



Gouverneur Central School District Financial Management

Report of Examination

Period Covered:

July 1, 2014 – May 31, 2016

2016M-351



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

November 2016

Dear School District Officials:

A top priority of the Office of the State Comptroller is to help school district officials manage their districts efficiently and effectively and, by so doing, provide accountability for tax dollars spent to support district operations. The Comptroller oversees the fiscal affairs of districts statewide, as well as districts' compliance with relevant statutes and observance of good business practices. This fiscal oversight is accomplished, in part, through our audits, which identify opportunities for improving district operations and Board of Education governance. Audits also can identify strategies to reduce district costs and to strengthen controls intended to safeguard district assets.

Following is a report of our audit of the Gouverneur 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 Gouverneur Central School District (District) is located in the Town of Antwerp in Jefferson County and the Towns of DeKalb, Edwards, Fowler, Gouverneur, Hermon, Macomb, Pitcarin and Rossie in St. Lawrence County. The District is governed by the Board of Education (Board), which is composed of nine elected members. The Board is responsible for the general management and control of the District's financial and educational affairs. The Superintendent of Schools (Superintendent) is the District's chief executive officer and is responsible, along with the Business Manager and other administrative staff, for the District's day-to-day management under the Board's direction.

The District operates three schools with approximately 1,600 students and over 300 employees. The District's budgeted appropriations for the 2015-16 fiscal year totaled \$34.3 million and were funded primarily with State aid and real property taxes.

Objective

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

- Did the Board adopt reasonable budgets and adequately manage the District's financial condition?

Scope and Methodology

We examined the District's financial condition for the period July 1, 2014 through May 31, 2016. We extended our audit scope back to July 1, 2012 to analyze financial trends in prior years.

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

Comments of District Officials and Corrective Action

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

The Board has the responsibility to initiate corrective action. Pursuant to Section 35 of General Municipal Law, Section 2116-a (3)(c) of New York State Education Law and Section 170.12 of the Regulations of the Commissioner of Education, a written corrective action plan (CAP) that addresses the findings and recommendations

in this report must be prepared and provided to our office within 90 days, with a copy forwarded to the Commissioner of Education. To the extent practicable, implementation of the CAP must begin by the end of the next fiscal year. For more information on preparing and filing your CAP, please refer to our brochure, *Responding to an OSC Audit Report*, which you received with the draft audit report. The Board should make the CAP available for public review in the District Clerk's office.

Financial Management

The Board and District officials are responsible for effectively planning and managing the District's financial operations. One of the most important tools for managing the District's finances is the budget process. The Board should adopt structurally balanced budgets in which recurring revenues finance recurring expenditures and reasonable levels of fund balance are maintained. In addition, the Board should develop multiyear plans to allow it to set long-term priorities and work toward specific goals.

The Board consistently overestimated general fund appropriations by an annual average of \$3.2 million, or 10.8 percent, from fiscal years 2012-13 through 2014-15. This resulted in most of the fund balance appropriated in the general fund not being used to finance operations. The District's reported unrestricted fund balance has exceeded the 4 percent statutory limit in two out of the last three fiscal years. When the unused appropriated fund balance is added back, the recalculated unrestricted fund balance has averaged over 16 percent of the ensuing year's appropriations, or about four times the statutory limit, for fiscal years 2012-13 through 2014-15. Also, fund balances reported in the school lunch fund exceeded the maximum amount allowed by federal regulations by an average of 43 percent in 2013-14 and 2014-15. Lastly, the Board did not develop a formal multiyear financial or capital plan to help identify developing revenue and expenditure trends and set long-term priorities and goals.

General Fund

The Board is responsible for estimating what the District will spend and what it will receive in revenue, estimating how much fund balance will be available at fiscal year-end and determining what the expected tax levy will be. Accurate budget estimates help ensure the tax levy is not greater than necessary. Budgets should be based on prior years' operating results, past expenditure trends and anticipated future needs.

