget, to cover liability claims. As of June 30, 2018, this reserve’s balance was \$855,340, and less than 3 percent of the budget. The Assistant Superintendent for Business told us the reserve is for unanticipated losses, but was unable to provide us with the reason for maintaining this reserve or any examples of potential liabilities that the District may incur that are not currently covered by the District’s liability insurance. Therefore, we question the need for this reserve.

Debt Service Reserve – District officials have retained a long-standing balance in its debt service reserve, which grew with interest annually to more than \$2.5 million as of June 30, 2018. District officials did not maintain records for the composition of the balance allocated to specific debt. Lacking the ability to apply these funds to the debt issuances from which they arose, the District should use the balance to pay off other outstanding debt and reduce the current burden on taxpayers.

District officials budgeted for and made annual principal and interest payments on long-term debt from the general fund. They did not use the reserve to fund annual debt payments and the balance has increased \$26,454 over the last three years. The Treasurer told us that the balance has increased from approximately \$400,000 in 1991 due to interest earnings and the accumulation of residual unused, but unidentified, debt over the years.¹⁴

Given how old the initial balance is, it is unlikely that most of the money in the reserve is related to currently outstanding debt. Therefore, much of these funds should likely have been returned to the general fund balance. Using these funds for debt service, to eliminate unaccounted for balances, would allow for general fund resources to be used to reduce the real property tax burden.

The Board budgeted to use \$190,000 from the debt service fund for debt in 2018-19 and District officials stated that they plan to use the remainder of these funds towards future payments for the current capital project once bonds are issued.

The Board Did Not Adopt a Comprehensive Reserve Plan

The Board did not adopt a comprehensive reserve plan. During our audit fieldwork, the Assistant Superintendent for Business provided us with a reserve plan (December 2018) and told us that the District did not have any reserve plans for the previous fiscal years, and that he considered it an internal business office document and did not share it with the Board for review or approval.

The current reserve plan is inadequate. For example, while the plan provided optimum funding levels for the reserves, some of these appeared arbitrary and the plan did not explain or justify why the specific levels were chosen or necessary. The selected percentages generally corresponded to the current balances in these reserves.

- The unemployment insurance reserve optimum funding level was listed as 1.42 percent of payroll with no further explanation. Based on the 2018-19 budgeted payroll expenditure listed in the plan, this equates to \$507,512. The reserve balance was \$510,149 at June 30, 2018.
- The EBALR optimum funding level was listed at 2 percent of budgeted appropriations and calculated as \$1.3 million based on the 2018-19 budget. No explanation was provided to support this optimum funding level, or the reported \$1.2 million balance as of June 30, 2018. Furthermore, the EBALR should generally be funded based on a properly-calculated accrued liability for eligible leave payments, not a percentage of the total budget. The plan

¹⁴ We also obtained electronic annual report data back to 2005 and determined that no sizeable transfers were made into the reserve since 2009, and the 2010 balance of \$2.4 million has since grown primarily from interest and premiums on obligations.

did not include the current liability amount, or the portion of the liability the Board found necessary to be maintained in the reserve.

- The plan states that the ideal tax certiorari balance is the equivalent of pending tax certiorari claims, but does not list the dollar amount of any such claims.
- The liability reserve stated the maximum balance per law (3 percent of the budget). A goal to fund this reserve at the maximum allowed balance appears unreasonable.¹⁵

In addition, the plan did not provide guidance for the intended use of each reserve or the circumstances under which reserve funds would be replenished. The purposes listed in the plan were generally summaries of reserve laws and did not describe the District's specific intentions. Furthermore, the plan stated that the debt service reserve would be funded with excess fund balance, which is not an appropriate funding source in accordance with related statutes.¹⁶

The lack of an adequate Board-approved reserve plan limits the ability of the Board and officials to effectively manage reserve funds and appropriately inform taxpayers of their plans and needs for reserves. While it is prudent to plan and provide for unforeseen circumstances, overfunding and/or not using reserves for their intended purpose results in property taxes being higher than necessary because the funds are not being used to fund operations.

What Do We Recommend?

