Office of the New York State Comptroller

Division of Local Government & School Accountability

Lansing Central School District

Financial Management

Report of Examination

Period Covered:

July 1, 2014 — September 9, 2015

2015M-256

Thomas P. DiNapoli

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State of New York
Office of the State Comptroller

**Division of Local Government
and School Accountability**

January 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 Lansing 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 Lansing School District (District) is located in the Towns of Dryden, Groton and Lansing in Tompkins County. The District is governed by the Board of Education (Board), which is composed 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 District's chief executive office responsible, along with the Business Administrator, for the day-to-day management under the Board's direction.

The District operates three schools with approximately 1,200 students and 360 employees. The District's budgeted appropriations for the 2015-16 fiscal year are $28.4 million, which are funded primarily with State aid, real property taxes and grants.

Objective

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

- Did District officials properly manage fund balance and ensure budget estimates and reserves were reasonable?

Scope and Methodology

We examined the District's general fund financial records for the period July 1, 2014 through September 9, 2015. We extended our scope period back to July 1, 2012 to examine the District's fund balance and budgeting practices to provide additional information for perspective and background.

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 C of this report. Unless otherwise indicated in this report, samples for testing were selected based on professional judgment, as it was not the intent to project the results onto the entire population. Where applicable, information is presented concerning the value and/or size of the relevant population and the sample selected for examination.

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 disagreed with certain aspects of our findings and recommendations in our report but indicated that they planned to implement some of our recommendations. Appendix B includes our comments on the issues raised in the District's response letter.

The Board has the responsibility to initiate corrective action. Pursuant to Section 35 of 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

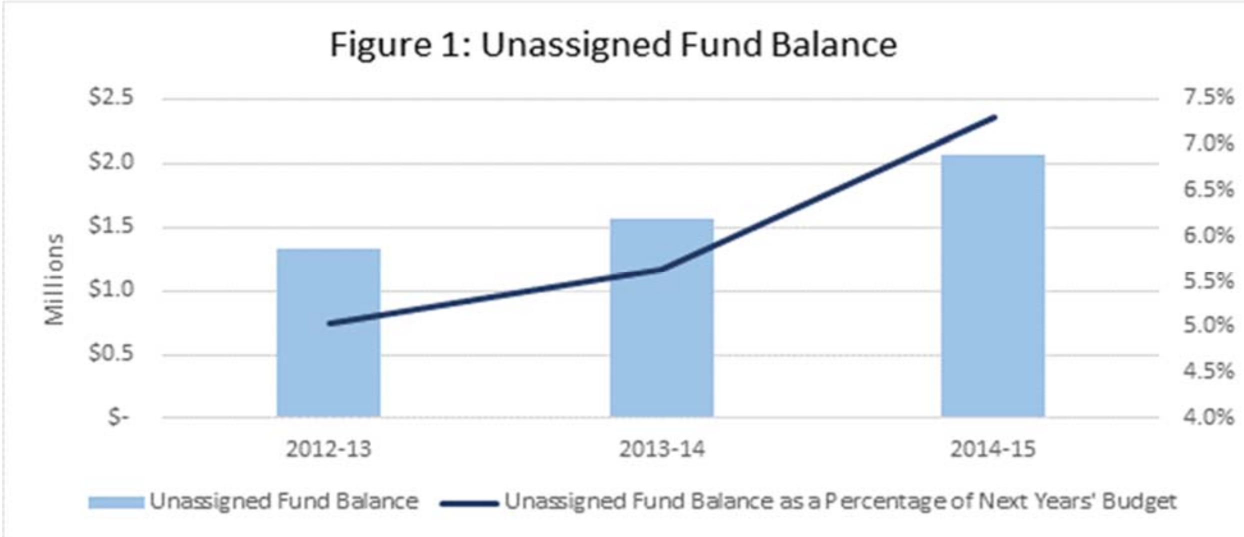
A school district's financial condition is a factor in determining its ability to fund public educational services for students within the district. District officials are responsible for managing fund balance, which represents resources remaining from prior fiscal years. A district may retain a portion of fund balance within the limits established by New York State Real Property Tax Law (RPTL). A district can also establish reserves to restrict a reasonable portion of fund balance to finance future costs for a variety of specified purposes. District officials should ensure that reserve fund balances do not exceed the amounts necessary to address long-term obligations or planned expenditures. Developing accurate budgets is an effective way to ensure fund balance is reasonable. Accordingly, it is essential that District officials develop reasonable budgets to balance recurring expenditure needs with recurring revenue sources while providing desired services on a continuing basis and manage fund balance responsibly.

