



Cuba-Rushford Central School District Financial Management

Report of Examination

Period Covered:

July 1, 2011 – March 27, 2015

2015M-125



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

August 2015

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 Cuba-Rushford Central School District, entitled Financial Management. 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 Cuba-Rushford Central School District (District) is located in the Towns of Belfast, Caneadea, Centerville, Clarksville, Cuba, Friendship, New Hudson and Rushford in Allegany County and the Towns of Farmersville, Freedom, Hinsdale, Ischua and Lyndon in Cattaraugus County. The District is governed by the Board of Education (Board) which is composed of seven elected members and 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 and is responsible, along with other administrative staff, for the District's day-to-day management under the Board's direction. The Business Executive (Executive) prepares budgets and manages the business affairs of the District. The Board, Superintendent and Executive are responsible for the annual budget. The District contracts with the Cattaraugus-Allegany Board of Cooperative Educational Services (CABOCES) to provide its central business functions.

The District operates two schools with approximately 850 students and approximately 200 employees. The District's general fund budgeted appropriations for 2014-15 totaled \$21 million, funded primarily with State aid and real property taxes.

Objective

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

- Did the Board and District officials effectively manage the District's fund balance?

Scope and Methodology

We evaluated the District's management of financial activities for the period July 1, 2011 through March 27, 2015 and projected certain financial activity through June 30, 2015. We also reviewed certain information relating to the establishment, use and funding of certain reserves back to 1991.

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 generally agreed with our recommendations and indicated they planned to take corrective action.

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 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 Management

A school district's financial condition is a factor in determining its ability to continue funding public educational services. The responsibility for accurate and effective financial management rests with the Board, Superintendent and Executive.¹ District officials are responsible for adopting realistic budgets and for ensuring that fund balance does not exceed the amount allowed by law. Fund balance represents the cumulative residual resources from prior fiscal years that can, and in some cases must, be used to lower property taxes for the ensuing fiscal year. A district may retain a portion of fund balance, referred to as unrestricted fund balance, but must do so within the legal limits established by New York State Real Property Tax Law (RPTL).² A district also can establish reserves to finance future costs for a variety of specified objects or purposes.

District officials have not effectively managed fund balance as unrestricted fund balance annually exceeded RPTL limits (projected to exceed by \$4.0 million as of June 30, 2015) and reserves are overfunded by approximately \$3.2 million. This occurred because District officials consistently overestimated expenditures by a total of \$8.5 million over the four-year period ranging from 7 to 14 percent more than actual expenditures. Although District officials adopted budgets which included appropriated fund balance, due to their overestimation of expenditures, the total appropriated fund balance was not needed. Despite the excess unrestricted fund balance, District officials continued to raise taxes each of the four years.

Budgeting and Unrestricted Fund Balance

We compared the District's budgeted expenditures and revenues with actual operating results for fiscal years July 1, 2011 through February 28, 2015 and projected results as of June 30, 2015. While revenue estimates were generally reasonable, District officials consistently overestimated expenditures by approximately \$8.5 million over four years, as shown in Figure 1. The most significant variances were found in employee benefits (\$2.4 million), teaching (\$2.0 million), programs for children with handicapping conditions (\$1.5 million), pupil transportation (\$1.1 million) and debt service interest (\$1.2 million).

¹ This position is part of the central business function contracted from CABOCES.

² RPTL statutorily limits the amount of unrestricted fund balance to 4 percent of the ensuing year's budget.

Figure 1: Over-Estimated Expenditures				
Fiscal Year	Budgeted Expenditures	Actual Expenditures	Difference	Percentage Difference
2011-12	\$19,921,314	\$18,525,444	\$1,395,870	7%
2012-13	\$19,780,932	\$18,187,317	\$1,593,615	8%
2013-14	\$20,676,616	\$17,967,040	\$2,709,576	13%
2014-15	\$20,941,359	\$18,109,023	\$2,832,336	14%

Since many of these costs are driven by contractual agreements, they should be reasonably predictable and not be consistently overestimated. The Board's inability to adopt budgets with more accurate expenditure estimates has contributed to an increasing amount in unrestricted fund balance, as shown in Figure 2.

