



# South Lewis Central School District Financial Condition

## Report of Examination

Period Covered:

July 1, 2014 – September 30, 2015

2016M-83



Thomas P. DiNapoli

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# State of New York Office of the State Comptroller

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## **Division of Local Government and School Accountability**

June 2016

Dear School District Officials:

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

Following is a report of our audit of the South Lewis Central School District, entitled Financial Condition. This audit was conducted pursuant to Article V, Section 1 of the State Constitution and the State Comptroller's authority as set forth in Article 3 of the New York State General Municipal Law.

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

Respectfully submitted,

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

# Introduction

## Background

The South Lewis Central School District (District) is located in the Towns of Greig, Leyden, Lyonsdale, Martinsburg, Osceola, Turin, Watson and West Turin in Lewis County. The District is governed by the Board of Education (Board), which is composed of nine elected members. The Board is responsible for the general management and control of the District's financial and educational affairs. The Superintendent of Schools is the District's chief executive officer and is responsible, along with other administrative staff, for the District's day-to-day management under the Board's direction.

The District operates three schools with approximately 1,050 students and more than 200 employees. The District's budgeted general fund appropriations for the 2015-16 fiscal year are approximately \$25.1 million, which are funded primarily with State aid and real property taxes.

## Objective

The objective of our audit was to review the District's financial condition. Our audit addressed the following related question:

- Did the Board and District officials adopt reasonable budgets and adequately manage the District's financial condition?

## Scope and Methodology

We examined the District's financial condition for the period July 1, 2014 through September 30, 2015. We extended our audit scope back to July 1, 2012 to analyze financial trends in prior years.

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

## Comments of District Officials and Corrective Action

The results of our audit and recommendations have been discussed with District officials, and their comments, which appear in Appendix A, have been considered in preparing this report. District officials generally agreed with the findings in the report. Appendix B includes our comment on issues raised in the District's response.

The Board has the responsibility to initiate corrective action. Pursuant to Section 35 of General Municipal Law, Section 2116-a (3)(c) of New York State Education Law and Section 170.12 of the Regulations of the Commissioner of Education, a written corrective action plan (CAP) that addresses the findings and recommendations in this report must be prepared and provided to our office within 90 days, with a copy forwarded to the Commissioner of Education. To

the extent practicable, implementation of the CAP must begin by the end of the next fiscal year. For more information on preparing and filing your CAP, please refer to our brochure, *Responding to an OSC Audit Report*, which you received with the draft audit report. The Board should make the CAP available for public review in the District Clerk's office.

## Financial Condition

The Board should adopt structurally balanced budgets in which recurring revenues finance recurring expenditures and reasonable levels of fund balance are maintained. The Board is responsible for estimating what the District will spend and what it will receive in revenue, estimating how much fund balance will be available at fiscal year-end and determining what the expected tax levy will be. Accurate budget estimates help ensure the tax levy is not greater than necessary. Budgets should be based on prior years' operating results, past expenditure trends and anticipated future needs.

Fund balance represents resources remaining from prior fiscal years that can be used to finance the next year's budget or set aside in reserve funds for specific purposes. The Board may retain a portion of fund balance for unexpected events and maintaining cash flow. Currently, New York State Real Property Tax Law (RPTL) limits the amount of fund balance that a school district can retain to no more than 4 percent of the ensuing fiscal year's budget. When fund balance is appropriated, the expectation is that there will be an operating deficit (budgeted appropriations exceeding budgeted revenues) financed by the appropriated fund balance. Sound budgeting practices provide that the Board should not adopt annual budgets that routinely appropriate fund balance that will not be used.

In addition, it is important for the Board to develop multiyear financial and capital plans to estimate the future costs of ongoing services and needs and financing sources over a three- to five-year period. Planning on a multiyear basis allows District officials to identify developing revenue and expenditure trends and set long-term priorities and goals. It also allows them to assess the impact and merits of alternative approaches (such as using unassigned fund balance or establishing and using reserves) to finance operations and capital needs.

Fund Balance and Budgeting – As indicated in Figure 1, the District's unassigned fund balance has exceeded the 4 percent legal limit from fiscal years 2012-13 through 2014-15. At the end of 2014-15, the District's fund balance was approximately \$2.4 million, or 9.7 percent of the ensuing year's appropriations. This amount exceeds the limit by 5.7 percentage points, or about \$1.4 million.

