



Lewiston-Porter Central School District Financial Condition

Report of Examination

Period Covered:

July 1, 2010 — June 6, 2014

2014M-202



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

October 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, 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 Lewiston-Porter 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 Lewiston-Porter Central School District (District) is located in the Towns of Lewiston and Porter, in Niagara County. The District is governed by the Board of Education (Board), which is comprised of 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 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 direction of the Board.

There are four school buildings and one administrative building operating within the District, with approximately 2,100 students and 375 employees. The District's budgeted appropriations for the 2014-15 fiscal year are \$41 million, funded primarily with real property taxes and State aid.

The Office of the State Comptroller's Fiscal Stress Monitoring System¹ monitors local governments for indications of fiscal stress, such as declining liquidity and available unrestricted cash. The District was identified as being susceptible to fiscal stress largely because the District's cash available to fund operations had declined to approximately \$855,098 as of June 30, 2013, or less than 25 percent of the average monthly expenditures of the District.

Objective

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

- Did the Board properly plan for and use unrestricted fund balance and reserve funds?

Scope and Methodology

We examined the District's financial condition and use of reserve funds for the period July 1, 2010 through June 6, 2014

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 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

¹ For more information on the Fiscal Stress Monitoring System, see the OSC website at: <http://osc.state.ny.us/localgov/fiscalmonitoring/index.htm>

generally agreed with our findings and indicated they planned to initiate corrective action.

The Board has the responsibility to initiate corrective action. Pursuant to Section 35 of the New York State General Municipal Law, Section 2116-a (3)(c) of the 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

A key component of budgeting is the estimation and use of fund balance, which represents a financing source within the adopted budget. The amount of fund balance retained at year end serves as a financial cushion for unexpected events and maintaining cash flow. The Board and District officials should monitor available fund balance and ensure that it is not reduced to a dangerously low level. The Board and District officials can also establish reserve funds to help finance expenditures.

The Board used fund balance as a financing source in the annual general fund budget until it was nearly depleted. Since 2010-11, the District appropriated more than \$4.7 million in fund balance to finance appropriations in the general fund. This has resulted in a dramatic reduction in the District's total fund balance. During this same time period, the District increased property taxes an average of \$521,000 (2.3 percent) annually. In addition, the District improperly used two reserves to help fund general fund operations during the 2012-13 fiscal year.

Fund Balance and Budgeting

Fund balance is the difference between revenues and expenditures accumulated over time. When maintained at reasonable levels, fund balance provides cash flow and can be used to help finance the next fiscal year's operations. The portion of the fund balance that is used to help finance the next fiscal year's budget is referred to as appropriated fund balance. The remaining portion, which can be used for cash flow purposes and unanticipated expenditures, is unrestricted fund balance. However, when too much fund balance is used to finance operations, instead of relying on recurring revenues to fund recurring expenditures, fund balance is depleted and the District may be left without adequate balances for cash flow needs or unforeseen circumstances.

The District's continued reliance on fund balance as a financing source in the annual budget has negatively impacted the District's financial condition. The District reported \$260,654 of unrestricted fund balance in the general fund as of June 30, 2013, and it is expected that unrestricted fund balance will further decrease to \$259,345 as of June 30, 2014. Given the size of the District's operations, this balance is well below 1 percent of the ensuing year's budget, which is a dangerously low level.

Figure 1: General Fund Unrestricted Fund Balance

	FY 2010-11	FY 2011-12	FY 2012-13	FY 2013-14 (Draft Financial Statements)
Beginning Fund Balance	\$7,294,156	\$4,526,730	\$4,183,972	\$1,210,394
Revenues	\$37,951,934	\$38,697,705	\$38,084,847	\$39,251,744
Expenditures	\$40,719,360	\$40,300,463	\$41,058,425	\$39,144,431
Operating Surplus/(Deficit)	(\$2,767,426)	(\$1,602,758)	(\$2,973,578)	\$107,313
Prior Period Adjustment - Increase in Fund Balance	\$0	\$1,260,000 ^a	\$0	\$0
Year-end Fund Balance	\$4,526,730	\$4,183,972	\$1,210,394	\$1,317,707
Less: Unrestricted, Appropriated for the Next Fiscal Year	\$1,800,000	\$1,800,000	\$500,000	\$600,000
Less: Encumbrances ^b	\$494,741	\$47,805	\$4,160	\$12,782
Less: Employee Benefit Accrued Liability Reserve	\$926,247	\$926,247	\$433,000	\$433,000
Less: Debt Reserve	\$1,145,000	\$1,145,000	\$0	\$0
Less: Capital Reserve	\$12,580	\$12,580	\$12,580	\$12,580
Unrestricted Year-end Fund Balance ^c	\$148,162	\$252,340	\$260,654	\$259,345