Fund balance represents resources remaining from prior fiscal years that can be used to finance the next year's budget or set aside in reserve funds for specific purposes. The Board may retain a portion of fund balance for unexpected events and maintaining cash flow but must do so within statutory limits. Currently, the New York State Real Property Tax Law (RPTL) limits the amount of unrestricted fund balance that a school district can retain to no more than 4 percent of the subsequent year's budget.

When fund balance is appropriated in the budget, the expectation is that there will be an operating deficit (budgeted expenditures exceeding budgeted revenues), financed by the appropriated fund balance. This allows a school district to use excess fund balance that it accumulated in prior years. Sound budgeting practices provide that adopted annual budgets should not routinely appropriate significant amounts of fund balance that will not actually be needed.

The Board and District officials overestimated appropriations when developing the budgets for the three fiscal years 2012-13 through 2014-15. We compared the District's general fund budgeted revenues and expenditures with actual results of operations for this period. While revenue estimates appeared reasonable and were generally close to the actual revenues received, expenditure estimates exceeded actual expenditures by an average of \$3.2 million or 10.8 percent over the three-year period.

Figure 1: Overestimated Appropriations

Fiscal Year	Appropriations	Actual Expenditures	Overestimated Appropriations	Percentage Overestimated
2012-13	\$31,372,044	\$28,001,469	\$3,370,575	12%
2013-14	\$32,598,193	\$29,247,883	\$3,350,310	11.5%
2014-15	\$33,723,438	\$30,956,065	\$2,767,373	8.9%
Average	\$32,564,558	\$29,401,806	\$3,162,752	10.8%

The majority of the budget variances during this three-year period was due to overestimates related to special education by \$2,305,810 (62 percent), health insurance by \$698,913 (16 percent), building utility costs (i.e., natural gas and electricity) by \$313,647 (89 percent), diesel fuel for transportation by \$127,156 (49 percent) and other union benefits by \$32,499 (144 percent). The Business Manager and Board President told us that these overestimates often serve to offset potential expenditure increases that may occur after the budget is adopted. While we acknowledge that some expenditures are often more difficult than others to accurately estimate, some of the Board's overestimates were preventable. For example, the District budgeted \$20,000 each year for interest payments on revenue anticipation notes (RANs), yet the District had not needed to issue RANs for at least the past five years.

District officials appropriated \$14.5 million of fund balance in the 2012-13 through 2014-15 budgets (about \$4.8 million each year), which should have resulted in operating deficits each year and a reduction in year-end fund balance. However, due largely to the overestimation of appropriations, the District generated much smaller

operating deficits than budgeted in fiscal years 2013-14 and 2014-15, and it generated an operating surplus in 2012-13 (Figure 2). As a result, the District did not use 92 percent of its appropriated fund balance.

Figure 2: Unrestricted Fund Balance at Year-End

	2012-13	2013-14	2014-15
Total Beginning Fund Balance ^a	\$11,389,955	\$11,430,918	\$11,194,736
Plus: Operating Surplus/(Deficit) ^b	\$40,945	(\$236,181)	(\$874,658)
Total Ending Fund Balance	\$11,430,900	\$11,194,737	\$10,320,078
Less: Restricted Fund Balance ^c	\$4,568,371	\$5,597,211	\$4,878,099
Less: Appropriated Fund Balance for the Ensuing Year ^d	\$4,399,336	\$4,149,460	\$3,445,636
Less: Encumbrances	\$196,327	\$154,529	\$74,770
Unrestricted Fund Balance at Year-End	\$2,266,866	\$1,293,537	\$1,921,573
Ensuing Year's Budgets	\$32,598,193	\$33,723,438	\$34,372,530
Unrestricted Fund Balance as a Percentage of Ensuing Year's Budgets	7.0%	3.8%	5.6%
^a Includes prior period adjustments and other minor adjustments ^b Includes interfund transfers ^c Consists of the following reserves: workers' compensation, unemployment insurance, retirement contribution, property loss, liability, insurance, tax certiorari, employee benefit accrued liability, capital and debt ^d \$5,969,975 was appropriated in 2011-12 for the 2012-13 fiscal year.			

