



Maine-Endwell Central School District Financial Condition

Report of Examination

Period Covered:

July 1, 2011 — January 3, 2013

2013M-49



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

May 2013

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 Maine-Endwell 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 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 Maine-Endwell Central School District (District) is located in the Towns of Maine, Nanticoke, Union, Newark Valley, and Owego, in Broome and Tioga Counties. 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 (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 direction of the Board.

On July 1, 2012, the Board entered into a contract with the Broome-Tioga Board of Cooperative Education Services (BOCES) for central business office (CBO) operations.¹ This agreement allows the BOCES CBO to provide all financial operations, including accounting, estimating, analyzing, and reporting of the District's financial performance. The CBO is now responsible for the District's daily financial operations, payroll processing, purchasing, cash disbursements, and claims auditing. This includes employing personnel with the knowledge and experience to ensure that District operations are performed within the confines of adopted budgets and in the best interests of the District taxpayers.

There are four schools in operation within the District, with 2,557 students and 459 employees. The District's general fund budgeted expenditures for the 2012-13 fiscal year were approximately \$46.5 million, which were funded primarily with State aid, real property taxes, and grants.

During the 2012-13 fiscal year it became evident to District management that the District was in a dire financial position. The projected operations for fiscal year 2012-13 indicate a deficit approaching \$3.6 million. District officials are in the process of addressing this deficit and developing a budget for the 2013-14 fiscal year.

Objective

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

- Did the Board and District management effectively manage the District's financial condition?

¹ The District has contracted with the CBO since 2002 for payroll services, since 2005 for accounts payable services, and since 2007 for fixed asset services.

**Scope and
Methodology**

We examined the District’s financial condition for the period July 1, 2011, through January 3, 2013. To develop additional information for perspective and background, we extended our scope back to review certain financial data from the 2009-10 and 2010-11 fiscal years. We also performed comparative analyses of the District’s financial performance to the component districts in the Broome-Tioga BOCES.

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 indicated in Appendix A, District officials generally agreed with our findings and recommendations and indicated that they have taken, or plan 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 Education Law and Section 170.12 of the Regulations of the Commissioner of Education, a written corrective action plan (CAP) that addresses the findings and recommendations in this report must be prepared and provided to our office within 90 days, with a copy forwarded to the Commissioner of Education. To the extent practicable, implementation of the CAP must begin by the end of the next fiscal year. For more information on preparing and filing your CAP, please refer to our brochure, *Responding to an OSC Audit Report*, which you received with the draft audit report. The Board should make the CAP available for public review in the District Clerk’s office.

Financial Condition

The Board is responsible for making sound financial decisions in the best interests of the District, the students it serves, and the taxpayers who fund its programs and operations. Sound budgeting practices based on accurate estimates, together with prudent fund balance management, ensure that sufficient funding will be available to sustain operations, address unexpected occurrences, and satisfy long-term obligations or future expenditures. A key component of budgeting is fund balance, which represents moneys accumulated from prior years. The amount of fund balance retained at year end serves as a financial cushion for unexpected events and maintaining cash flow. District officials should monitor available fund balance throughout the year and ensure that it is not depleted to a dangerous level.

Use of Fund Balance — Over the past three years, District officials have tried to maintain the same level of programs and services while keeping the tax levy as low as possible. However, they were able to do so only by continually appropriating fund balance, resulting in the drastic depletion of the year-end unexpended surplus fund balance from \$1.7 million in 2009-10 to just over \$64,000 (or 0.2 percent of District expenditures) in 2011-12.