Figure 2: Fund Balance Over Statutory Limit and Tax Levy				
	2011-12	2012-13	2013-14	2014-15 ^a
Ensuing Year's Appropriations	\$19,780,932	\$20,676,616	\$20,941,359	\$20,863,591
Unrestricted Fund Balance at Fiscal Year End	\$2,445,488	\$3,666,184	\$4,085,756	\$4,867,194
Statutory Limit	\$791,237	\$827,065	\$837,654	\$834,544
Amount Over Statutory Limit	\$1,654,251	\$2,839,119	\$3,248,102	\$4,032,650
Amount as a Percentage of Ensuing Year's Appropriations	12%	18%	20%	23%
Tax Levy (Including STAR) ^b	\$5,589,000	\$5,700,780	\$5,843,300	\$5,989,383

^a 2014-15 is actual data through February 28, 2015 and projected through June 30, 2015
^b The New York State School Tax Relief Program

Annually, unrestricted fund balance exceeded the 4 percent limit by amounts that ranged from \$1.7 million in 2011-12 to a projected \$4.0 million by the end of 2014-15. Contributing to the unrestricted fund balance growth, District officials' overestimation of expenditures resulted in operating surpluses totaling \$2.5 million.³ We further note that, while District officials developed a multiyear plan⁴ for 2013-2017, the plan continues to project unrestricted fund balance in excess of the statutory limit each year rather than using unrestricted fund balance to lower the tax levy, which results in taxpayers paying millions of dollars in excess taxes.

Reserves

Reserve funds may be established by Board action, pursuant to various laws, and are mechanisms for accumulating money for future capital outlays and other allowable purposes. The Board adopted a reserve policy in 2011 which requires that District officials prepare an annual report of reserve activity that includes a description of

³ Based on actual results of operations for 2012-13 and 2013-14 and projected results of operations for 2014-15

⁴ Planning on a multiyear basis enables District officials to identify developing revenue and expenditure trends, establish long-term priorities and goals and consider the impact of near-term budgeting decisions on future fiscal years.

each reserve, any withdrawals made, the cash balance of the reserves and the projected needs for each reserve in the upcoming fiscal year. Furthermore, shortly after our fieldwork began, District officials developed a reserve plan setting funding thresholds and planned use of some of the reserves. However, the plan does not indicate projected needs for upcoming fiscal years.⁵

As of June 30, 2014, the District reported six reserves totaling \$4.3 million. The Board then established three additional reserves in December 2014 totaling \$240,000 and increased two existing reserves by \$730,000. We analyzed the District's reserves for reasonableness and adherence to statutory requirements. We found the District properly established and/or funded the following four of the nine reserves: workers' compensation (\$242,000), repair (\$200,000), insurance (\$25,000) and property loss (\$15,000).⁶ We found that the remaining five reserves, totaling approximately \$4.8 million, were overfunded by approximately \$3.2 million.

Retirement Contribution Reserve – This reserve is authorized to make contributions for employees covered by the New York State and Local Employees' Retirement System.⁷ This reserve reported a balance of \$1.4 million as of February 28, 2015. However, the Board has budgeted and paid expenditures for retirement contributions in the general fund budget and, therefore, levied taxes for this purpose rather than using this reserve. The District's reserve plan indicates that the Board plans to fund this reserve at five times the highest rate of related expenditures from the past five years. This level of funding is excessive as the Board annually levies taxes for these expenditures, which average approximately \$268,000, rather than budgeting to appropriate reserve funds.⁸ As a result, we question the \$1.4 million the Board has restricted in this reserve.

Employee Benefit Accrued Liability Reserve – This reserve is authorized for the cash payment of accrued and unused sick, vacation and certain other accrued but unused leave time owed to employees when they separate from District employment.⁹ The District's calculated liability for such compensated absences was approximately \$1.6 million as of June 30, 2014.¹⁰ However, the reserve balance was \$2.6 million. As a result, this reserve is overfunded by approximately \$1 million.

⁵ December 2014

⁶ The District used a net of \$10,000 from the workers' compensation reserve in 2012-13 which appeared to be properly supported. The District did not use funds from these remaining three reserves.

⁷ General Municipal Law (GML) authorizes the Board to establish this reserve.

⁸ Average based on actual expenditures in fiscal years 2011-12 through 2013-14

⁹ GML authorizes the Board to establish this reserve.

¹⁰ We reviewed the District's liability calculations and determined they generally appeared reasonable and supported.

Unemployment Insurance Reserve – This reserve is authorized to reimburse the State Unemployment Insurance Fund for payments made to claimants and had a balance of \$253,995 as of February 28, 2015.¹¹ The Board has annually budgeted and paid expenditures for unemployment costs, which average approximately \$35,000, from the general fund budget and, therefore, levied taxes for this purpose rather than using this reserve.¹²

While the District's reserve plan identifies the Board's intention to fund this reserve to a level which is approximately three times the highest unemployment expenditure from the past five years, there is no current plan or past practice of budgeting to appropriate the reserved funds towards related expenditures.¹³ As a result we question the extent of funds the Board has restricted in this reserve.

