



Albion Central School District Budgeting

Report of Examination

Period Covered:

July 1, 2010 – December 16, 2015

2016M-80



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

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 Albion Central School District, entitled Budgeting. 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 Albion Central School District (District) is located in the Towns of Albion, Barre, Carlton, Gaines, Kendall, Murray and Ridgeway in Orleans County and the Town of Elba in Genesee 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 (Superintendent) is the chief executive officer of the District and is responsible, along with other administrative staff, for the day-to-day management of the District under the Board's direction. The Assistant Superintendent for Business is responsible for the District's accounting records.

There are three schools in operation within the District, with approximately 1,880 students. The District's budgeted appropriations for the 2015-16 fiscal year were \$33 million, which were funded primarily with State aid, real property taxes and grants.

Objective

The objective of our audit was to evaluate the District's budgeting practices. Our audit addressed the following related question:

- Did the Board adopt realistic budgets to ensure that the real property tax levy is not greater than necessary to fund operations?

Scope and Methodology

We examined the District's budgeting practices for the period July 1, 2010 through December 16, 2015.

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

Comments of District Officials and Corrective Action

The results of our audit and recommendations have been discussed with District officials, and their comments, which appear in Appendix A, have been considered in preparing this report. District officials generally agreed with our findings and recommendations and indicated they planned to initiate corrective action.

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.

Budgeting

The annual operating budget represents the District's financial plan for a fiscal year and is an important tool for managing District finances. A good budget begins with sound estimates and well-supported budgetary assumptions. The Board, Superintendent and Assistant Superintendent for Business are responsible for accurate and effective budgeting. While preparing the budget, District officials should accurately assess spending levels and financial resources to ensure they will be able to properly fund planned services.

A district can legally set aside and reserve portions of fund balance to finance future costs for a variety of specified objects or purposes. The Board should balance the intent for accumulating money for future identified needs with the obligation to ensure that residents are not overburdened.

District officials did not prepare accurate budgets for the 2010-11 through the 2015-16 fiscal years. While the District appropriated fund balance to help finance operations, it was not needed because the District's budgeting practices regularly produced significant operating surpluses. District officials plan to use \$13 million of the accumulated surplus to finance a capital project, rather than issue debt that aligns with the State's building aid payment schedule. District officials have maintained real property taxes at a consistent level over the past five years. However, for perspective, the District's tax levy could have been \$2 million (24 percent) lower for each of the last five completed fiscal years, and the District would have continued to realize an operating surplus in each fiscal year.

In addition, the District's retirement contribution reserve and unemployment insurance reserve were overfunded. The balance of the retirement contribution reserve as of June 30, 2015 was \$7.8 million, which was more than 18 times the District's annual average contribution of approximately \$422,000. The balance of the unemployment insurance reserve as of June 30, 2015 was \$244,000, which was 22 times the District's average annual unemployment costs of \$11,000.

Budget Estimates

The Board and District management are responsible for accurately estimating revenues and appropriations in the District's annual budget. Accurate budget estimates help ensure that the real property tax levy is not greater than necessary.

We compared the District's adopted budgets with actual operating results for 2010-11 through 2014-15 and found that the District overestimated appropriations by \$22.4 million (13.4 percent).

Figure 1: Overestimated Appropriations

	Appropriations	Encumbrances	Expenditures ^a	Difference	Percentage
2010-11	\$32,254,544	\$871,084	\$28,896,860	\$4,228,768	12.8%
2011-12	\$32,662,922	\$727,054	\$28,558,568	\$4,831,408	14.5%
2012-13	\$33,146,250	\$538,687	\$28,501,997	\$5,182,940	15.4%
2013-14	\$33,349,049	\$827,771	\$29,137,029	\$5,039,791	14.8%
2014-15	\$33,551,051	\$359,504	\$30,729,101	\$3,181,454	9.4%
Totals	\$164,963,816	\$3,324,100	\$145,823,555	\$22,464,361	13.4%

^a Excludes transfers to the capital projects fund. These transfers were not included in the adopted operating budget.

