



Central Islip Union Free School District

Financial Management

Report of Examination

Period Covered:

July 1, 2012 — June 30, 2013

2013M-380



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

March 2014

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 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 Central Islip Union Free School District, entitled Financial Management. This audit was conducted pursuant to the State Comptroller's authority as set forth in Article V, Section 1 of the State Constitution, and Article 3 of the 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*



State of New York Office of the State Comptroller

EXECUTIVE SUMMARY

The Central Islip Union Free School District (District) is located in the Town of Islip, in Suffolk County. The District is governed by the Board of Education (Board) which comprises seven 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 day-to-day management of the District under the Board's direction. The Assistant Superintendent for Business plays a key role in the budget development process and the Business Office's daily administration.

Scope and Objective

The objective of our audit was to evaluate the District's financial operations, including factors which contributed to accumulating and using unexpended surplus funds,¹ for the period of July 1, 2012 through June 30, 2013. We expanded our scope back to July 1, 2008 to evaluate the District's financial condition and to provide additional information for perspective and background. Our audit addressed the following related question:

- Did the Board provide adequate oversight and management of the District's budgets and financial condition?

Audit Results

District officials underestimated revenues and overestimated expenditures in the Board-adopted budgets for fiscal years 2008-09 through 2012-13, resulting in combined operating surpluses totaling more than \$25 million. Although the Board appropriated unexpended surplus funds each year (exceeding a combined \$13.2 million over the five-year period) to help finance the next years' operations, District officials actually used less than \$5.3 million to fund District operations. Additionally, the District's accumulated unexpended surplus funds exceeded the amount allowed by statute in each of the past three years.² While the District's unexpended surplus exceeded the statutory limit over these years,

¹ The Governmental Accounting Standards Board (GASB) issued Statement 54, which replaces the fund balance classifications of reserved and unreserved with new classifications: nonspendable, restricted and unrestricted (comprising committed, assigned and unassigned funds). The requirements of Statement 54 are effective for fiscal years ending June 30, 2011 and beyond. To ease comparability between fiscal years ending before and after the implementation of Statement 54, we will use the term "unexpended surplus funds" to refer to that portion of fund balance that was classified as unreserved, unappropriated (prior to Statement 54), and is now classified as unrestricted, minus appropriated fund balance, amounts reserved for insurance recovery and tax reduction, and encumbrances included in committed and assigned fund balance (post Statement 54).

² Real Property Tax Law limits the amount of unexpended surplus funds that can be legally retained by District officials to no more than 4 percent of the next fiscal year's budget. The District's unexpended surplus funds as a percentage of the next year's budget appropriations totaled 10 percent in 2010-11, 18 percent in 2011-12 and 5 percent in 2012-13.

District officials continued to increase the real property tax levy by more than \$6.6 million, a 9 percent increase.

Comments of District Officials

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. Except as specified in Appendix A, District officials generally agreed with our recommendations and indicated they planned to take corrective action. Appendix B includes our comments on the issues raised in the District's response letter.

Introduction

Background

The Central Islip Union Free School District (District) is located in the Town of Islip, in Suffolk County. The District is governed by the Board of Education (Board) which comprises seven 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 Assistant Superintendent of Business plays a key role in the budget development process and the Business Office's daily administration.

The District operates eight schools, with approximately 6,500 students and 845 employees. The District's expenditures for the 2012-13 fiscal year were \$168.5 million, funded primarily with State aid, real property taxes and grants.

Objective

The objective of our audit was to evaluate the District's financial operations, including factors which contributed to accumulating and using unexpended surplus funds.³ Our audit addressed the following related question:

- Did the Board provide adequate oversight and management of the District's budgets and financial condition?

Scope and Methodology

We evaluated the Board's management of the District's financial condition and budgeting practices for the period of July 1, 2012 through June 30, 2013. We extended our scope back to July 1, 2008 to evaluate the District's financial condition and to provide additional information for perspective and background.