Debt Service Fund – In certain circumstances, money must be restricted for debt service. For example, the proceeds from the sale of property must be restricted if related debt remains outstanding. In addition, unexpended debt proceeds and related interest earnings must be restricted and used to pay debt service on that debt issue or for related capital expenditures. Districts are not allowed to establish a debt reserve for any other purpose.

The District maintains a debt service fund with a balance of \$297,786 as of February 28, 2015. District officials were unable to provide documentation to identify the source of these funds, or demonstrate why this money should be restricted in the debt service fund. Debt payments are budgeted for and paid out of the general fund. The Executive stated the fund was originally established in 1991 and funded with excess general fund money. Therefore, these funds are not being used for taxpayer benefit. As such, the funds in this reserve should be returned to the general fund¹⁴ and used for District operations and/or to reduce the tax levy.

Capital Reserves – This reserve is authorized to pay the cost of any object or purpose for which bonds may be issued and is established solely by voter approval.¹⁵ The proposition put before the voters must specify the purposes of the reserve, ultimate dollar amount to be deposited into the reserve, probable term of the reserve and source of the funds to be deposited into the reserves.

¹¹ GML authorizes the Board to establish this reserve.

¹² Average based on actual expenditures in fiscal years 2011-12 through 2013-14

¹³ In 2012-13 the District did not budget for but transferred \$75,000 from this reserve into the general fund; however, within the same year, the District added \$65,000 from the excess fund balance back into the reserve at year end, for a net difference of \$10,000.

¹⁴ Money not statutorily required to be restricted in the debt service fund must be returned to the general fund.

¹⁵ The New York State Education Law authorizes the Board to establish this reserve subject to voter approval.

During the last four fiscal years, the District's two capital reserves carried a balance of \$220,000. While District officials provided resolutions for two capital reserves established in 1991, the resolutions do not indicate voter approval or probable term of the reserves. One resolution does not indicate the specific Board-authorized purpose, such as financing a capital expenditure with operating funds.¹⁶ As such, approximately \$220,000 of general fund money is improperly residing in the capital projects fund.

Recommendations

The Board should:

1. Adopt budgets that include realistic expenditure estimates of actual needs, so as not to overtax District taxpayers.

The Board and District officials should:

2. Ensure that unrestricted fund balance is within statutory limits.
3. Refine the multiyear plan to reduce unrestricted fund balance in a manner that benefits District taxpayers. Such uses could include, but are not limited to, increasing necessary reserves, paying off debt, financing one-time expenditures and reducing property taxes.
4. Review the reserves' balances at least annually and determine if the amounts reserved are necessary, maintained and reasonably funded in compliance with the District's reserve fund policy and long-term plan and with applicable statutory requirements. To the extent that they are not, transfers should be made to unrestricted fund balance (where allowed by law) or to other reserves established and maintained in compliance with statutory directives.
5. Determine if the capital reserves were properly established to ascertain whether the funds contained therein are properly restricted.

¹⁶ One capital reserve resolution indicates the purpose was to finance purchases of buses.

APPENDIX A

RESPONSE FROM DISTRICT OFFICIALS

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

CUBA-RUSHFORD CENTRAL SCHOOL

*Superintendent of Schools, 585-968-2650 / Fax: 968-2651
Transportation Supervisor, 585-968-2446*

*Cuba-Rushford Middle/High School
5476 Route 305N, Cuba, NY 14727
585-968-2650 / Fax: 968-1091*

*Cuba-Rushford Elementary School
15 Elm Street, Cuba, NY 14727
585-968-1760 / Fax: 968-3181*

August 20, 2015

Jeffrey D. Mazula, Chief Examiner
Office of the State Comptroller
295 Main Street, Suite 1032
Buffalo, New York 14203-2510

Dear Mr. Jeffrey Mazula,

The Cuba-Rushford School District is in receipt of the draft audit, financial management, for the period of July 1, 2011 through March 27, 2015, prepared by the Office of the State Comptroller. The Board of Education and the administration would like to thank the state auditors for their patience and professionalism throughout this audit as well as the recommendations cited in the report. This letter includes the district's response as well as the Corrective Action Plan.

Audit Recommendation: Adopt budgets that include realistic expenditure estimates of actual needs so as not to overtax District taxpayers.