**Figure 1: Unassigned Fund Balance at Year-End**

	2012-13	2013-14	2014-15
Total Beginning Fund Balance <sup>a</sup>	\$3,925,360	\$3,623,128	\$4,633,787
Plus: Operating Surplus/(Deficit) <sup>b</sup>	(\$302,345)	\$1,010,598	(\$450,797)
Total Ending Fund Balance	\$3,623,015	\$4,633,726	\$4,182,990
Less: Restricted Fund Balance	\$349,586	\$349,681	\$349,721
Less: Appropriated Fund Balance for the Ensuing Year	\$1,326,000	\$1,389,409	\$1,389,409
Less: Encumbrances	\$22,223	\$34,875	\$14,447
Fund Balance at Year-End	\$1,925,206	\$2,859,761	\$2,429,413
Ensuing Year's Budget	\$24,559,383	\$24,575,418	\$25,138,993
Unassigned Fund Balance as a Percentage of Ensuing Year's Budget	7.8%	11.6%	9.7%
<sup>a</sup> Includes prior period adjustments and other minor adjustments			
<sup>b</sup> Includes interfund transfers			

The Board has appropriated more than \$1.3 million in fund balance annually to finance operations in the 2012-13 through 2014-15 fiscal years. We compared the total amounts budgeted to actual revenues and expenditures for fiscal years 2012-13 through 2014-15 and found that the budget variances were generally reasonable in 2012-13 and 2014-15. As a result, the District incurred planned operating deficits those years but used only a portion of the fund balance that the Board had appropriated to finance operations.

In 2013-14, the District's budget variances were more significant for both revenues and expenditures, which resulted in the District incurring a \$1,010,598 operating surplus and not using any of the \$1,326,000 of fund balance the Board appropriated in the budget, as indicated in Figure 2.

**Figure 2: General Fund Budget to Actual Comparison for 2013-14**

Actual Revenues	\$24,160,748
Estimated Revenues	\$23,233,383
Difference	\$927,365
Appropriations	\$24,559,383
Actual Expenditures	\$23,150,150
Difference	\$1,409,233
Planned Operating Deficit (Appropriated Fund Balance)	(\$1,326,000)
Actual Operating Surplus (Revenues Less Expenditures)	\$1,010,598

The majority of overestimated appropriations in fiscal year 2013-14 were for retirement contributions (\$230,888, overestimated by 24 percent), computer and technology equipment (\$200,860, by 42 percent) and utilities (\$167,038, by 25 percent). The Business Administrator told us that he budgets conservatively for retirement contributions. He also told us that the District intended to purchase

a block of computers and other technology equipment but decided to postpone certain purchases during the year. The Business Administrator told us that he prefers to have additional appropriations budgeted for utility costs due to the uncertainty of winter weather in the region.

The revenue variance was primarily due to the Board's underestimation of State aid in 2013-14 by \$701,438, or 5 percent. The Business Administrator told us that the District used the Executive Budget estimates of State aid to develop the budget and it did not receive the final State budget estimates until later in March 2013, after the District's budget had already been adopted. The Board did not take any action to update the budgeted State aid estimates prior to establishing the tax levy in August 2013.

Districts should calculate the amount of State aid that they are likely to receive based on their best estimates available at the time the tax warrant is issued. According to the Commissioner of Education, once the State budget is enacted into law, the amount of State aid projected for each district in the State budget becomes the best estimate and districts should use this when calculating their tax levies. Due to the budget variances for revenues and appropriations in 2013-14, the unassigned fund balance at year-end increased by almost \$1 million, or 49 percent from 2012-13 to 2013-14; however, it decreased by approximately, \$430,000, or 15 percent, in 2014-15 because the District's budget was closer to actual results.

Although the District's unassigned fund balance has exceeded the statutory limit for the past three fiscal years, the Board increased the tax levy from \$7.8 million in 2012-13 to \$8.3 million in 2015-16, an increase of about 6 percent.

Multiyear Planning – The Board has not adopted a multiyear capital or operational plan to outline the use of surplus fund balance. The Business Administrator told us he plans to develop a long-term capital plan once the District receives the results of its building condition survey, which the District expects to receive soon. Without a long-term plan, the Board may not be able to adequately assess future costs, suitable financing sources and capital needs, or adequately address the District's excessive fund balance.

By maintaining an excessive fund balance, District officials are withholding significant funds from productive use and may be levying more taxes than necessary to sustain operations. Board members told us they prefer to maintain enough fund balance to provide the District with an adequate financial cushion in case of unforeseen circumstances. However, the fund balance as of June 30, 2015 was more than twice the statutory limit.