While District officials kept taxpayers informed about the level of fund balance through public meetings, budget newsletters and internet video recordings, they did not properly manage fund balance or ensure budget estimates and all reserve fund balances were reasonable. Total fund balance has increased by more than $1 million from 2012-13 through 2014-15 and unassigned fund balance was over 7 percent of the ensuing year's budget as of June 30, 2015, exceeding the statutory limit of 4 percent. Over the past three years, District officials used approximately $1 million of the annual operating surpluses to fund five reserves that, as of June 30, 2015, totaled approximately $2.9 million. While most reserve fund balances were reasonable, one was overfunded. As a result of these practices, District officials may have levied real property taxes that that were higher than necessary to fund District operations.

Unassigned Fund Balance

A district may retain a portion of fund balance, but must do so within the limits established by RPTL. Currently, the amount of unassigned fund balance that the District can retain may not be more than 4 percent of the next fiscal year's budget.

For the 2012-13 through 2014-15 fiscal years, unassigned fund balance increased by $734,000 or 55 percent and exceeded the statutory limit each year, ranging between 5 and 7 percent of the next year's budget. As of June 30, 2015, the District's unassigned fund balance totaled approximately $2 million, or 7 percent of the ensuing year's budget, which exceeded the statutory limit by $937,000.



Reserves

Fund balance may be restricted for particular purposes. Districts should maintain reserve balances that are reasonable. Funding reserves at greater than reasonable levels essentially results in real property tax levies that are higher than necessary.

From 2012-13 through 2014-15, District officials increased reserves by more than $1 million, or 55 percent. As of June 30, 2015, the District had five reserves totaling approximately $2.9 million. We analyzed these reserves for reasonableness and found the funding for the retirement contribution, tax certiorari, compensated absences and capital reserves were reasonable.

However, the amount retained in the reserve for unemployment insurance was significantly more than the amount necessary to pay unemployment insurance claims each year. This reserve's balance as of June 30, 2015 was $195,000. However, the District's unemployment claims totaled approximately $38,000 from 2012-13 through 2014-15, and if these costs continue to average approximately $13,000 a year, the reserve would last for more than 15 years without additional funding. Further, District officials budgeted and paid for unemployment claims from the operating funds instead of using the reserve fund for its intended purpose. Therefore, we question the reasonableness of the amount in this reserve and the need for this reserve at all.

Budgeting Practices

District officials are responsible for preparing and adopting reasonable budgets based on historical or known trends for appropriations and revenues. In preparing the budget, it is essential that District officials use the most current and accurate information available to ensure that budgeted appropriations are reasonable and not overestimated.

We reviewed the District's budgets for the 2012-13 through 2014-15 fiscal years and found District officials planned to incur operating deficits of $4.8 million during these years. However, the District incurred an operating deficit of $711,000 in 2012-13 and operating surpluses aggregating to $1 million from 2013-14 through 2014-15. This occurred because the Board overestimated appropriations each year by an average of more than 4 percent of actual expenditures.

While the variances for each year were small, ranging from 3 to 6 percent, in aggregate they resulted in a 22 percent increase to fund balance over these years. The majority of these variances occurred in the contractual expenditures, which made up 20 percent of total expenditures, and employee benefits, which made up 25 percent of total expenditures each year. These expenditures should be easy to estimate based on historical trends.