District Comment: The district budgets conservatively throughout the budget process in open session and reviews historical expenditure reports for the last five prior years to adequately develop a budget that ensures we are financially prepared to meet the planned and unplanned programmatic needs of our students. The district has reduced the budget for the upcoming year and is reducing the tax levy for the 2015-16 school year by over 2.5% as we see the positive results of bidding all supplies and services and creating shared service opportunities with neighboring districts.

Implementation Plan of Action: The district will continue to look at expenditure trends over 5 years, examine the success of the shared service models put in place over an 18 months period and make adjustments to the proposed budget in accordance with our five year financial plan.

Implementation Date: During the 2015-2016 budget development process.

Person(s) Responsible for Implementation: District Administration, Business Manager and the Board of Education.

Audit Recommendation: Ensure that unrestricted fund balance is within statutory limits.

District Comment: We recognize that our budgeted expenditures in certain areas may have been overstated as a result of anticipating possible expenses to ensure our ability to meet the programmatic needs of students. As cited in the audit report, the district

<http://www.crcs.wnyric.org>

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has carried an unassigned fund balance in excess of the 4% statutory limit. However, the district has reduced special education and transportation budgets for two consecutive years. This is a direct result of following the recommendations of our external auditors who have provided clear guidance and helped develop the district's five-year financial plan.

It is important to note, particularly over the past four years, that the district has had to reduce programs, reduce thirty four (34) staff and close an elementary school in the town of Rushford due to the economic crisis, state aid reductions, and the reduction of district aid through the Gap Elimination Adjustments (GEA). As a result, our budgeting has become more conservative and the district has budgeted expenditures that include unanticipated, but highly probable expenses based on our ten year expenditure reports. As a district that is situated in rural Western New York with a very transient population, our district faces challenges that are very unique to us. For example, as a district that encompasses 156 square miles and transports to schools 60 miles away, we attempt to anticipate the cost of transportation, special education programs and placement outside the district to meet our student's needs.

In addition, over the 2012-2015 period, the district has examined our expenditure reports and pursued securing better pricing as recommended by the Comptroller's Procurement Guidelines through the following venues:

- Bidding all services and supplies on an annual basis.
- Sharing Services and employees with our three neighboring districts of Belfast, Friendship and Bolivar-Richburg.
- Reducing our utility costs through procurement practices and system upgrades through capital projects.

The district agrees with the comptroller's findings that our projected expenditures are slightly overstated. They are overstated with particular expenses for 18 months until the particular cost reduction model being implemented has proven to be educationally and financially effective. Thus, cost reductions come as shared saving models are proven and can be counted on.

In addition, during the 2013-14 school year, the district pursued owed state aid dated back to 2004 and received \$400,000 in revenues it did not anticipate.

Implementation Plan of Action: The district will continue to examine expenditure reports and continue to reduce or eliminate any assigned fund balance for the upcoming year as recommended by the external auditors in the last three years. The Amount of Assigned fund balance has been steadily reduced over the last three years as noted

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below:

- 2012-13 (\$1,234,278)
- 2013-14 (\$925,981)
- 2014-15 (\$442,449)

Implementation Date: During the 2015-2016 budget development process.

Person(s) Responsible for Implementation: District Administration, Business Manager and the Board of Education.

Audit Recommendation: Refine the multiyear plan to reduce unrestricted fund balance in a manner that benefits District taxpayers. Such uses could include, but are not limited to, increasing necessary reserves, paying off debt, financing one-time expenditures and reducing property taxes.

District Comment: The district established a five-year financial plan that is very conservative after coming out of the economic crisis in 2010. The conservative practices take into account unforeseen expenses that the district has incurred in the past five years and the possible loss of aid which the district experienced to the tune of \$4.5 million over 5 years. These conservative practices have allowed us to follow our Board Adopted Strategic Plan, reestablish programs and plan for the future through the board developed and adopted Reserve Plan (2013-14)

Implementation Plan of Action: The district will not acknowledge the loss of \$4.5 million it has lost in aid over the last 5 years when updating our multi year financial plan. The district will consider paying off debt as we proceed with long-term financing of our most recent capital project and is reducing the tax levy by over 2.5% for the 2015-16 school year.

Implementation Date: During this past year's budget development process, the August 2015 tax rate setting process and the 2016-2017 budget development process.

Person(s) Responsible for Implementation: District Administration, Business Manager and the Board of Education.

Audit Recommendation: Review the reserves balances at least annually and determine if the amounts reserved are necessary, maintained and reasonably funded in compliance with the District's reserve fund policy, long term plan and applicable statutory requirements. To the extent that they are not, transfers should be made to unrestricted fund balance (where allowed by law) or other reserves, established and maintained in compliance with statutory directives.