The District has reported year-end unrestricted fund balance in excess of the 4 percent statutory limit in two of the last three completed fiscal years. In addition, the District's practice of consistently appropriating significantly more fund balance than needed is, in effect, a reservation of fund balance that is not provided for by statute and a circumvention of the 4 percent statutory limit. When unused appropriated fund balance is added back, the District's recalculated unrestricted fund balance at the end of the 2012-13 and 2013-14 fiscal years exceeded the legal limit by 16 and 10 percentage points, respectively.

During 2014-15, the District appropriated about \$3.4 million for the 2015-16 budget. Based on the District's 2015-16 projected year-end operating results, we estimate that the District will generate an operating surplus and will not need to use any of the appropriated fund balance. As a result, the District's recalculated unrestricted fund balance was likely four times the legal limit at the end of 2014-15 (Figure 3).

Figure 3: Unused Fund Balance

	2012-13	2013-14	2014-15
Total Unrestricted Funds at Year-End	\$2,266,866	\$1,293,537	\$1,921,573
Add: Appropriated Fund Balance Not Used To Fund Ensuing Year's Budget	\$4,163,155	\$3,274,802	\$3,445,636
Total Recalculated Unrestricted Funds	\$6,430,021	\$4,568,339	\$5,367,209
Recalculated Unrestricted Funds as Percentage of Ensuing Year's Budget	20%	14%	16%

The District tax levy increased from \$5.22 million in 2012-13 to \$5.66 million for the 2015-16 fiscal year, an increase of approximately \$440,000, or 8.4 percent. These increases may not have been necessary if the Board had used more realistic budget estimates.

Based on our review of the District's 2016-17 adopted budget, the Board has reduced the amounts appropriated for some of the budget items it has overestimated in previous years. However, it continues to overestimate others, including special education, union benefits and RAN interest. The Board reduced the amount of appropriated fund balance in the 2016-17 budget by approximately \$820,000 to \$2.62 million. However, it is likely most of this will not be needed to finance operations based on the continued practice of overestimating expenditures.

School Lunch Fund

According to New York State Education Department (SED) guidelines, the school lunch fund's budgeted appropriations must balance with its estimated revenues. Its budget is not submitted to District residents for approval. Only the budgeted subsidy, if any, from the general fund requires voter approval. The school lunch fund may be charged for direct program costs, such as food purchases, food service workers' salaries and benefits and, to the extent funds are available, indirect costs such as utilities and custodial and administrative expenditures.¹ Federal regulations limit the allowable school lunch fund balance to three months' average operating expenditures.

The fund balance in the school lunch fund has increased approximately \$114,300, or 50 percent, from the beginning of 2012-13 to the end of 2014-15.

¹ The indirect cost allocation must be approved by SED.

Figure 4: School Lunch Fund Results of Operations

	2012-13	2013-14	2014-15
Beginning Fund Balance	\$227,115	\$248,400	\$322,828
Revenues	\$715,476	\$725,364	\$712,921
Expenditures	\$694,191	\$650,936	\$694,375
Operating Surplus	\$21,285	\$74,428	\$18,546
Ending Fund Balance	\$248,400	\$322,828	\$341,374

Each fiscal year, SED calculates the District's three months' average expenditure level and compares it to fund balance in the lunch fund. If SED identifies an excess fund balance in the fund, it requests the District to submit a plan to address the excess fund balance and provides the District with acceptable means of reducing the excess.² Districts can also choose to accumulate excess funds for major equipment purchases or for pending contract settlements.