^a The District previously recorded grant money received from the Greenway Recreation/Tourism fund (Greenway) in the capital fund. The District decided to reclassify this revenue to the general fund to finance bond payments related to Greenway projects.

^b Encumbrances represent purchase orders, contracts or other commitments for the expenditures of moneys. Encumbrances are presented as a reservation of fund balance and do not represent expenditures or liabilities. The commitment will be honored and the expenditures will be recognized in a subsequent period when the liability is incurred or the commitment is paid.

^c Includes all general fund net assets that do not meet the criteria of non-spendable, restricted, committed or assigned and are deemed to be available for the general use by the school district.

Revenues and expenditures in the general fund for 2013-14 produced an operating surplus of \$107,313, which slightly improved the District’s tenuous financial position. The District realized negative budget variances for revenues from fiscal years ending 2011 through 2013 and expenditures over the last four fiscal years. For example, during 2012-13, actual revenues were \$588,000 less than estimated, and expenditures exceeded budgeted appropriations by \$585,000. These variances reduced fund balance by more than \$1.1 million.

We also reviewed the District’s 2014-15 budget, which is similar to the 2013-14 budget. The District has not made any significant changes to the budget to improve its financial position. If the District realizes unfavorable budget variances in the 2014-15 fiscal year, it could exhaust the District’s unrestricted fund balance in the general fund and there will be no fund balance available to fund unanticipated costs or maintain cash flow.

Reserves

The Board is responsible for adopting a comprehensive reserve policy that clearly communicates to District taxpayers the purpose and intent for establishing each reserve fund, the manner in which the Board will fund and maintain each reserve fund, the optimal or

targeted funding levels and conditions under which each fund's assets will be used or replenished.

District officials established an employee benefit accrued liability reserve (EBALR)² to fund the cash payment of accrued and unused sick, vacation and other leave time due employees upon separation from service. The reported balance of this reserve as of June 30, 2011 was approximately \$926,000. District officials also segregated \$1.1 million in a debt reserve,³ presumably to be used to help pay the principal and interest on the related outstanding debt. District officials appropriated funds from the EBALR and the debt reserve to finance general fund operations.

During 2012-13, District officials appropriated \$493,000 of the EBALR and \$680,000 from the debt reserve to finance the unplanned portion of the reported operating deficit of \$2.9 million.⁴ The EBALR funds were used to pay retirement incentives, separation payments and the cash value of accrued sick leave. We estimate that approximately \$355,169 of EBALR funds were inappropriately used to fund operating costs unrelated to sick leave payouts. Furthermore, in 2012-13, the District budgeted \$4.2 million in debt service costs, and subsequently spent \$4.3 million, exceeding the budget by \$100,000. We estimate that none of the debt reserve was used to help repay outstanding debt as intended.⁵

District officials stated that they needed to use fund balance and reserves to fund operations because of the effects of the tax cap levy limit, increasing health care and retirement costs and decreasing State aid. Sound budgeting practices, together with prudent management of fund balance and reserves, will help ensure that sufficient funding will be available to sustain operations, address unexpected occurrences and satisfy long-term obligations or future expenditures.

Recommendations

The Board should:

1. Reduce its reliance on fund balance as a financing source in the annual budget and adopt budgets that rely on recurring revenue to fund recurring expenditures.

² See General Municipal Law

³ The District has reported a debt reserve in the general fund since the 2001 fiscal year. At our exit discussion, District officials indicated they were unsure whether the reserve included unexpended bond proceeds from completed capital projects or only surplus cash from prior years' operations.