## **Recommendations**

The Board should:

1. Ensure that the unassigned fund balance is in compliance with statutory limits.
2. Use the State aid from the enacted State budget as the best estimate of State aid available when determining how much revenue to raise through the local real property tax levy.
3. Formulate long-term multiyear operational and capital plans for the use of excess unassigned fund balance in the general fund in a manner that benefits District residents. Such uses may include, but are not limited to, reducing property taxes, paying off debt, establishing necessary reserves or financing one-time expenditures.

## **APPENDIX A**

### **RESPONSE FROM DISTRICT OFFICIALS**

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

# *South Lewis Central Schools*

**Mr. Douglas Premo, Superintendent**

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[www.southlewis.org](http://www.southlewis.org)

May 11, 2016

Ms. Rebecca Wilcox, Chief Examiner  
Office of the State Comptroller  
Syracuse Regional Office  
State Office Building, Room 409  
333 E. Washington Street  
Syracuse NY 13202-1428

Dear Ms. Wilcox:

South Lewis CSD is in receipt of the Draft Financial Condition Report of Examination for the period July 1, 2014 to September 30, 2015.

Our Board of Education and the District's administration would like to thank the local field staff of the Comptroller's Office for the professional and courteous method in which they conducted their duties while performing the audit.

As a district, we are pleased that the audit showed no findings material in nature as well as no signs of improprieties, waste, fraud, or abuse. The audit did result in recommendations dealing with budget preparation, long-range planning, reserve use, and fund balance management. In as much as the district has no strong objections to the recommendations included in the report, we find it somewhat incomplete as the report did not take uncertain volatile economic conditions and a new restrictive economic environment into account:

The ARRA Funding Cliff- The District faced uncertain economic conditions when the Federal Government ceased ARRA funding during a serious economic downturn. This caused the district to budget conservatively in preparation of the end of these funds to mitigate the possibility of mass layoffs and program decimation that many districts faced. Due to this fiscally conservative approach, South Lewis CSD was able to maintain all existing programs and maintain proper staffing levels. During these lean years, the district was also hearing the possibilities of mid-year cuts from Albany and protected itself accordingly.

Gap Elimination Adjustment (GEA) - Since New York State imposed the GEA, the cumulative loss of revenue to the South Lewis CSD has totaled over \$4.7 million. These reductions in funding resulted in the district delaying initiatives, select purchases, and eliminating positions due to attrition.

Tax Cap- The State imposed tax cap restricts the District's ability to balance budgets through the increase of tax levies. The current year levy allows the district no tax increase at all. In recent years the district has been dealing with large increases in pension fund contributions, large increases in health insurance costs, and contractual salary increases. These three items alone far exceed the 2% levy increase cap. Since the inception of the tax cap, the District has continually been under the allowable increase. Factually, the District's average tax levy increase over the past four years (since tax cap legislation) has been 1.97% while the allowable tax increase over the same period of time has averaged 4.46%. The Board of Education is very conscientious of the tax burden on the community and works hard to keep the tax increases as low as possible.

State Aid- The South Lewis BOE typically approves the spending plan for the following year at it's mid-March meeting. It is always based upon the best information available at the time, as NYS has not concluded its budget process by then. South Lewis continues to receive aid increases at a rate lower than most schools in the area. For example, while this year's overall state aid increase is over 6.4% across the state, while South Lewis is scheduled to receive an increase of only approximately 1.7%, of which about half must be spent on new Community Schools expenses and does not help the District address current operating expense increases. The State's budget process also makes it next to impossible to generate a true and accurate multi-year spending or capital plan since the District has no forecast of future year aid.

See  
Note 1  
Page 13

Other notable factors- The District made an extremely difficult decision to close an elementary school to balance the expenditure side of the budget. Not only did these savings bail the District out of a financial hole during the year of closure, the continued savings have allowed the District to maintain programs that would have otherwise been lost. The District has also kept its finger on the pulse of current employment conditions and initiatives in creating new programs and investments into equipment for the new STEM programs and technology. The District also is a leader in the area for use of technology as we attempt to level the playing field with more affluent districts in regards to opportunity for our students.