Appropriations that were consistently overestimated over a three-year period (2012-13 through 2014-15) included employee benefits (\$4.4 million, 19 percent budget variance), special education tuition (\$1 million, 32 percent), contract transportation (\$790,000, 19 percent), transportation supplies and materials (\$534,000, 43 percent) and all Board of Cooperative Educational Services (\$486,000, 16 percent).

The District also underestimated revenues by \$5.1 million (3.3 percent) for the 2010-11 through 2014-15 fiscal years.

Figure 2: Underestimated Revenues

	Estimated Revenues ^a	Actual Revenues	Difference	Percentage
2010-11	\$30,989,339	\$32,520,816	\$1,531,477	4.9%
2011-12	\$30,670,187	\$31,370,893	\$700,706	2.3%
2012-13	\$31,205,184	\$31,864,884	\$659,700	2.1%
2013-14	\$31,553,965	\$32,549,067	\$995,102	3.2%
2014-15	\$32,088,216	\$33,327,155	\$1,238,939	3.9%
Totals	\$156,506,891	\$161,632,815	\$5,125,924	3.3%

^a Excludes a budgeted revenue identified as interfund transfers. The Assistant Superintendent for Business indicated that this item represented the appropriation of a reserve fund, rather than a planned operating transfer.

Actual revenues were greater than budgeted estimates for the 2012-13 through 2014-15 fiscal years because the District underestimated State aid. The District deducted planned bus purchase costs from the transportation aid estimate and reduced the estimated revenue from building aid to the amount of the scheduled debt service payments. Therefore, the budgeted revenue estimates for transportation aid and building aid were routinely underestimated. The Board continued this budgeting practice in the 2015-16 budget.

Because the District has underestimated revenues and overestimated expenditures in its budgets, it has levied more real property taxes than necessary to fund operations.

Fund Balance

During the budget process, the Board must estimate the amount of unrestricted fund balance that can be applied as a financing source in the adopted budget. New York State Real Property Tax Law currently limits unrestricted fund balance to no more than 4 percent of the ensuing fiscal year's budget. Any unrestricted fund balance over this percentage should be used to reduce the upcoming fiscal year's tax levy.

Due to the District's practice of overestimating appropriations and underestimating revenues, it has experienced a cumulative operating surplus of approximately \$15.8 million for the five-year period (Figure 3). After allocating more than \$13 million of fund balance to finance a planned capital project and appropriating \$680,000 of fund balance as a financing source in the 2015-16 budget, the District's unrestricted fund balance was \$2.8 million as of June 30, 2015, which exceeded the statutory limit by 4.5 percentage points.

Figure 3: Unrestricted Fund Balance at Year-End					
	2010-11	2011-12	2012-13	2013-14	2014-15
Beginning Fund Balance	\$16,109,388	\$19,284,228	\$21,731,660	\$24,742,688	\$27,789,960
Add: Operating Surplus	\$3,623,956	\$2,812,325	\$3,362,887	\$3,412,038	\$2,598,054
Less: Transfers to the Capital Projects Fund	(\$449,116)	(\$364,893)	(\$351,859)	(\$364,766)	(\$13,813,717)
Ending Fund Balance	\$19,284,228	\$21,731,660	\$24,742,688	\$27,789,960	\$16,574,297
Less: Restricted Fund Balance ^a	\$11,848,309	\$13,216,840	\$17,813,959	\$17,565,056	\$12,566,042
Less: Encumbrances	\$727,054	\$538,687	\$827,771	\$359,504	\$517,953
Less: Appropriated Fund Balance for the Ensuing Year	\$1,575,850	\$1,514,512	\$1,363,563	\$1,030,404	\$680,209
Unrestricted Fund Balance at Year-End	\$5,133,015	\$6,461,621	\$4,737,395	\$8,834,996	\$2,810,093
Ensuing Year's Budgeted Appropriations	\$32,662,922	\$33,146,250	\$33,349,049	\$33,551,051	\$33,240,940
Unrestricted Fund Balance as a Percentage of the Ensuing Year's Budget	15.7%	19.5%	14.2%	26.3%	8.5%

^a Includes non-spendable and reserved fund balance

The District appropriated an average of \$1.2 million in fund balance as a financing source in the annual budget from 2010-11 through 2014-15. This appropriation of fund balance reduced the level of the District's reported unrestricted fund balance at the end of each fiscal year. However, the District did not need to use any of the appropriated fund balance to finance operations because the District realized operating surpluses during the same period. When unused appropriated fund balance was added back, the recalculated unrestricted fund balance exceeded the statutory limit by 6.5 to 25.4 percentage points.