District officials told us they are planning for the possible loss of a major business property and the associated revenues,[1] estimated at $1.3 million annually. As a result, District officials may have unnecessarily increased the tax levy. After considering the possibility of losing significant PILOT payments, the Board adopted budgets that increased real property taxes to fund a plan in case the loss actually occurred. The Board adopted budgets with actual tax levy increases of 16 percent or $2.3 million for 2012-13 through 2015-16 because of the potential need for future tax levy increases. In 2014-15 and 2015-16, District officials increased the real property tax levy close to the maximum amount allowed by the statutory limit.[2]

Recommendations

The Board and District officials should:

1. Ensure the amount of unassigned fund balance complies with the statutory limits and reduce the amount of surplus fund balance in a manner that benefits District taxpayers. Such uses could include, but are not limited to:

    - Paying off debt.

    - Financing one-time expenditures.

[1] These revenues are payments in lieu of taxes (PILOTs) made to compensate the District for some or all of the tax revenue that it loses because of the nature of the ownership or use of a particular piece of real property.

[2] The New York State Legislature enacted Chapter 97 of the Laws of 2011, establishing a tax levy limit on all local governments and school districts, which was effective beginning in the 2012 fiscal year. The law precludes school districts from adopting a budget that requires a tax levy that exceeds the prior year tax levy by more than 2 percent or the rate of inflation, whichever is less, and certain exclusions permitted by law, unless at least 60 percent of district voters approve a budget that requires a tax levy that exceeds the statutory limit.

- Funding appropriate reserves.
- Reducing property taxes.

2. Develop more realistic budget appropriations based on prior year's actual results and anticipated operations to avoid raising more real property taxes than necessary.

3. Review all reserve balances and transfer excess funds to fund balance, where allowed by law, or other reserves established and maintained in compliance with statutory directives.

APPENDIX A

RESPONSE FROM DISTRICT OFFICIALS

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

Lansing Central School District

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Lansing, NY 14882
Phone: 607-533-3020 www.lcsd.k12.ny.us Fax: 607-533-3602

December 20, 2015

H. Todd Eames, Chief Examiner
Office of the State Comptroller
State Office Building, Room 1702
44 Hawley Street,
Binghamton, NY 13901

Dear Mr. Eames:

The Lansing Central School District prides itself on its determination to strive toward establishing and maintaining the highest possible ethical standards in its use of taxpayer dollars to support its outstanding educational program. To that end, we also strive for complete transparency in our communications with taxpayers about operations and short and long-term financial planning.

We are in receipt of the Comptroller's audit for the period July 1, 2012 – September 9, 2015, and appreciate the review and input the local office has provided our team relative to our potential for improvement. The representatives of the Comptroller have conducted themselves in a professional yet collaborative manner throughout this process and we embrace the positive relationship that has developed from it.

Please accept the following response to the report:

The most significant charges made by this report are:

1) One reserve fund is overfunded
2) The District's 'unassigned' fund balance is in excess of the 4% currently allowed by NYS Real Property Tax Law.
3) The Board of Education adopted budgets that overestimated actual expenditure needs.

With the exception of the last item, the District does not dispute the essence of these findings. Both the treatment of reserves and the maintenance of fund balance in excess of the 4% are issues that the Board of Education and District management discuss openly at our regularly scheduled, well-attended, and publicly reported meetings. We do have a significant potential liability with our largest taxpayer; one that represents about $1.3 million dollars of tax-rate-based revenue each year. That revenue amount represents about 4.6% of our total (2015-2016) budget (/revenue) and almost 7 % of our tax-rate-based revenue. We have no other legal means by which to save money to alleviate the negative pressures that the loss of this revenue source will bring to both our educational program and the taxpayer. We hope to have a better understanding of the future of this liability with a Public Service Commission action that this community has been waiting for, for several years now.