³ The Governmental Accounting Standards Board (GASB) issued Statement 54, which replaces the fund balance classifications of reserved and unreserved with new classifications: nonspendable, restricted and unrestricted (comprising committed, assigned and unassigned funds). The requirements of Statement 54 are effective for fiscal years ending June 30, 2011 and beyond. To ease comparability between fiscal years ending before and after the implementation of Statement 54, we will use the term "unexpended surplus funds" to refer to that portion of fund balance that was classified as unreserved, unappropriated (prior to Statement 54), and is now classified as unrestricted, minus appropriated fund balance, amounts reserved for insurance recovery and tax reduction, and encumbrances included in committed and assigned fund balance (post Statement 54).

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 is 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. Except as specified in Appendix A, District officials generally agreed with our recommendations and indicated they planned to take corrective action. Appendix B includes our comments on the issues raised in the District's response letter.

The Board has the responsibility to initiate corrective action. Pursuant to Section 35 of the General Municipal Law, Section 2116-a (3) (c) of the Education Law and Section 170.12 of the Regulations of the Commissioner of Education, a written corrective action plan (CAP) that addresses the findings and recommendations in this report must be prepared and provided to our office within 90 days, with a copy forwarded to the Commissioner of Education. To the extent practicable, implementation of the CAP must begin by the end of the next fiscal year. For more information on preparing and filing your CAP, please refer to our brochure, *Responding to an OSC Audit Report*, which you received with the draft audit report. The Board should make the CAP available for public review in the District clerk's office.

Financial Management

The Board is responsible for making sound financial decisions that are in the best interests of the District, the students it serves and the taxpayers who fund the District's programs and operations. Prudent unexpended surplus fund management along with sound budgeting practices based on accurate estimates can help ensure that sufficient funding will be available to sustain operations, address unexpected occurrences and satisfy long-term obligations or future expenditures. Accurate budget estimates also help ensure that the real property tax levy is not greater than necessary.

District officials underestimated revenues and overestimated expenditures in the Board-adopted budgets for fiscal years 2008-09 through 2012-13, resulting in combined operating surpluses totaling more than \$25 million. Although the Board appropriated unexpended surplus funds each year (exceeding a combined \$13.2 million over the five-year period) to help finance the next years' operations, the District actually used less than \$5.3 million to fund operations. The District accumulated unexpended surplus funds that exceeded the statutory limit⁴ over the last three years while, at the same time, increasing the real property tax levy by more than \$6.6 million, a 9 percent increase.

Budgeting Practices

The Board is responsible for preparing and presenting the District budget to the public for voter approval. In preparing the budget, the Board is responsible for estimating revenues and expenditures and for determining how much unexpended surplus funds will be available at fiscal year-end and the expected real property tax levy. Accurate estimates help ensure that the real property taxes levied are not greater than necessary.

Revenue and expenditure estimates should be developed based upon prior years' operating results, past expenditure trends, anticipated future needs and available information related to projected changes in significant revenues or expenditures. Unrealistic budget estimates can mislead District voters and taxpayers and significantly impact the District's year-end unexpended surplus funds and financial condition.

District officials presented, and the Board approved, budgets

⁴ Real Property Tax Law limits the amount of unexpended surplus funds that can legally be retained by District officials to no more than 4 percent of the next fiscal year's budget. The District's unexpended surplus funds as a percentage of the next year's budgeted appropriations totaled 10 percent in 2010-11, 18 percent in 2011-12 and 5 percent in 2012-13.

which significantly underestimated revenues and overestimated appropriations in three of the last five years. We compared the District’s general fund budgeted revenues and expenditures with actual results of operations for our scope period and found that District officials underestimated revenues by as much as \$9.3 million and overestimated expenditures by as much as \$16.2 million.

For example, for fiscal years 2008-09 through 2012-13, District officials underestimated other real property tax items (e.g., school tax assessment relief) by as much as \$11.1 million, State aid by as much as \$7.7 million, miscellaneous revenues by as much as \$1.9 million, sale of property and compensation for loss by more than \$3 million and use of money and property by as much as approximately \$821,000. Also, over three years, (fiscal years 2010-11 through 2012-13), the District overestimated programs for children with handicapped conditions by as much as \$7.4 million, regular school teaching expenses by as much as \$5 million, pupil transportation by as much as \$1.7 million and pupil services by as much as \$1.6 million.