Table 1: Operations and Fund Balance				
	2009-10	2010-11	2011-12	Total
Beginning Fund Balance	\$8,419,459	\$9,574,227	\$7,725,026	
Revenues	\$41,718,972	\$43,887,662	\$41,736,288	\$127,342,922
Plus: Transfers In	\$187,585	\$122,701	\$1,565,000	\$1,875,286
Expenditures	\$40,703,867	\$45,806,242	\$44,759,884	\$131,269,993
Less: Transfers Out	\$47,922	\$53,322	\$51,320	\$152,564
Operating Surplus/(Deficit)	\$1,154,768	(\$1,849,201)	(\$1,509,916)	(\$2,204,349)
Year-End Fund Balance	\$9,574,227	\$7,725,026	\$6,215,110	
Less: Unexpended Surplus Appropriated for the Next Fiscal Year	\$2,500,000	\$2,500,000	\$2,500,000	\$7,500,000
Less: Restricted Fund Balance	\$5,339,048	\$5,100,650	\$3,651,059 ^a	
Unexpended Surplus Fund Balance at Year End	\$1,735,179	\$124,376	\$64,051	

^a Includes approximately \$42,000 in assigned, unappropriated fund balance

In an effort to limit tax increases, the Board adopted a budget that planned to spend \$2.5 million of appropriated fund balance in each of the three fiscal years 2010-11, 2011-12, and 2012-13. While the District did not use as much fund balance as planned in either the 2010-11 or 2011-12 fiscal years, the net operational deficit in those two years and the continued use of fund balance to finance operations

for 2012-13 resulted in a near depletion of its unexpended surplus fund balance. As shown in Table 1, at the end of the 2011-12 fiscal year the District had only \$64,000 of unexpended surplus following a decline of almost \$1.7 million over the three-year period.

Revenue Estimates — Further, over the same three-year period the District received \$2.4 million less in revenues than budgeted. Most of this shortfall was from State aid and interest earnings. Estimates of State aid that the District could expect to receive for each fiscal year were available from the New York State Education Department (SED) weeks before the Board adopted each budget;² however, the District’s budget estimates were well above the SED estimates, as Table 2 shows.

	Budget Estimates				Actual Aid Received	
	SED Estimate	District’s Budgeted Estimate	Variance (Amount)	Variance (Percent)	State Aid Received	Variance From SED Estimate
2009-10	\$18,107,152	\$21,541,938	\$3,434,786	19%	\$17,138,362	(\$968,790)
2010-11	\$20,585,480	\$22,882,489	\$2,297,009	11%	\$21,481,889	\$896,409
2011-12	\$21,525,318	\$22,503,014	\$977,696	5%	\$19,641,207	(\$1,884,111)

Even though the State aid the District actually received was an average of \$652,164 less than the SED estimates, the District still budgeted for far more aid than it received. The 2012-13 budget estimate for State aid was again over-estimated by approximately \$500,000, or 2.5 percent more than the SED figures available in March 2012.

The Board’s adopted budgets also included estimates for interest revenue well above historical results. The estimates for 2010-11 and 2011-12 were more than four times and two times higher than the actual interest earned in each respective prior year.³ (The interest earnings estimate for the 2012-13 budget was \$35,000, much closer to what the District may actually receive.)

Expenditure Estimates — Luckily, the effects of the revenue over-estimates were offset by the over-estimated expenditures that amounted to about \$9 million over the three-year period. The vast majority of this over-estimation, \$7.4 million, was in salaries and benefits, which should be budgeted on established salary schedules and therefore should not have significant variances. However, if these

² The SED notifies school districts every January of the amount of State aid they can expect to receive for the following fiscal year. These figures are then updated and available in March. School district budgets are voted on in May of the same year.

³ The District budgeted \$255,000 in earned interest for 2010-11 after actually receiving \$61,288 the prior year. For 2011-12, the District budgeted \$113,280 after receiving \$55,045 the prior year. The District received \$29,618 in earned interest in 2011-12.

appropriations had been fully expended as approved by the District's voters, and the revenues remained significantly less than budgeted, the fund balance of the general fund could have resulted in a deficit of approximately \$6.5 million. As it stands, the District has almost completely depleted the general fund's unexpended surplus and can no longer rely on it as a source of financing District operations but instead will have to rely on recurring revenues. Moreover, with less fund balance available to absorb unexpected fluctuations, the accuracy of budgeted amounts becomes critical.