#### CORRECTIVE ACTION PLAN

The District's corrective action plans, based upon recommendations listed in the audit, are as follows:

1. *Ensure that the assigned fund balance is in compliance with statutory limits.*

Implementation Plan of Action

South Lewis CSD agrees with the recommendation of the audit to work diligently towards reducing the unappropriated fund. The District has begun that process in the 2014-15 school year as can be witnessed by the auditor's charts showing a decrease in fund balance of over \$450,000 or almost 2%. The 4% level in statute is becoming more difficult to attain and may cost taxpayers interest expenses as the level creates difficulty in meeting cash flow requirements until the districts property tax revenues begin flowing in late September. Another hindrance is the fact that Lottery Aid, the District's first true State Aid for the year, was typically received in late August but during the past few years has been delayed until the last day of September. A moderate use of fund balance, resulting in a decrease of the overall fund balance, will not result in the financial hole that would result if a District reduced fund balance all at once.

Date of Implementation

March 2015

2. *Use the State Aid from the Enacted State budget as the best estimate of State Aid available when determining how much revenue to raise through the local real property tax levy.*

Implementation Plan of Action

As mentioned earlier, the South Lewis BOE adopts the budget at its mid-March meeting. The final State enacted budget is often available at that time. The BOE purposely approves the budget at that time to give the administration plenty of time to present and explain the budget to taxpayers and organizations. The BOE is proud of the fact the budget is transparent and presented at each and every opportunity to educate our taxpayers on how their dollars are being invested. The BOE and administration will continue to reach out to our elected representatives to estimate where the budget may end up to the best of their ability.

Date of Implementation

March 2016

3. *Formulate long-term multiyear operational and capital plans for the use of excess unassigned fund balance in the general fund in a manner than benefits District residents.*

Implementation Plan of Action

The District is currently developing a capital building plan with the assistance of an architectural firm. This plan may include use of fund balance after discussion with the BOE. The District often discusses multi-year operational plans with the BOE; however, it is next to impossible to do without forecast of revenues matching the spending plan. As previously stated, the District receives revenue projections for only one year at a time. This makes a multiyear operational spending plan merely a best guess situation, which results in a working document that isn't based upon facts. Prior to 6/30/2016 the district will establish an EBLAR reserve to properly fund for compensated absences.

See  
Note 1  
Page 13

Date of Implementation

May 2016

In conclusion, South Lewis CSD appreciates the work of the Comptroller's Office and the opportunity to respond to the written report. We are constantly looking for ways to strengthen our District.

Sincerely,

Barry R. Worczak, President  
South Lewis Board of Education

## APPENDIX B

### OSC COMMENT ON THE DISTRICT'S RESPONSE

#### Note 1

A multiyear financial plan illustrates what could happen to a school district's ability to pay for and provide services, given a set of policy and economic assumptions. These projections help the Board assess expenditure commitments, revenue trends, financial risks and the affordability of new services and capital investments. We realize that State aid revenues may be difficult to predict because the timing and relative health of the State budget affect most of its aid categories. Therefore, it is generally accepted practice to hold these revenues constant, unless there is a reasonable possibility of a decrease or the solid expectation of a specific increase.

Most long-range financial plans are based on three or four years of historical data, including the most recent year for which data are available. In the case of major revenues, such as aid, a longer trend line is often useful to get a sense of patterns during different economic conditions. Multiyear plans must be tracked and updated regularly to accurately guide policy decisions. Assistance on multiyear financial planning can be found on the OSC website at <http://www.osc.state.ny.us/localgov/myfp/index.htm>.

## APPENDIX C

### AUDIT METHODOLOGY AND STANDARDS

Our overall goal was to evaluate the District's financial condition for the period July 1, 2014 through September 30, 2015. We extended our audit scope back to July 1, 2012 to analyze financial trends in prior years. To achieve our audit objective and obtain valid evidence, we performed the following procedures:

- We interviewed District officials to gain an understanding of their budget development process and budget monitoring procedures and to determine whether the District adopted long-term financial and capital plans.
- We reviewed the results of operations and analyzed changes in fund balance for the general fund from July 1, 2012 through June 30, 2015.
- We compared the adopted budgets to operating results from July 1, 2012 through September 30, 2015 to determine if the budget assumptions for revenues and expenditures were reasonable. We interviewed District officials to identify reasons for significant budget variances.
- We reviewed the appropriation of fund balance from July 1, 2012 through June 30, 2015.
- We reviewed adopted budgets to identify the trend in real property tax levies from fiscal years 2012-13 through 2015-16.

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

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