	2008-09	2009-10	2010-11	2011-12	2012-13
Estimated Revenues	\$156,833,453	\$161,344,813	\$165,882,626	\$165,085,065	\$173,516,302
Actual Revenues	\$166,151,355	\$161,223,146	\$162,998,317	\$172,616,121	\$173,802,990
Variance	\$9,317,902	(\$121,667)	(\$2,884,309)	\$7,531,056	\$286,688
Appropriations	\$157,842,890	\$165,613,689	\$171,471,355	\$167,127,721	\$176,412,706
Actual Expenditures	\$161,298,515	\$166,464,909	\$155,272,045	\$155,080,290	\$168,507,985
Variance	(\$3,455,625)	(\$851,220)	\$16,199,310	\$12,047,431	\$7,904,721
Total Variance	\$5,862,277	(\$972,887)	\$13,315,001	\$19,578,487	\$8,191,409

Unexpended Surplus Funds

Estimating unexpended surplus funds is integral to the District’s budget process because it represents resources remaining from prior fiscal years that can be used to benefit District taxpayers. Any unexpended surplus funds that exceed the statutory limit should be used to lower property taxes, transferred to reserve funds, be used to pay one-time expenses or used to pay down debt. District officials should not appropriate unexpended surplus funds that will not be used to fund operations simply to circumvent the statutory limit.

District officials appropriated a combined \$13.2 million in unexpended surplus funds to fund subsequent years’ operations which should have resulted in planned operating deficits each year. However, because of large variances between budgeted and actual revenues and expenditures, the District realized large operating surpluses (See Table 2). As a result, only about \$5.2 million of appropriated unexpended surplus funds was actually used to finance District operations.

Fiscal Year	Revenues	Expenditures	Operating Surplus/(Deficit)	Appropriated, Unexpended Surplus	Appropriated, Unexpended Surplus Used
2008-09	\$166,151,355	\$161,298,515	\$4,852,840	\$1,000,000	\$0
2009-10	\$161,223,146	\$166,464,909	(\$5,241,763)	\$4,000,000	\$5,241,763
2010-11	\$162,998,317	\$155,272,045	\$7,726,272	\$3,485,000	\$0
2011-12	\$172,616,121	\$155,080,290	\$17,535,831	\$2,000,000	\$0
2012-13	\$173,802,990	\$168,507,985	\$5,295,005	\$2,750,000	\$0
Totals	\$836,791,929	\$806,623,744	\$30,168,185	\$13,235,000	\$5,241,763

The District's unexpended surplus funds exceeded the statutorily allowed limit in each of the last three years because the Board consistently underestimated revenues, overestimated expenditures and/or appropriated significant unexpended surplus funds that were not used to fund operations. Unexpended surplus funds as a percentage of the next year's budget in the 2011-12 fiscal year was 18 percent, the highest level over the five-year period and more than four times the statutory limit. Although District officials significantly reduced unexpended surplus funds in 2012-13 by transferring surplus funds to existing and newly created reserve funds, they still did not meet the statutory requirement.

The District's 2010-11 and 2011-12 fiscal year independent audit reports advised the Board that the District exceeded the unexpended surplus funds' statutory limit each year. However, the Board did not take action until March 2013, when it authorized establishing a retirement contribution reserve of \$15 million. In May 2013, the Board authorized increasing its existing employee benefit accrued liability reserve by \$5 million and received voter approval to establish a capital reserve of \$7.5 million. Even after transferring \$27.5 million to these reserves, the District still exceeded the statutory limit by \$2.2 million as of June 30, 2013.

	2008-09	2009-10	2010-11	2011-12	2012-13
Unexpended Surplus Funds	\$6,600,504	\$2,854,492	\$15,934,228	\$32,319,535	\$9,768,064
Next Year's Budget Appropriations	\$165,613,689	\$171,471,355	\$167,127,721	\$176,412,706	\$187,955,865
Unexpended Surplus Funds as a Percentage of Next Year's Budget Appropriations ^a	4%	2%	10%	18%	5%

^a The unexpended surplus fund balance percentages were calculated by dividing the end of the year's unexpended surplus funds less encumbrances by the next year's adopted budgeted appropriations.

District officials stated that the surplus funds were accumulated to fund a contingent liability of more than \$13.6 million owed to the State Education Department (SED) for rescinded building aid.⁵ However, the SED claim is no different than any other claim against the District. Therefore, setting money aside to pay this claim, should it come due, does not restrict these funds because the District could decide to use these resources for other purposes or issue debt if and when the claim comes due.