While the District kept its property tax increases relatively low,⁴ its continued reliance on fund balance as a financing source diminished its ability to absorb short-term variations in actual revenues and expenditures, protect against risks and other potential budget shortfalls, and ensure a consistent cash flow for paying bills.

Recommendations

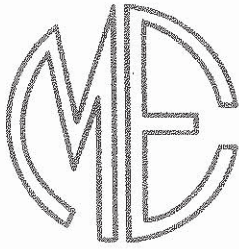
1. District officials should reduce reliance on fund balance as a financing source and evaluate recurring revenue sources over which they have direct control to fund appropriations.
2. District officials should develop budgets that are based on sound estimates of revenues and appropriations, using all available data including:
 - Employment contract costs
 - State aid estimates from the SED
 - Current interest rates
 - Historical trends.

⁴The District's real property tax levy increased 2.2 percent annually for fiscal years 2009-10 through 2011-12 while surrounding districts' levies increased an average of 4 percent annually during the same period.

APPENDIX A

RESPONSE FROM DISTRICT OFFICIALS

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



MAINE-ENDWELL CENTRAL SCHOOL DISTRICT

ADMINISTRATIVE OFFICE
712 Farm to Market Road
Endwell, New York 13760-1199
(607) 754-1400 Fax (607) 754-1650

May 10, 2013

Mr. H. Todd Eames, Chief Examiner
Office of the State Comptroller
State Office Building, Room 1702
44 Hawley Street
Binghamton, New York 13901-4417

Dear Mr. Eames:

Please accept this letter as the Maine-Endwell Central School District's official audit response letter for the Financial Condition: Report of Examination for the Maine-Endwell Central School District for the period of July 1, 2011 through January 3, 2013. The draft audit report has been reviewed by all members of the Board of Education, Assistant Superintendent, Mr. Jeff L'Amoreaux, and Superintendent, Mr. Jason R. Van Fossen.

The District agrees with the findings of the report and will explain the process used by the District which led to structural deficits. Additionally, the District has taken multiple steps – prior to the audit report – to improve our overall financial condition, and, more specifically, the budgeting process as cited in this report. Beginning in July of 2012, the District began utilizing the BOCES Central Business Office (CBO) service, utilizing their expertise in financial and budget planning and oversight. CBO conducted an extensive review of our budgeting process and helped identify, oversee, and implement a comprehensive plan for eliminating our structural deficit and restoring fund balance to healthy levels. We are currently finalizing our 2013-2014 budget and anticipate a return to financial health within a year.

KEY FINDINGS:

The audit report has identified two substantial areas of focus: Use of Fund Balance and Revenue and Expenditure estimates. The District has used fund balance over the past three years to offset significant increases in employee costs (e.g. health insurance, pension, and salary increases). The District, with the help of CBO, has implemented

processes to correct the structural deficit including zero-based budgeting, detailed state-aid analysis, daily cash-flow analysis, detailed health insurance employee cost analysis, and improved employee verifications. These processes have been fully implemented in the development of the 2013-2014 budget.

HISTORICAL PERSPECTIVE: October 2009 OSC Audit of Maine-Endwell

The most recent audit report of the District began in December 2008 and concluded in September 2009. The report was issued in October of 2009 and cited the District as “underestimating its fund balance and reserves by \$6.7 million”. The report also stated “the District could use [excess reserves] to benefit the tax payers”. The front page of the Binghamton Press & Sun-Bulletin ran the story title; *State: M-E made a \$6.7M error*. As one can imagine, this headline and article created much negative criticism and distrust of the District by community members.

The 2009 report does not tell the District how much fund balance to use. However, it explicitly implies the District should use fund balance to positively impact tax payers – e.g. use to reduce tax levy. The District, facing multiple financial variables largely outside its control (e.g. significant decreases in state aid and increases of employee costs), and pressure from the community to utilize these “excess” funds chose to appropriate significant fund balance to (1) offset rising costs, (2) stave off layoffs as long as possible, and (3) ease the mind of tax payers that fund balance was being utilized to benefit the tax payer. Ultimately, the District made the conscious decision to appropriate significant fund balance both to keep student programs intact, and, to address the community expectation of a lower tax levy.