District officials received letters from SED in June 2015 and 2016 informing them that the fund balance for 2013-14 and 2014-15 was in excess of the three-month average expenditure level allowed by federal regulations. We reviewed and recalculated the three months of average expenditures and found fund balance was in excess of the allowable limit for 2013-14 by \$80,417 (41 percent) and for 2014-15 by \$95,316 (46 percent).³

The District responded in July 2015 with a plan to address the excess fund balance for 2013-14, and SED approved the plan.⁴ The plan identified various cafeteria equipment purchases that District officials planned to make from 2014-15 through 2016-17, which they expected would reduce the excess fund balance. However, some of the planned equipment expenditures in 2014-15 and 2015-16 were partially offset by grants or paid out of other funds, so they did not result in the reduction of the school lunch fund balance that District officials had anticipated.

² Includes improvements in equipment for the cafeteria, meal enhancement, marketing and merchandising to promote meal programs and capital improvements that directly relate to the lunch program.

³ SED adjusts fund balance by the amount of federal reimbursement surplus food accrued revenues when calculating the amount of excess fund balance at year-end.

⁴ In August 2016, the District also submitted a plan to SED to address the excess fund balance at the end of 2014-15. It identified various cafeteria equipment purchases the District plans to make in 2016-17 and salaries of cafeteria monitors to be paid from the school lunch fund beginning September 2016. SED had not approved this plan at the time of our fieldwork.

The District's preliminary results of operations for the 2015-16 fiscal year indicate the school lunch fund will incur an operating deficit of approximately \$12,000, which will decrease fund balance to about \$329,000. The fund balance is projected to remain approximately \$72,000 in excess of the federal limit at the close of 2015-16. However, the school lunch fund encumbered approximately \$35,000 for the cost for ovens and dishwashers at the end of the 2015-16 year.⁵ The District also recently received SED approval for the first phase of a planned capital project for its cafeterias and plans to use fund balance to fund the equipment purchases that are part of the project.

In addition, the Business Manager told us that all trash removal and utility costs,⁶ as well as the lunch fund manager's salary and benefits, are being paid out of the general fund. The school lunch fund's share of these costs, net of aid received,⁷ is approximately \$34,000 annually. If the District's equipment purchases do not reduce the school lunch fund balance to within the federal limit, the Board and District officials should consider requesting SED's approval to allocate these costs to the school lunch fund to reduce the excess fund balance.

Multiyear Planning

Planning on a multiyear basis enables the Board 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. It also allows the Board to assess the merits of alternative approaches (such as appropriating fund balance or establishing and using reserves) to finance operations and capital needs. Any long-term financial plan must be monitored and updated on a continuing basis to provide a reliable framework for preparing budgets and to ensure that information used to guide decisions is current and accurate.

The Board has not developed a formal multiyear financial or capital plan to define how reserves and unrestricted fund balance in the general fund will be used. Board members told us that the Board often discusses long-term planning but has not developed a written plan.

Board members told us they received voter approval in May 2016 to establish a separate capital reserve fund in the general fund for up to a maximum of \$1.5 million to purchase three buses annually over the next five years. The District also received voter approval to fund a \$1 million building capital reserve to use for building renovations based

⁵ We reviewed the purchase orders and related supporting documentation for these purchases.

⁶ Electricity and natural gas

⁷ The District shares the position of lunch fund manager with another local school district and receives Board of Cooperative Educational Services (BOCES) aid for the position. The District should subtract the BOCES aid when determining the net cost of the salary and benefits to allocate to the school lunch fund.

on a recent building condition survey. Currently, there is a capital project underway to make modifications to the District's elementary schools and add and demolish sections of the middle school.

As the District moves forward, a formal, well designed long-term plan can assist the Board in making timely and informed decisions about the District's programs and operations and help manage the fund balances in the general and school lunch funds.

Recommendations

The Board should:

1. Develop realistic estimates of appropriations and the use of fund balance in the annual budget.
2. Ensure that the amount of the District's unrestricted fund balance is in compliance with statutory limits.
3. Use surplus funds as a financing source for:
 - Funding one-time expenditures;
 - Funding needed reserves; and
 - Reducing District property taxes.
4. Consider requesting SED approval to allocate indirect costs to the school lunch fund to reduce the excess fund balance and adhere to federal regulations.
5. Develop a comprehensive multiyear financial plan to establish long-term objectives for funding long-term needs, provide a framework for future budgets and guide the District's management of financial condition. This plan should be periodically reviewed and updated as appropriate.