Despite there being no statutory exceptions to the limit on unexpended surplus funds, District officials hoped that funds for this contingent liability could be placed in a reserve and excluded when calculating the statutory limit. However, there is no statutory authority to establish a reserve for this liability. District officials could assign a portion of unexpended surplus funds to fund this liability, but assigned amounts would still be included in the fund balance limit calculation.

Additionally, District officials accumulated more unexpended surplus funds than were required to fund this liability. For example, after officials learned of this liability in February 2010, the entire amount needed was accumulated in unexpended surplus funds by the end of the 2010-11 fiscal year, due to the operating surplus incurred that year. Yet officials continued to accumulate additional unexpended surplus funds in subsequent fiscal years. In addition, SED approved a repayment plan which allowed District officials to repay the liability in three annual installments of \$4.5 million,⁶ further reducing the liability officials needed to fund each year.

While the District's unexpended surplus funds exceeded the statutory limit over the last three years, District officials continued to increase the real property tax levy. For example, in the 2010-11 fiscal year the tax levy totaled approximately \$70.5 million and in the 2012-13 fiscal year the levy was more than \$77.1 million. Had District officials used more realistic budget estimates, they could have avoided accumulating excess unexpended surplus funds and reduced the real property tax levy. Instead, the levy increased by more than \$6.6 million, a 9 percent increase. As a result, District officials levied and collected more taxes than necessary to fund District operations.

⁵ SED building aid received during the 2003-04 through 2008-09 fiscal years was rescinded for failure to file reports in a timely manner.

⁶ As a result of remedial legislation passed in 2012, relief was granted to school districts that failed to file their building project costs reports in a timely manner. Repayment installments were due in June 2011, June 2012 and June 2013 which reduced the District's liability to \$5.46 million. The District subsequently filed an appeal to its lawsuit to have the liability reduced to zero, which had been set aside due to the 2012 legislation.

Recommendations

1. The Board should develop and adopt budgets that include realistic estimates for revenues and expenditures based on all information available at the time the budget is developed.
2. The Board should discontinue the practice of adopting budgets that result in appropriating unexpended surplus funds that will not be used to fund the next year's operations.
3. The Board should ensure that the amount of the District's unexpended surplus funds complies with the statutory limit.
4. District officials should consider using unexpended surplus funds in a manner that benefits District taxpayers. Such uses could include, but are not limited to:
 - Reducing property taxes,
 - Increasing necessary reserves,
 - Paying off debt and
 - Financing one-time expenditures.

APPENDIX A

RESPONSE FROM DISTRICT OFFICIALS

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

CENTRAL ISLIP UNION FREE SCHOOL DISTRICT

BOARD OF EDUCATION

FRED PHILIPS, *President*
DANIEL M. DEVINE, *Vice President*
WILLIAM G. SOFTY
MONIQUE B. McCRAY
EDNA CARBAJAL
DORIS DODSON
KELLY VALENTIN
EDWARD F. FREUDENBERG, *Treasurer*
DENISE RIDGEWAY, *District Clerk*

Post Office Box 9027
Central Islip, New York 11722



CRAIG G. CARR, Ed.D.
SUPERINTENDENT OF SCHOOLS

MICHAEL WOLPERT
ASSISTANT SUPERINTENDENT FOR PERSONNEL

KEVIN M. MILLER
ASSISTANT SUPERINTENDENT FOR BUSINESS

SHARON DUNGEE
ASSISTANT SUPERINTENDENT FOR EDUCATION AND ADMINISTRATION

March 5, 2014

Division of Local Government and School Accountability
Office of the State Comptroller
NYS Office Building, Room 3A10
250 Veteran's Memorial Highway
Hauppauge NY 11888-5533

Re: Central Islip Union Free School District – 2013M-380
Response from District

Dear Comptroller:

Please accept this letter as the Central Islip Union Free School District's official response to the preliminary draft findings of your recent audit entitled "Financial Management, Report of Examination" 2013-M-380.