See
Note 1
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FUND BALANCE USE:

The District made a conscious decision to utilize fund balance to “maintain the same level of programs and services while keeping the tax levy as low as possible”. The District was able to stave off instructional layoffs until the 2012-2013 and 2013-2014 budgets using this approach while other local school districts made substantial layoffs years earlier. The District made these decisions with the sole intent of maintaining student programs until conditions improved. The District realizes that reliance on appropriated fund balance as a revenue source without appropriate reductions on the expenditure side is a recipe for financial distress. However, the District did have a rationale behind the conscious decision to use appropriated fund balance.

ESTIMATIONS:

We recognize that expenditure and revenue estimates should be based on sound data and will utilize and focus on all available data including employee contract costs, state aid estimations from SED, current interests rates, and historical trends. For the 2013-2014 budget, we have employed a zero-based budget model to identify costs associated with materials and supplies, equipment, contracted services, and

technology. This approach will give us a baseline for determining actual needs throughout the District and will be employed in subsequent years.

SUMMARY:

The District takes the findings of this report seriously. We have been proactive in addressing and fixing the structural issues regarding reliance on fund balance use. Furthermore, the move to BOCES Central Business Office (CBO) has significantly improved our budgeting processes. The 2013-2014 budget will be our baseline moving forward. The District, with the help of CBO, has implemented processes to eliminate the structural deficit including zero-based budgeting, detailed state-aid analysis, daily cash-flow analysis, detailed health insurance employee cost analysis, and improved employee verifications. We believe the District has improved its financial condition and budgeting processes responsibly, and, in line with the findings of this report.

Very Sincerely,

Alan F. Ewing,
President of the Board of Education
Maine-Endwell Central School District

APPENDIX B

OSC COMMENT ON THE DISTRICT'S RESPONSE

Note 1

We reported in 2009⁵ that the District had over \$5.3 million in unreserved fund balance available, or 12.8 percent of the ensuing year's appropriations (more than three times the amount allowed by SED regulations). Reducing the tax levy was just one of several options suggested in our recommendation that District officials use the surplus fund balance to benefit District taxpayers; as stated, such uses "could include, but are not limited to, increasing necessary reserves, paying off debt, financing one-time expenditures, or reducing District property taxes." Realistic budgeting from year to year, based on historical results and other available information, can help the District reach and maintain a reasonable level of fund balance that is neither excessive nor dangerously depleted.

⁵ *Maine-Endwell Central School District – Internal Controls Over Selected Financial Activities* (Report No. 2009M-120)

APPENDIX C

AUDIT METHODOLOGY AND STANDARDS

Our overall goal was to assess the financial condition of the District. To accomplish the objectives of our audit we performed the following steps:

- We interviewed officials to gain an understanding of the District’s budgeting process.
- We reviewed the results of operations and analyzed changes in fund balance for the general fund. To gain additional background information and perspective, we also reviewed financial data from fiscal years prior to the audit scope period.
- We compared the adopted budgets to the modified budgets and actual operating results for both revenues and appropriations to determine if the budget assumptions were reasonable.
- We analyzed general fund receivables including those from other funds and the State and Federal governments to determine the likelihood of collection and availability to finance operations.
- We analyzed the composition of revenue sources to identify trends.
- We reviewed expenditures based on the District’s budget categories to identify significant expenditures and analyze trends.
- We reviewed the real property tax revenue budgets to determine what property tax increases the Board implemented during our scope period. We compared these increases to those of the component districts in the Broome-Tioga BOCES.
- We tested the reliability of the data reported on the ST-3 and the independently audited financial statements by comparing to accounting records and to each other.

We conducted this performance audit in accordance with generally accepted government auditing standards (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 objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

APPENDIX D

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