The Board and District Officials Should:

1. Develop and adopt budgets that include more reasonable estimates for revenues and appropriations and the amount of fund balance and reserves that will be used to fund operations.
2. Develop a plan to reduce the amount of surplus fund balance in the general fund to comply with the statutory limit. Surplus funds can be used as a financing source for:
 - Funding one-time expenditures
 - Funding needed reserves
 - Paying off debt
 - Reducing District property taxes.

¹⁵ Refer to The Board Was Not Transparent When Funding Reserves.

¹⁶ LFL, Section 165.00 and GML, Section 6-I

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3. Develop a plan to continue reducing the school food service fund balance to a reasonable level, including a review of necessary meal prices.
 4. Approve a comprehensive multiyear financial plan and ensure that the plan is used and periodically updated to address the District's current financial position and needs.
 5. Review all reserves and determine if balances are necessary, reasonable and in compliance with statutory requirements. To the extent that they are not, transfers should be made to unrestricted fund balance, where allowed by law, or to other reserves established and maintained in compliance with statute.
 6. Allocate interest earned on reserved money, proportionately, to each individual reserve fund.
 7. Use reserve funds in accordance with statute and use the debt service fund's balance for debt payments as appropriate.
 8. Adopt a comprehensive reserve plan that includes justified optimum funding levels for each reserve and conditions under which reserves will be used and replenished.

Appendix A: Response From District Officials



Victor Central School District

953 High Street, Victor, New York 14564 (585) 924-3252 FAX: (585) 742-7023

Dawn A. Santiago-Marullo, Ed.D., Superintendent of Schools
Joseph Dougherty, School Business Administrator

May 13, 2019

Mr. Edward V Grant Jr. Chief Examiner
Office of the State Comptroller
16 West Main Street, Suite 522
Rochester, NY 14614

Dear Mr. Grant,

The Victor Central School District (VCSD) has received and reviewed the draft Financial Management Report of Examination 2019M-62 for the audit period of July 1, 2015- February 7, 2019. Thank you for your time and effort in conducting this review. While we are pleased that the audit found no evidence of fraud or professional misconduct, we do however respectfully disagree with the majority of the report's key findings. This letter includes both the District's response to the report as well as the corrective action plan.

The VCSD is a rare example of a school district in New York State that over the past decade has experienced significant enrollment increases. While other districts are laying off teachers, closing buildings and even engaging in talks of merging with other districts, VCSD has experienced tremendous student enrollment growth of approximately 500 students resulting in extensive staff hiring and the need for capital construction in the form of classroom additions to our school buildings. At the same time as our growth, the state of New York introduced a new Foundation Aid Formula in 2007-08 only to freeze the formula's increases to school districts a mere two years after its inception. On the District's New York State Executive Budget state aid run dated January 15, 2019, it shows that our 2018-19 Foundation Aid base was \$12,101,836, while further showing that our Full Phase In Amount (the proper amount that we should be receiving from New York State if the formula was fully phased in) would be \$20,058,759. This indicates that VCSD is underfunded nearly \$8,000,000 per year from the state of New York. If we rightfully received these funds, as the correct formula intended, these additional funds would be further utilized to effectively educate our students and perhaps even lower our local tax levy, however this is not the case. During the five year peak of our 500 student enrollment growth, our Foundation Aid increases per year during that corresponding time starting in 2009-10 were -.09%, 0%, 0%, 1.37% and .35% respectfully. Coupled with the fact that we have one of the lowest tax rates per \$1,000 compared to similar size school districts, only to have it then capped by the property tax cap, has resulted in the fact that the VCSD ranks 687th out of 688 or second lowest in the state of New York, in expenditures per student at \$14,522 when the state average

To Teach • To Learn • To Support • To Improve • To Achieve



See
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was \$25,664 (FY17 data). With that being said, we believe that our budgets are realistic, accurate and leave little room for error or the ability to pay unforeseen circumstances within our budget.

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Note 2
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The audit had seven key findings. These will be addressed in order:

1. The Board Overestimated Expenditures and Appropriated Fund Balance that Was Not Needed

Throughout this report, it is described in a non-favorable view, that the VCSD uses conservative budgeting practices. We do not believe that the VCSD budgets are overly conservative, nor were we unreasonable with estimating appropriations. To ensure fiscal integrity, a district has a duty to plan for unforeseen expenditures that may occur during the course of a school year. It is stated on page 5 of this report, "District officials indicated in their Reserve Plan that they intentionally budget conservatively." The District is unable to locate such a statement in our Reserve Plan referring to us purposely budgeting conservatively. What we did find, was a statement that reads, "The goal of the Victor Central School District is to plan conservatively to maintain strong academic programs. This conservative approach ensures that the District can maintain programs when unforeseen events arise." If this is the statement that was taken out of context, we stand by the intent of our statement.