Figure 4: Unused Fund Balance					
	2010-11	2011-12	2012-13	2013-14	2014-15
Unrestricted Fund Balance at Year-End	\$5,133,015	\$6,461,621	\$4,737,395	\$8,834,996	\$2,810,093
Add: Appropriated Fund Balance Not Used to Fund Ensuing Year's Budget	\$1,575,850	\$1,514,512	\$1,363,563	\$1,030,404	\$680,209
Recalculated Unrestricted Fund Balance	\$6,708,865	\$7,976,133	\$6,100,958	\$9,865,400	\$3,490,302
Recalculated Unrestricted Fund Balance as a Percentage of Ensuing Year's Budget	20.5%	24.1%	18.3%	29.4%	10.5%

While the District has realized operating surpluses and retained excessive fund balance, it also consistently levied real property taxes averaging \$8 million during each of the five years.¹ Furthermore, the District's practice of consistently 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.

We project that the \$680,000 of unrestricted fund balance appropriated in the 2015-16 budget will not be needed to help finance 2015-16 operations. Therefore, we expect unrestricted fund balance will increase once again and continue to exceed the statutory limit.

Reserves

Money set aside in reserves must be used only in compliance with statutory provisions that determine how reserves are established, funded, expended and discontinued. Generally, school districts should maintain reserve balances that are reasonable. Funding reserves at greater than reasonable levels contribute to real property tax levies that are higher than necessary because the excessive reserve balances are not being used to fund operations. The District's reserve fund policy indicates that District officials should determine optimal funding levels for reserves, periodically assess the reasonableness of the amounts accumulated and, as conditions warrant, reduce or liquidate the balances.

As of June 30, 2015, the District reported four reserves in the general fund totaling \$12.5 million. We analyzed the reserves for reasonableness and found the District properly maintained a capital reserve (\$4.4 million) and a tax certiorari reserve (\$127,000). However, we did not find any evidence to suggest that the Board or District officials followed the District's reserve fund policy with the remaining two reserves (totaling \$8 million), which were overfunded. In addition, the District should use anticipated building aid revenue on an upcoming capital project to help reduce the annual tax levy because the District will not have any outstanding debt on the project.

Retirement Contribution Reserve – New York State General Municipal Law (GML) authorizes the Board to establish this type of reserve to pay contributions for employees covered by the New York State and Local Retirement System. The balance of this reserve as of June 30, 2015 was \$7.8 million, which is more than 18 times the District's average contribution of approximately \$422,000 over four years.² Consequently, we question the reasonableness of the amount in this reserve.

¹ 2010-11 through 2014-15

² These expenditures were budgeted for and paid out of the general fund as routine operating costs.

Unemployment Insurance Reserve – GML authorizes the Board to establish this type of reserve to reimburse the New York State Unemployment Insurance Fund for payments made to claimants on the District’s behalf. The balance of this reserve as of June 30, 2015 was \$244,000. The District incurred average annual unemployment costs of \$11,000 over the last four fiscal years. If unemployment costs continue to average approximately \$11,000 per year, the reserve would last for 22 years. Therefore, we question the reasonableness of the amount in this reserve.

By maintaining excessive reserves, combined with ongoing budgeting practices that generated operating surpluses, the Board and District officials have levied higher taxes than necessary.

Capital Reserve – School districts normally finance a capital construction project by borrowing funds and receiving State building aid on approved project costs, including an assumed debt interest expense on project costs. State building aid is available for the construction of new school buildings, additions and alterations or modernization of district-owned buildings. Building aid is based on an assumed amortization schedule using a statewide average interest rate. Districts pay the remainder of the capital project costs after building aid is taken into consideration (the “local share”).

District officials plan to use \$13 million of accumulated surplus funds and up to \$1.3 million from a capital reserve to finance a capital project approved by voters in May 2015 to improve existing facilities. The project’s maximum authorized amount is \$14.3 million. In 2014-15, the District transferred the funds from the general to the capital projects fund. The project has been approved by the New York State Education Department and is expected to begin in the summer of 2016 and be completed in 2018. The District does not plan to issue debt to finance this project.