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District Comment: The district began the development of a reserve plan in the 2013 school year and adopted the plan in December 2014 in accordance with Cuba-Rushford's Board Policy #5511 Reserve Funds and the guidance from the Comptroller's Offices Guide on Reserve Funds Pages 1 and 2. It reads...

"Reserve funds, like other savings plans, are mechanisms for accumulating cash for future capital outlays and other allowable purposes. The practice of planning ahead and systematically saving for capital acquisitions and other contingencies is considered prudent management. Saving for future capital needs can reduce or eliminate interest and other costs associated with debt issuances. Similarly, certain reserve funds can be utilized to help protect the budget against known risks (a potential lawsuit) or unknown risks (a major ice storm).

Most reserve funds are established to provide resources for an intended future use. An important concept to remember is that a reserve fund should be established with a clear intent or plan in mind regarding the future purpose, use and, when appropriate, replenishment of funds from the reserve. Reserve funds should not be merely a "parking lot" for excess cash or fund balance. Local governments and school districts should balance the desirability of accumulating reserves for future needs with the obligation to make sure taxpayers are not overburdened by these practices. There should be a clear purpose or intent for reserve funds that aligns with statutory authorizations."

The district agrees with the guide recommendations. Reserves are a prudent way to establish financial stability for the district. Furthermore, the district agrees that reserves should not be merely a "parking lot" for excess cash. For this reason, the Cuba-Rushford Reserve Plan concisely describes when each fund was created, the use of Fund (intent), the funding method (unrestricted fund-balance), the funding level, and how it will be monitored.

Since the last State Comptroller's Audit in 2008, the district has not contributed to the Employee Benefit Accrued Liability Reserve (EBALR) fund. Furthermore, the district has utilized the funds to pay accumulated unused sick days payable upon retirement and reduced the (EBALR) fund by \$750,000.

Implementation Plan of Action: Continue to follow the Reserve Plan as funding levels will decrease with past higher expenditures not being utilized in the new five year average. The Board of Education will revisit funding levels prior to the 2016-17 budget development process.

Implementation Date: December 2015 during the beginning of the budget development process.

Person(s) Responsible for Implementation: District Administration, Business Manager and the Board of Education.

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Audit Recommendation: Determine if the capital reserves were properly established to ascertain whether the funds contained therein are properly restricted.

District Comment: The capital reserves the audit refers to were established soon after the merger of Cuba Central School and Rushford Central School. The remaining balance will be expended with voter approval.

Implementation Plan of Action: No corrective action being taken.

Implementation Date: NA

Person(s) Responsible for Implementation: District Administration, Business Manager and the Board of Education.

Sincerely,

Carlos Gildemeister
Superintendent of Schools
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APPENDIX B

AUDIT METHODOLOGY AND STANDARDS

Our objective was to assess the District's financial management practices for the period July 1, 2011 through March 27, 2015 and project certain financial activity through June 30, 2015. We also reviewed certain information relating to the establishment, use and funding of certain reserves back to 1991. To accomplish our objective, we performed the following procedures:

- We interviewed District officials and Board members to gain an understanding of the District's financial management practices.
- We projected 2014-15 revenues and expenditures to June 30, 2015 by analyzing the rate of actual revenues and expenditures as of February 28, 2015 for the current fiscal year and then applying that rate to the remaining four months of the fiscal year (March, April, May and June). We then compared the resulting projected revenues and expenditures to the adopted budget and investigated variances over \$10,000 to account for significant variances. We then analyzed the significant variances further and adjusted the amounts accordingly.
- We calculated unrestricted fund balance as a percentage of the ensuing year's appropriations to determine if the District was within the statutory limit during 2011-12 through 2014-15.
- We analyzed the District's 2014-15 budget and compared the prior year's actual results to the current year's budget and expenditures and encumbrances through February 28, 2015 to determine if the District is overestimating expenditures.
- We analyzed the trend in fund balance for 2011-12 through 2013-14. We compared appropriated fund balance to the same year's operating results to determine the extent to which the amount of appropriated fund balance that the District budgeted was actually used.
- We analyzed the District's use and funding of reserves from 2011-12 through 2013-14 to determine if the funds were properly authorized and planned for. We reviewed the reserve balances and compared them to the related liabilities and expenditures to determine if the balances were excessive. We also reviewed the District's December 2014 reserve plan and discussed it with District officials to determine if there were any plans for the use of the funds.
- We reviewed the real property tax levy increases to determine the rate of increase in property taxes compared to the increase in fund balance.
- We reviewed the property tax cap reports for 2012-13 through 2014-15 to determine if the District stayed within the tax cap.

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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