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Note 3
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As pointed out, the most significant areas of variance included health insurance, retirement contributions and fuel. These happen to be the most fluctuating areas in a budget, making them challenging to appropriate without a margin of variance to account for such spikes or dips. If we review Figure 1- Budget Variance, and not rounding up as the table shows, VCSD overestimated revenues by .6%, underestimated revenues by -.2% then overestimated by .9% in the three years under review. That translates to 2 of the 3 years we underestimated revenues by less than 1% and even overestimated revenues in one of the years. We do not believe that you can estimate approximately \$65,000,000 in revenues over the course of a year any more accurately than this. As for appropriations, again not rounded up, the overestimated amounts were 2.9%, 2.6% and .8% for fiscal year ending in 2016, 2017 and 2018 respectively. Over the course of the three years the variance is decreasing to less than a 1% variance. This demonstrates that the district is closing this variance gap. Again we would state that it would be challenging to estimate approximately \$65,000,000 in expenditures over the course of a year more accurately than this. Caution needs to be considered in order to safeguard the district to enable flexibility to accommodate any unforeseen expenditures that were not initially appropriated for. As mentioned in our exit interview, between the time periods of March 6th through April 9th of 2019 the District incurred unplanned for, therefore unbudgeted, expenditures in excess of \$300,000, mostly in unanticipated special education costs. This was a one month time frame out of twelve months in a year. This demonstrates evidence that a District can quickly exceed any budget variance in a given year as your findings indicate. In fact, this report goes as far as making an assumption as stated on the bottom of page 5 reading, "it is likely that the District will end 2018-

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19 with an operating surplus, appropriated fund balance will be unused and fund balance will continue to increase.” The District finds this assumption to be inaccurate as a cash flow projection with only two months remaining in the school year shows us needing to utilize all of our budgeted reserves, plus \$270,000 of the appropriated \$529,000 fund balance to balance this year’s budget. Therefore the District will not end with any significant operating surplus, it will be using appropriated fund balance and our fund balance will not continue to increase, instead it will decrease. If we did not budget \$529,000 in appropriated fund balance this fiscal year, the District would have found itself in a deficit. Appropriated fund balance is budgeted with the assumption that it will be used. Although it may not have been necessary to utilize it in the recent past, the past is not always indicative of the future as we do need to utilize a large portion of this appropriated fund balance this fiscal year.

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Note 5
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At the conclusion of the 2018-19 school year, this will be the fourth out of the past seven years where the District has not had the ability to fund any reserves due to lack of year end fund balance. This is essentially deficient spending as each year we have relied on budgeted reserves as a revenue source but were unable to replenish them at year end with any available fund balance. This is an unsustainable practice. In 2013 The Office of the State Comptroller developed and launched the Fiscal Stress Monitoring System. This report assesses school districts experiencing notable levels of fiscal stress or those showing susceptibility to fiscal stress. While VCSD has not been identified as having fiscal stress, we were however assigned negative points in the scoring in our 2018 report for having an operating deficit over one of the past three fiscal years. The District is unclear as to how the Comptroller can record a finding in this audit review that the District overestimated expenditures and appropriated fund balance that was not needed, while at the same time, penalizing the district in the Fiscal Stress Monitoring system for an operating deficit in one of the past three years. Both reports were covering the same three fiscal years, 2016, 2017 and 2018.

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Note 7
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As previously stated, it is referenced numerous times throughout this report in a non-favorable fashion, that the District has “conservative budgets.” According to the Merriam-Webster’s dictionary, the word conservative is related to words such as, conventional, steady, true, appropriate, fitting, suitable, practical, sensible, careful, cautious, guarded, and safe. In contrast to this, antonyms of the word conservative include, reckless, thoughtless, neglectful, injudicious and unwise. The District does not believe that we should be budgeting in a reckless or neglectful manner.