⁴ \$1.8 million of the operating deficit was planned, as indicated by the appropriation of fund balance in the 2012-13 adopted budget.

⁵ The remaining \$465,000 of the debt reserve was appropriated in the 2013-14 budget.

2. Closely monitor actual operating results to prevent unfavorable budget variances and further deterioration of unrestricted fund balance.
3. Develop and adopt a reserve policy and ensure that reserves are properly used.

APPENDIX A

RESPONSE FROM DISTRICT OFFICIALS

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



Lewiston-Porter Central School District

Aiming Higher

September 25, 2014

Mr. Jeffrey D. Mazula
Buffalo Regional Office
Office of the State Comptroller
295 Main Street, Suite 1032
Buffalo, New York 14203

Dear Mr. Mazula:

On September 10, 2014, Lewiston-Porter Central School District received a draft report of an audit performed by the NYS Comptroller's Office. After reviewing the draft and meeting with staff members from the Comptroller's Office, the District offers the following response regarding this report.

As a result of many factors, including the reduction in State Aid, the tax cap limit, as well as increased State pension costs, Lewiston-Porter CSD experienced dwindling financial resources, resulting in fiscal stress on the District. In an attempt to balance expenditures and revenues, the District eliminated 22 staff positions in 2012-2013 and 29 in 2013-2014. However, this alone was not able to totally stem the financial decline.

At the end of the 2012-2013 year, to correct a \$2.9 million operating deficit, and upon the advice of the District's external audit firm, the debt reserve fund was liquidated and money from the EBLAR reserve was spent to pay for retiree health benefits. Before liquidating the debt reserve extensive review of records was completed to determine the origin of the moneys in this reserve. Officials were unable to find any indication this reserve had been properly set up or funded. Therefore, through proper board action, the reserve was liquidated.

For the 2013-2014 fiscal year, the Superintendent took a much greater role in budget development to ensure revenues and expenditures were in better balance. The reliance on fund balance was significantly reduced from \$1.8 million in past years to \$500,000 for the 2012-2013 year. In addition, the Board retained a retired, experienced School Business Official to help determine what further steps needed to be taken to correct the fiscal problems.

The above mentioned steps have made a positive change in the District's fiscal condition. Between 2012-2013 and 2013-2014, the District experienced a \$ 3 million change in Operating Surplus/Deficit from a negative (deficit) in 2012-2013 of \$ 2,973,578 to a \$107,313 positive (surplus) in 2013-2104.

There is recognition by the Board and its executive staff that more needs to be done. Processes, procedures, staffing reorganization and auditor changes have been under consideration. Some changes have already been made and others are in the planning stages. Specifics on these changes will be provided when the Board completes its Corrective Action Plan (CAP) later this year.

The District wishes to thank the Comptroller's staff for the assistance and time taken to help Lewiston-Porter CSD with this matter.

Sincerely yours,

R. Christopher Roser
Superintendent of Schools

Cc


J. Riordan
S. Villiers

R. Christopher Roser

4061 Creek Road, Youngstown, NY 14174

Phone: 716-286-7266 Fax: 716-754-2755 Email: roserc@lew-port.com

www.lew-port.com

APPENDIX B

AUDIT METHODOLOGY AND STANDARDS

Our overall goal was to assess the adequacy of the internal controls put in place by officials to safeguard District assets for the period July 1, 2010 through June 6, 2014. To accomplish this, our initial assessment included a review of financial condition, payroll and information technology. During the initial assessment, we interviewed appropriate District officials, performed limited tests of transactions and reviewed pertinent documents, such as District policies and procedures, Board minutes and financial records and reports. In addition, we reviewed the District's internal controls and procedures over its computerized financial systems to help ensure that the information produced by such systems was reliable.

After reviewing the information gathered during our initial assessment, we determined where weaknesses existed and evaluated those weaknesses for the risk of potential fraud, theft and professional misconduct. We then decided on the reported objective and scope by selecting for audit those areas most at risk. We selected financial condition for further audit testing.

To accomplish our objective we performed the following procedures:

- We reviewed financial condition related policies and procedures.
- We interviewed District officials regarding the District's financial condition.
- We reviewed adopted budgets, financial statements, financial reports and other relevant supporting schedules.

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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