The Central Islip Board of Education and its administration respects Real Property Tax Laws which limits the amount of unexpended surplus funds that can be legally retained by District officials to no more than four (4) percent of the next fiscal year's budget. The District acknowledges the fact that the District's unexpended surplus funds as a percentage of the next year's budget appropriations totaled ten (10) percent at the end of fiscal year 2010-2011, eighteen (18) percent at the end of fiscal year 2011-2012, and five (5) percent at the end of fiscal year 2012-2013. However, the reasons and rationale behind the District's decisions to retain unexpended surplus beyond the statutory limit must be made clear.

On May 26, 2011, the Central Islip Union Free School District commenced litigation against the New York State Education Department (SED) which took the position that the District was required to return to SED approximately \$13,619,629 in State Building Aid previously paid to the District between the 2003-2004 school year and the 2008-2009 school year in connection with aid paid on seven prior year building projects and that the District was not entitled to any future payments of State Building Aid in connection with those building projects. SED based its position upon the fact that five years and three administrations earlier, Central Islip did not timely file final building project cost reports for the seven associated building projects, and that such failure was grounds for eliminating all aid (past and future) associated with these projects.

The District was originally notified verbally by SED officials in February, 2010, that such recoupment of aid would take place at a future date, and in addition, that the District would not be paid the State Building Aid due for the 2009-2010 fiscal year and for all future years State Building Aid was not to be paid in connection with the seven prior year building projects. On April 19, 2011, District officials signed a letter provided by SED that was to commence the recoupment of the \$13,619,629 beginning in June 2011. On May 26, 2011, Albany County Supreme Court granted on behalf of the Central Islip Union Free School District a temporary restraining order and thereby enjoined SED from implementing and enforcing the recoupment of the \$13,619,629 set forth in there April 19, 2011, letter and further ordered SED to pay to the District the State Building Aid it failed to pay for the 2009-2010, 2010-2011, and 2011-2012 school years (approximately \$7,500,000). The approximate \$7,500,000 in additional State Building Aid was paid to the District during the 2011-2012 school year creating the potential, immediate recoupment of over and estimated \$21,120,000.00 from the taxpaying public in Central Islip.

From the time the District was notified in February of 2010 until March 31, 2012, and while the temporary restraining order was in place and litigation remained pending it was the position of the Central Islip Board of Education and its administration that the taxpayers of this District were not to bear the burden of this potential liability which by this time had grown to some \$21,120,000. As you are aware, in connection with the enactment of the April 1, 2012, Budget Bill, the State Legislature approved amendments to the Education Law and thereby provided relief to School Districts, including Central Islip, that had failed to timely file their final building project cost reports, provided that such reposts were filed on or before December 31, 2012. The Budget Bill indicated that such final building project cost reports were ratified and validated and that Districts would only suffer loss of State Building Aid for only the years that the reports were filed late. In the case of Central Islip, the reports were due in June of 2006, and filed in June of 2008 (two years late). According to an affidavit filed in our litigation against SED, an SED official confirmed that Central Islip had filed final building project cost reports for all seven building projects and therefore qualified for the relief under this budget bill. The SED official went on to further confirm that the total amount of State Building Aid estimated to be lost as a result of the remediation provided under this bill to be approximately \$5,460,000.

Immediately upon the relief of this potential \$21,120,000 liability, the district placed the value of the released liability into appropriate reserve accounts. The remaining 1% over the reserve allowance on June 30, 2013 is the exact amount of the remaining liability; thus retained to indemnify the taxpaying public.

See
Note 1
Page 17

In addition to the \$21,120,000 potential liability the Central Islip Union Free School District faced in March 2012, during the 2010-2011 and the 2011-2012 school years the District suffered an unprecedented loss in total State Aid. As a result, programmatic cuts were enacted district-wide along with the excessing of some 150 instructional and non-instructional staff. During those years, the Board of Education adopted budgets based on the revenues it anticipated while being mindful of the corresponding rise in the District's

tax levy and of its resident taxpayers ability to pay all while staying within the “2% tax cap” first enacted for the 2011-2012 fiscal year. It was also during these fiscal years that the Board of Education negotiated with both its instructional and non-instructional bargaining units, which resulted in wage freezes and other concessions. It was in July of 2010 that the Board of Education accepted the tenants of both the New York State Teachers Retirement System and the New York State Employees Retirement System affording some twenty-five employees the opportunity to take advantage of an early retirement incentive. All of these listed reductions in expenses occurred after the adoption of ensuing year Budget(s). It was a major result of these factors; the repayment of some \$7,500,000 in State Building Aid as a result of the temporary restraining order granted, and in addition to the District enacting other cost saving measures that contributed greatly to unexpended surplus funds at the end of these fiscal years which merely contributed to an appearance of over-budgeting.