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Note 3
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2. The Board Was Not Transparent When Funding Reserves

District leadership is very much aware of the 4% limitation of surplus fund balance allowable by RPTL and works diligently to maintain fund balance within the limits. The audit report’s recommendation of instead of transferring year end surplus into reserves, the District should include funding of reserves in the annual budget would be extremely difficult to achieve. As described in the opening few paragraph of this response, the District continues to struggle to keep up with the educational needs due to the past enrollment growth combined with the

restricted revenue streams. Each year we are challenged to meet our growing special education and social emotional needs of our students. Due to continuous revenue deficiencies we have not been able to accommodate additional requests such as teachers, psychologists, counselors, etc. The thought of inserting a line item appropriation into the budget to fund a reserve instead of adding educators to further enhance the development of our students would not be viewed favorably by our staff or community.

See
Note 10
Page 20

Furthermore, The Comptroller's office wrote on page 4 of this document as a proper guidance tool under *What is Effective Financial Management*, "Any surplus fund balance that exceeds the statutory limit should be used to pay for one-time purchase, fund needed reserves, pay down debt or reduce next year's real property tax levy." This is exactly what the District did when it could, it funded needed reserves. If this is what is recommended by the Comptroller's office and this is what the District did, we are unclear as to why it is listed as a finding.

See
Note 7
Page 19

See
Note 3
Page 19

3. General Fund Surplus Balance Exceed the Statutory Limit

The District is unclear as to why the report is recalculating our fund balance including the Debt Service reserve. As indicated, the District has a written plan to utilize the entire Debt Service reserve toward the upcoming bond from our current capital project, thus minimizing the local share tax impact.

See
Note 11
Page 20

The District believes the appropriate methodology that should be used by districts to calculate the 4% cap is that what was written in the Office of State Comptroller's memo on Generally Accepted Accounting Principles (GAAP), the Office of Comptroller clarified the requirements of fund balance commonly referred to as GASB 54. On page four of this document under Statutory Fund Balance Limitations, it states:

"School Districts- Real Property Tax Law §1318 limits the amount of unexpected surplus funds a school district can retain to no more than 4 percent of the next years budgetary appropriations. Funds properly retained under other sections of law (i.e., reserve funds established pursuant to Education Law or GML) are excluded from the 4 percent limitation."

Based on this methodology from the Comptroller's office, the Debt Service or any other reserve, should not be used in the 4 percent calculation.

As mentioned in the audit, VCSD has eight general fund reserves totaling just over \$6,000,000. This represents 8.6% of our current year budget. If we added our unappropriated fund balance to that formula we would reach 12.6% of our budget. Important to school districts is their bond rating. The stronger the bond rating, the lower the interest rate the district will yield when securing bonds for capital projects thus resulting in paying less interest when borrowing multiple millions of dollars. Moody's Investors Services has provided data that the New York school district average fund balance and reserves for an A2 rating in NYS is 19.3%, nationwide 20.7%. VCSD does not believe that our 12.6% reserves to budget ratio would be considered overfunded as our percent level is far below both the state and national levels for desirable bond ratings.

See
Note 12
Page 21

The Board does not believe that we unnecessarily overrode the tax cap when adopting the 2016-17 budget. As indicated in this report on page 5, Figure 1- Budget Variances, the 2016-17 school year happens to be the year where budget variance in our revenues was a -.2%, meaning that the amount of revenue we actually received was less than what we actually budgeted. This dilemma could have been further compounded had additional revenues not been realized through the tax levy.

See
Note 13
Page 21

4. School Food Service Fund Balance Was Excessive

Past practices for school food authorities (SFA) have been to fill out a spreadsheet known as the PLE tool, which is distributed by the US Department of Agriculture Food and Nutrition Services (USDA-FNS) assessing whether a district is charging enough for our lunch prices. The initial guidance as shown on the New York State Child Nutrition Management System, under the adult/student selling prices states as follows, "There is no maximum selling price for reimbursable lunches and breakfasts served to full price or paid students. However, if your lunch price is less than \$2.92, you must evaluate your average selling lunch price to determine the required increase for the 2018-2019 school year.