APPENDIX A

RESPONSE FROM DISTRICT OFFICIALS

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

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November 8, 2016

Ms. Rebecca Wilcox, Chief Examiner
Office of the State Comptroller
Syracuse Regional Office
State Office building, Room 409
333 E. Washington Street
Syracuse, NY 13202-1428

Dear Ms Wilcox,

Gouverneur CSD is in receipt of the Draft Financial Management Report of Examination for the period July 1, 2014 through May 31, 2016.

Our Board of Education and the District's administration would like to thank the local field staff of the Comptroller's Office for the professional and courteous method in which they conducted their duties while performing the audit.

As a district, we are pleased that the audit showed no findings of improprieties, waste, fraud or abuse. Please allow this letter to serve as the District's response and Corrective Action Plan to the audit findings.

Audit Recommendations:

1. Develop realistic estimates of appropriations and the use of fund balance in the annual budget.
2. Ensure that the amount of the District's unrestricted fund balance is in compliance with statutory limits.
3. Use surplus funds as a financing source for funding one-time expenditures; funding needed reserves; and reducing District property taxes.

While the District does not dispute the findings of the report, we feel that the report shows an incomplete picture of the District's budget practices. The District has prepared budgets guided by two fundamental principles. The first is to provide quality educational programs for our District's children. The second is to be fiscally responsible to our community by providing budget and tax rate stability over time. We agree that sound budgeting, along with managing of fund balance and reserves, supports the District's goals to maintain high quality educational programs, manage emergencies, address unexpected expenses, and satisfy long term financial obligations. The District faces many unknown factors when projecting expenditures at the time of budget development. We acknowledge that during the period reviewed the appropriated fund balance was not fully utilized, however we continue to stand by our budgeting practices and cannot commit to the use of appropriated fund balance in its entirety. Future budgets will continue to be planned to utilize a portion of the appropriated fund balance, however the District must look forward when developing the budget and cannot always anticipate when key elements of the budget will increase or decrease. The District must be prepared to cover any and all expenses.

As cited in your report, the District's budget variances during this three-year period were due to overestimates related to Special Education; health insurance; building utility costs; diesel fuel; and other

union benefits.

- Special Education costs are difficult to project. The movement of students in and out of the District is very volatile and beyond our control. The District is required by law to provide the services to the student with a disability per their Individualized Education Plan. We budget for the possibility of additional students coming to the District; the need for additional services; and the possibility of residential placements.
- During the three-year period reviewed for this audit, the District negotiated successfully with all unions to change all employees' health insurance plan. The District's transition to the new plan, a less expensive plan, happened over two fiscal years. The health insurance budget was developed with contract language that changed the benefit costs during the multiple fiscal years and this resulted in a positive budget variance.
- The District has been reducing the budget for building utility costs over multiple years. The District has benefitted from "easier" winters which factor into actual costs. The District also invested in lighting upgrades to reduce usage and therefore reducing costs. In addition, the District closed and sold one elementary school.
- The District renegotiated the transportation contract which went into effect for the 2014-15 budget. The District did not accept the first bids and re-bid the contract. The contract was written for double trips instead of single trips. A budget assumption was to double the annual number of gallons purchased due to the double bus runs. This did not occur and resulted in a positive budget variance. The diesel budget has been decreased with data from multiple years to support the reduction. This fiscal decision could only be made with data from multiple years.
- The other union benefits are for the contractual obligation to pay a specified amount for each accrued sick day to a 403(b) account on behalf of the retiring employee. The employee is eligible for this benefit if they provide the District a letter of resignation for purposes of retiring nine months prior to their retirement date. This means, the District is provided this information by September 30th of each year. The District has developed and the voters have approved the budget in May. The District must budget a reasonable amount of funds using the assumption that all eligible employees may retire.