See
Note 2
Page 17

It was never the intention of the Central Islip Board of Education or its administration to underestimate revenues, overestimate expenditures and appropriate significant unexpended surplus funds not to be used to fund operations during the last three fiscal years (2010-2011, 2011-2012 and 2012-2013).

It was never the intention of the Board of Education or its administration to accumulate unexpended surplus funds exceeding the statutory limit while at the same time purposely increasing the real property tax levy during the last three fiscal years (2010-2011, 2011-2012 and 2012-2013).

With a potential \$21,120,000 potential liability facing the Central Islip Union Free School District; it was for this reason and this reason only that the District exceeded the statutory allowed limit in each of the last three fiscal years (2010-2011, 2011-2012 and 2012-2013). Issuing debt to cover this potential loss and shifting this debt to the District’s resident taxpayers was not an option.

See
Note 1
Page 17

While the district did indeed hold funds in what is termed overestimated budget, underestimated revenues and excess fund balance; it was requested by the district to the Comptroller’s office to provide an avenue to legitimately place these funds. The Comptroller’s office did empathize with our plight, however, it was cited that there was no statutory exceptions to the limit on unexpended surplus plus and no statutory authority to establish a reserve for this liability.

The District recognizes, agrees with, and appreciates your recommendations. We believe that these recommendations provide constructive feedback and will prove to strengthen and improve our overall financial operation, internal controls and reduce risk. We have begun implementation of your recommendations and will include these procedures in our Corrective Action Plan which will be submitted for consideration upon the receipt of the final report and in accordance with the ninety day requirement.

On behalf of the Board of Education of the Central Islip Union Free School District, we would like to thank you and your office for providing us this service. We strive to

continuously improve and strengthen internal controls and oversight of District financial operations. To that end, we appreciate your input.

Very truly yours;

Kevin M. Miller
Assistant Superintendent for Business

APPENDIX B

OSC COMMENTS ON THE DISTRICT'S RESPONSE

Note 1

We understand the District's desire to not burden its taxpayers with this potential liability. However, there is no statutory exception to the 4 percent limit. Furthermore, because there is no statutory authority to establish a reserve for this purpose, the SED claim is no different than any other claim against the District.

Note 2

The Board-adopted budgets included \$16.2 million more than was actually expended in 2010-11 and \$12 million more than was actually expended in 2011-12. At the same time, the District increased its tax levy.

APPENDIX C

AUDIT METHODOLOGY AND STANDARDS

We interviewed District officials to obtain an understanding of the organization and the accounting system and reviewed pertinent documents, such as District policies and procedure manuals, Board minutes and financial records and reports. Further, we reviewed the District's internal controls and procedures over the computerized financial databases to help ensure that the information produced by such systems was reliable.

After reviewing the information gathered during our initial assessment, we evaluated the District's internal controls for the risk of potential fraud, theft or professional misconduct. We then decided upon the reported objectives and scope by selecting for audit the areas most at risk. We selected the Board's financial management of the District for further audit testing. To accomplish our audit objectives and obtain valid audit evidence, our procedures included the following:

- We reviewed reserve funds to ensure that they were adequately funded and in compliance with applicable laws.
- We obtained an understanding of the District's internal control environment and specific controls that are significant to the District's budget process.
- We reviewed the last four annual financial statements, the accompanying management letters prepared by the District's independent public accountant and related budget reports.
- We compared amounts reported on the ST-3 reports to the annual financial statements and balance sheets provided to verify their reliability.
- We analyzed general fund revenue and expenditure trends and budget-to-actual comparisons for the 2008-09 through 2012-13 fiscal years to determine operating surpluses or deficits.
- We reviewed and analyzed reported unexpended surplus fund levels to determine if the unexpended surplus funds complied with the 4 percent statutory limit.
- We reviewed real property tax rates and tax levy increases.

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 D

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