See
Note 14
Page 21

VCSD was charging \$2.10 for K-6 and \$2.30 for 7-12, for the 2017-2018 school year, well below the threshold, as stated on the New York State Child nutrition website. Also, as stated on the USDA-FNS website, SFA's still maintains the discretion to complete the steps necessary to determine their target SY2018-2019 paid lunch price. For these reasons, the choice was made to evaluate Victor Central School District's average selling lunch price to determine the increase for the 2018-2019 school year. For the upcoming 2019-2020 school year, meal prices will not be increased, as part of the initiative to reduce the fund balance to the appropriate parameters. VCSD is currently one of the lowest meal priced districts in our area, and still manages to provide variety as well as high quality, healthy and nutritious meals.

See
Note 14
Page 21

The District is unclear as to why a finding states that District officials did not implement any corrective action to reduce the surplus fund balance, however one paragraph later, the Comptroller acknowledges the fact that District officials provided the Comptroller's office with documentation of actions taken to reduce the fund balance such as installing new coolers, hiring a nutritionist, hiring an additional cleaner, increased wages, as well as being in the process of purchasing a new food service delivery vehicle.

See
Note 15
Page 21

5. The Board Did Not Adopt a Multiyear Financial Plan

The District had been developing a multiyear financial plan several months prior to the arrival of the Comptroller's review. As it is known, each budget building year has a fair amount of estimating or projecting involved, therefore predicting an exact amount of either actual

revenues or actual expenses is difficult. Extrapolating out five years further exacerbates the problem of accuracy. With such pertinent unknown variables such as the CPI rate, PILOT agreements, and the tax base growth factors affecting the tax cap calculation, with the addition of the unknown and unpredictable amount from the state Foundation Aid formula, it makes it extremely challenging to estimate revenues. With our enrollment changes and staffing changes, it makes it extremely challenging to estimate payroll expenses, retirement contributions and health insurance costs on any given year let alone five years out. While we did produce a multiyear plan, it was viewed as an internal document and not board adopted due to the amount of speculation involved and therefore inaccuracies. When the District reviewed the Multiyear Financial Planning Guide on the Comptroller's website, under the table of contents there is a section entitled, "Be Conservative." Under this section, the first sentence reads, "Although it is good to be as accurate as possible, it is best to err on the side of being conservative." The District is now unclear of the Comptroller's stance on conservative budgeting or financial planning.

See
Note 16
Page 21

See
Note 17
Page 21

See
Note 3
Page 19

While we have a multiyear financial plan, we understand that it is not a legal requirement for the Board to adopt such a plan. We will take your comments into consideration.

See
Note 16
Page 21

6. The Board Overfunded and Did Not Use Reserves

The District will take into consideration your comments on reserve balances by reanalyzing and potentially reallocating such balances in accordance with the law. As previously mentioned, the Debt Service reserve has been fully earmarked to be utilized. The Liability reserve could be used against potentially unplanned for and unbudgeted major expenses such as a costly employment separation associated with a 3020a hearing. These potential liability costs could be several hundreds of thousands of dollars each. The report stated that some of our reserves are overfunded and potentially unnecessary, however that falls in contrast to the Comptroller's Reserve Fund Management Guide that opens with the statement:

See
Note 11
Page 20

"Savings for future projects, acquisitions, and other allowable purposes is an important planning consideration for local governments and school districts. Reserve funds provide a mechanism for legally saving money to finance all or part of future infrastructure, equipment, and other requirements....The practice of planning ahead and systematically saving for capital acquisitions and other contingencies is considered prudent management."

See
Note 18
Page 22

We believe that statement is appropriate but it is in contrast to your findings that some of our reserves are overfunded and potentially unnecessary. Without a legal hard cap on the allowable amounts on reserves, this is therefore construed that Boards of Education would have the discretion to decide what they deem as an appropriate level of funding per reserve as it pertains to their individual district.

See
Note 18
Page 22

7. The Board Did Not Adopt a Comprehensive Reserve Plan

While we do have a reserve plan, we understand that it is not a legal requirement for the Board to adopt. The District does not agree with the finding that the plan did not provide guidance for the intended use of each reserve. The VCSD reserve plan kicks off each individual reserve page with a definition of the purpose of the reserve on that page. The purpose defines the intended use of the reserve. We will take your comments into consideration while we reanalyze and potentially reallocate such balances in accordance with the law.