Gouverneur CSD agrees with the recommendation of the audit to work diligently towards reducing the unappropriated fund balance to ensure compliance with statutory limits. The 4% level in statute is becoming more difficult to attain and meet all cash flow requirements until property taxes and state aid is received in September.

The uncertainty of the District's annual allocation of state aid and the state's imposed adjustments (GEA) has created a volatile economic climate for the District. Therefore, the District has chosen to continue to raise taxes annually to provide a stable tax rate for our taxpayers and maintain a consistent percentage of property tax revenue compared to total revenue. The District's tax rate per \$1,000 of assessed value is the third lowest in St. Lawrence County. Our community has been very supportive of the District and the educational programs.

Corrective Action Plan:

We believe it is important to note that annual school budget development is based on prior years' operating results, past expenditure trends, anticipated future needs and available information at the time the budget is developed. Responsible budgeting requires that a District build contingencies for unanticipated expenditures. As such it has, and will continue, the practice of conservatively estimating certain expenditures over which the District has little or no control, such as Special Education and Transportation.

Implementation Date:

December 2016

Corrective Action Plan:

The District will continue to appropriate fund balance to reduce the amount required to be raised via the tax levy. The District will review the fund balance levels during the development of the 2017-18 budget to determine their appropriateness and, if necessary, adjust accordingly.

Implementation Date:

January 2017

Corrective Action Plan:

The District will review reserve balances and future needs to determine funding levels and opportunities for funding one-time expenditures with surplus funds.

Implementation Date:

January 2017

Audit Recommendations:

4. Consider requested SED approval to allocate indirect costs to the school lunch fund to reduce the excess fund balance and adhere to federal regulations.

Corrective Action Plan:

The District has contacted NYS Child Nutrition asking for information and approval about allocating indirect costs to the School Lunch Fund.

Implementation Date:

November 2016

Audit Recommendations:

5. Develop a comprehensive multiyear financial plan to establish long-term objectives for funding long-term needs, provide a framework for future budgets and guide the District's management of financial condition. This plan should be periodically reviewed and updated as appropriate.

Corrective Action Plan:

The District is currently developing a multi-year financial plan. The plan will include use of fund balance. The development of the plan is difficult due to the uncertainty of state aid, our largest revenue source. This makes a multiyear operational spending plan merely a best guess based on assumptions.

Implementation Date:

January 2017

In conclusion, Gouverneur CSD appreciates the work of the Comptroller's Office and the opportunity to respond to the written report. We are constantly looking for ways to strengthen our District.

Sincerely,

Lisa Dunkelberg, President
Gouverneur CSD Board President

APPENDIX B

AUDIT METHODOLOGY AND STANDARDS

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

- We interviewed District officials to gain an understanding of the budget process and to determine whether the District adopted multiyear financial plans. We reviewed the Board minutes to determine the reports provided to the Board and reviewed the financial information provided to the Board.
- We reviewed the results of operations for the general and school lunch funds for fiscal years 2012-13 through 2014-15.
- We compared the budgeted revenues and expenditures to the actual revenues and expenditures for the general fund for fiscal years 2012-13 through 2014-15 and identified any budget categories with significant variances. We also analyzed direct and indirect lunch fund costs being paid from the general and school lunch funds.
- We reviewed the 2015-16 budget and compared it to the 2014-15 budget. We projected revenues and expenditure trends for the remainder of the 2015-16 fiscal year for the general fund.
- We analyzed the trend in total fund balance, including the use of reserves in the general fund for the fiscal years 2012-13 through 2014-15. We also compared the unrestricted fund balance to the ensuing year's budgeted expenditures to determine if the District was within the statutory limitation during these same fiscal years.
- We calculated excess fund balance in the school lunch fund for 2013-14 through 2015-16 using SED guidelines with actual and projected results of operation.

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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