A more transparent way of financing a capital project would be to seek voter approval to establish capital reserves, rather than tax District residents, accumulate surplus funds in violation of Real Property Tax Law and then seek voter approval to spend the money. The District’s building aid ratio is high (81.5 percent). Therefore, most of the cost for the capital project will be borne by the State.³ However, instead of paying just the local share and financing the rest, by using surplus funds the District is prepaying for a cost that will be paid over time in State aid. The District should use the building aid revenue to help reduce the annual tax levy because the District will not have any outstanding debt on the project.

³ The State will pay the District building aid over 15 years.

Recommendations

The Board and District officials should:

1. Develop realistic estimates of revenues, appropriations and the use of fund balance in the annual budget.
2. Ensure that the amount of unrestricted fund balance is in compliance with the statutory limit and develop a plan to use excess funds in a manner that benefits residents. Such uses could include but are not limited to:
 - Funding one-time expenditures;
 - Funding needed reserves; and
 - Reducing District property taxes.
3. Comply with the District's reserve fund policy.
4. Use the excess amounts in reserve funds, in accordance with applicable statutory provisions, in a manner that benefits residents.
5. Use the anticipated building aid from the upcoming capital project to reduce the tax levy.

APPENDIX A

RESPONSE FROM DISTRICT OFFICIALS

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



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May 23, 2016

Jeffery D. Mazula, Chief Examiner
295 Main Street – Suite 1032
Buffalo, New York 14203-2510

Dear Mr. Mazula,

The Albion Central School District is in receipt of the draft audit report prepared by the Office of the State Comptroller. The information presented in the audit demonstrates the intent of the process by providing us with an opportunity to reflect on our operations and governance procedures. At all times during the process [REDACTED] auditor assigned to our District, was thorough, helpful, professional and courteous. We appreciated the opportunity to work with an individual of her caliber.

As indicated at the exit conference attended by Mrs. Brown, President of the Board of Education, Mr. Bonnewell, Superintendent of Schools, and Shawn Liddle, School Business Official our collective goal over the years has been to minimize the impact of inconsistency of funding levels from the State Education Department while trying to maintain an effective instructional program insulated from swings in state aid revenues. Due to the fact that approximately 80% of the District's operating funds come directly from New York State, we have adopted an extremely conservative philosophy in budget preparation and execution. Application of this philosophy has allowed the District to reduce or freeze the local tax levy 9 of the past 10 years while achieving the lowest true value school tax rate in Orleans County and its three contiguous counties of Monroe, Genesee and Niagara. Available monies have been applied to reduce the district's current debt and to avoid issuance of debt for on-going projects, saving an estimated \$4.6 million dollars in interest payments. The Board of Education is committed to improving its operations and looks forward to comparable successes over the next decade.

The audit report is accepted in the spirit in which it was prepared; that is, to identify strategies to reduce costs and to strengthen controls in order to safeguard assets, principles espoused by the district. Implementing a Corrective Action Plan, as per the requirement, is consistent with one of our District values, Committed to Continuous Improvement. On behalf of our District, I extend our appreciation to you for your insight and recommendations.

Sincerely,

Michael S. Bonnewell
Superintendent

Achievement, Character, and Success for Life ... ACS

APPENDIX B

AUDIT METHODOLOGY AND STANDARDS

To achieve our audit objective and obtain valid audit evidence, we performed the following audit procedures:

- We interviewed District officials to obtain an understanding of the District's financial condition, budgeting practices and use of reserve funds.
- We compared budgets with actual operating results for the 2010-11 through 2014-15 fiscal years and analyzed items with significant variances.
- We reviewed Board minutes and accounting records to determine whether reserves reported as of June 30, 2015 were properly established and reasonably funded.
- We analyzed unrestricted fund balance levels from the 2010-11 through 2014-15 fiscal years.
- We reviewed interim 2015-16 operating results and estimated whether appropriated fund balance would be needed to finance operations.
- We interviewed District officials about the funding of the planned building capital project.

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

APPENDIX C

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