See Note 19 Page 22

Based on the Comptroller's recommendations, VCSD will execute the following action plan:

1. The District and Board will continue to monitor the appropriate budgeting practices necessary to minimize risks and safeguard the District's resources in a valiant effort to properly educate the students of the District.
2. The District will continuously review the school food service fund balance and meal prices in accordance with the law and as outlined in our spend down plan.
3. The District and Board will review all reserve balances for reasonableness and make the necessary adjustments if necessary in accordance with law.
4. The District will allocate interest earned on reserved money, proportionality to each individual reserve fund.
5. The District and Board will consider your recommendation on adopting a comprehensive reserve and multiyear financial plan.

In closing, VCSD Board of Education will make every effort to implement budgeting practices and a financial plan that we feel is realistic and in the best interest of the District and our taxpayers. The District will take into account the Comptroller's recommendations as set forth in this report. We will continue to work with our independent financial advisors and external auditors to ensure that we continue to use taxpayer funds appropriately and prudently to provide every child with the highest quality education while remaining fiscally responsible to our taxpayers.

Sincerely,

Joseph Dougherty
Assistant Superintendent for Business

Appendix B: OSC Comments on the District's Response

Note 1

The real property tax rate is determined by the amount of the tax levy to be raised and the taxable assessed value of the properties within the District. Our report discusses the tax levy, not the tax rate. The District's tax levy increased \$5 million (13 percent) over the last three years, by 3 to 5 percent each year. The Board increased the tax levy again by \$1.9 million (4 percent) in adopting its 2018-19 budget.

Note 2

Flexibility to meet unanticipated expenditures and revenue shortfalls is provided by surplus fund balance and reserves. At the end of 2017-18, the District had more than \$2.7 million in surplus fund balance available for this purpose.

Note 3

While it may be appropriate, at times, to budget for certain items conservatively, using multiple conservative budgeting methods together results in overly conservative budgets and potentially higher than necessary tax levies.

Note 4

The District's reserve plan stated that they "plan conservatively" and use a "conservative approach." These statements indicate that they intentionally budget conservatively. Further, District officials indicated they plan to budget conservatively throughout the response.

Note 5

District officials did not provide any documentation, as requested, to support their statements at our exit conference about 2018-19 projections. We therefore did not change our report based on unsupported assertions.

Note 6

By appropriating fund balance to finance operations, the District budgeted for a planned operating deficit equal to the amount of appropriated fund balance and reserves. In the 2018-19 budget, District officials budgeted to use \$529,000 in appropriated fund balance and \$479,681 in appropriated reserves. Using the numbers provided in the District's response, the District still had \$259,000 in unused appropriated fund balance, which is well within its budgeted plan.

Note 7

District officials should not rely on year-end budgetary surpluses to fund reserves. Officials could accumulate funds for reserves by transparently budgeting to fund

them, thereby informing voters and seeking their approval. During our three-year audit period, the District did not use \$811,897 (63 percent)¹⁷ of the \$1.3 million in appropriated reserves. The appropriation of fund balance or reserves represents a plan to use them, and should result in a decrease to the corresponding fund balance or reserves.

Note 8

The Fiscal Stress Monitoring System analyzes the financial information submitted to OSC against a set of uniform financial and environmental indicators.¹⁸ This information is intended, in part, to help decision-makers and the public understand the trade-offs of their budgeting approach. Enhancements were made to the system for fiscal year data reported after 2016. The District's 2018 overall rating is 0, no designation (not in, or susceptible to, fiscal stress).¹⁹

Note 9

Our audit report does not suggest that District officials budget recklessly or in a neglectful manner. The report recommends that the Board and District officials develop and adopt budgets that include more realistic estimates for revenues and appropriations and the amounts of fund balance and reserves that will be used to fund operations.

Note 10

Although District officials expressed concerns about including a line item in the budget to fund reserves, they have funded reserves throughout our audit period. The District also wrote that it was unsustainable to not fund reserves regularly using year-end surpluses. We reiterate our belief that the Board should inform voters of its plans to increase reserves by including them in the budget submitted for voter approval.

Note 11

As stated in the report, debt service funds should be used to pay off specific outstanding debt, not held for payments on future bond issues. Because the balance of the debt service fund was unaccounted for and not related to specific outstanding debt, the District should not restrict the money in a reserve fund. The reported funds actually are an unrestricted fund balance available for operations.

¹⁷ All of the appropriated liability (\$528,205) and unemployment insurance (\$89,681) reserves and a portion of the EBALR (\$144,011, 33 percent) and workers compensation (\$50,000, 20 percent) reserves.

¹⁸ www.osc.state.ny.us/localgov/fiscalmonitoring/pdf/system-basics.pdf

¹⁹ http://www1.osc.state.ny.us/localgov/fiscalmonitoring/satfiles/2018/School/Financial/Victor_18.pdf

Note 12

Bond rating agencies analyze the risk to investors of an entity's indebtedness. Our audit assessed different objectives (i.e., whether the Board and District officials adopted realistic budgets and effectively managed fund balance and reserves).

Note 13

In 2016-17, the District overrode the tax cap by \$812,481. The District finished the year with an operating surplus of \$758,192 plus \$529,000 in unused appropriated fund balance and \$141,681 in unused appropriated reserves. Therefore, the tax cap override was unnecessary.

Note 14

District officials provided us with additional guidance from the US Department of Agriculture Food and Nutrition Services which they felt supported their need to gradually increase meal prices. However, that same guidance clearly states that school food authorities with positive or zero fund balance are exempt from required price increases. During our exit conference, District officials acknowledged this and stated that they were previously unaware of the exemption until we brought it to their attention.

Note 15

District officials had not implemented corrective action to reduce the surplus fund balance in response to any of the external auditor's previous reports. The corrective action occurred in the current 2018-19 fiscal year, and was not shared with us until after we completed audit fieldwork and met to discuss our tentative audit findings. As a result, we added the language to our report to acknowledge the District's recent efforts to begin corrective action.

Note 16

The Board should review and provide input on any multiyear plan in exercising its duty to oversee financial operations.

Note 17

Our publication specifically addresses multiyear planning, not the annual budget. As for multiyear plans, it is important to be as accurate as possible, but to use conservative projections when exact numbers are unknown.

Note 18

Our publication does not contradict the language in the report. The District may fund reserves for specific future purposes as planned by the Board. However, the Board did not review, approve or adopt a plan, and there is no other documentation of discussion or approval of the desired funding level and need for each reserve balance.

Note 19

As stated in the report, the purposes listed in the plan were generally summaries of reserve laws. The District's plan should include Board guidance on how, when, or why the District specifically intends to use each reserve.

Appendix C: 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, our audit procedures included the following:

- We interviewed District officials and employees, reviewed Board minutes, resolutions, policies, multiyear financial plan and reserve plan to gain an understanding of the budget process, financial management policies and procedures and the monitoring of fund balance and reserves.
- To assess budget reasonableness we compared budget estimates to actual results for 2015-16 through 2017-18. We also compared the 2018-19 adopted budget to determine whether any significant changes had been made to the District's budgeting practices.
- We analyzed fund balance for the general fund and calculated surplus fund balance as a percentage of the next year's appropriations to assess compliance with statute.
- We reviewed operating results and compared the results to the appropriated fund balance to determine whether appropriated fund balance was used as budgeted.
- We recalculated surplus fund balance as a percentage of the next year's appropriations after adding back unused appropriated fund balance and unused debt service funds.
- We analyzed surplus fund balance for the school food service fund to determine whether it was reasonable.
- We analyzed the debt service fund balance and activity to determine amounts that accounted for the balance and whether the fund was used to make debt payments.
- We analyzed the fund balance for the capital projects fund to determine whether the funds were for ongoing/open capital projects.
- We analyzed reserves and related expenditures to determine whether they were properly established, used and funded and whether balances were reasonable.
- We reviewed general fund cash balances for each month of 2017-18, and calculated the average reserve portion of the balances and the interest that should have been allocated to reserves.
- We reviewed summaries from the District's 2015-16 through 2018-19 tax cap filings to determine if District officials overrode the tax cap during the audit period. For the 2016-17 override, we reviewed voter results.

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.

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 D: 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/pubs/cyber-security-guide.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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