This audit report ends with the statement, "…District officials increased the real property tax levy close to the maximum amount allowed by the statutory limit." That is an open conversation between the Board, management and taxpayers every year as we try to determine the appropriate use of our fund balance. As long as we have no legal recourse to the liability presented by this $1.3 million PILOT payment, we will continue to ask our taxpayers if they trust us to hold onto the dollars we end the year with (through efficient operations) so that we can apply these dollars if and when we know the future of the power plant. If we lose that revenue, under the Property Tax Cap formula, the District may be able to increase the tax levy by almost 10% and the tax rate by almost 8.5% in a single year with a simple majority vote of the District taxpayers. We believe that this is not an appropriate long-term financial plan. And so every year we put the information to the public, and plan to appropriate only as much as we may need to meet our projected budget while increasing the tax levy to the amount allowed under the law. If the question of the power plant settles in its favor, we can plan to return those excess funds over the course of time by keeping the tax levy low in the face of increasing costs. We have presented information at our Board of Education meetings that shows a potential term of how all of the District's 'savings' might be 'returned' to the tax base in the event of the loss of the PILOT. Logically, we would follow a similar path to return the funds in excess in the event of an assurance of the power plant's ongoing operation. Naturally any such conversation would include other long-term pressures on the District, not the least of which would be facilities improvements needs.

See Note 1 Page 12

Regarding the last item, the District respectfully maintains that the Comptroller's representatives did not sufficiently investigate the methods used to build the budget for them to be able to make this judgment against these methods. For example, the representative insisted that since the District had underspent its instructional salaries by $600,000 (more precisely, $573,671), which represented about 4.86% of the total budget for these codes, ergo it must be engaged in inappropriately budgeting for these codes. Once the representative was presented with an analysis of every employee salary that was budgeted in this category, the unexpected changes to these budgeted amounts (late-notice retirements, unpaid absences, breakage from other transient employee activity) that occurred during the operations of the fiscal year, this item was dropped from the Comptroller's final report. Despite the explanation that employee benefits are calculated as budget items based on the same wage projections noted previously, they are cited in the report as a flaw in budgeting practice because they were underspent. And yet if the amount budgeted is based on the contractual obligations of the District for the 'shoes on the ground' during the budget planning, then it only stands to reason that the attached benefits (pensions, FICA, worker's comp), would also be budgeted thus. And if the actual experience comes in shy of the budgeted amount on the salaries due to the variations cited above, then too should the benefits attached to those wages vary.

See Note 2 Page 12

The Comptroller's audit report cited variations in budgeted versus actual results in contractual codes, but did not take the time to analyze the reasons for these variations. We are proud of the impact we have seen related to our ongoing energy conservation measures (significant relative amounts in the contractual object codes, and something that you cannot typically predict the savings impact, but rather have to experience it). In fact, we have been reducing these budget amounts, but we continue to engage in behavioral changes to bring about more savings each year. We also saw significant variations in 14/15 of our BOCES expenditures related to Special Education, which is potentially a highly variable area, depending on the transient nature of the students involved, and for which the District experienced something close to a 30% 'savings' from budgeted amount to actual amount, primarily related to the loss of a high-needs student. Even the Administrative portion of the BOCES budget was realized at around 7% less than the budgeted amount, and the District has no control over the projected amount nor actualized amount in the BOCES budget.

See Note 3 Page 12

In short, the Comptroller's analysis of budget variations fell short of anything that might be considered thorough. Instead, the audit makes sweeping generalizations, indicating that the budget-building process must be flawed, or worse, a calculated exaggeration of projected costs, which is simply not true. In fact, those things that can be calculated in the budget process, like salaries and related benefit costs, BOCES, requests from instructional staff for materials, conferences, and other needs, are calculated (zero-based budgeting). And those things that are better budgeted by historical trend analysis, like energy costs and transportation costs, are budgeted in that manner. A thorough analysis of the details and process would have shown that this District is in fact budgeting according to best practices. What the audit fails to recognize is that we experience variations in labor supply and related costs similar to any other industry, and that we operate every day in a manner that seeks savings for the taxpayers regardless of what appropriately budgeted projections might have indicated we would spend. We don't "just spend the budget". We operate striving to spend less where and when we are able to do so without jeopardizing the educational program our community has supported.

Despite our stated disagreement with some aspects of the report, we continue to operate on the belief that all audits are an opportunity for learning and growth, and we do embrace this particular experience in that vein. We are pleased that there are no citations of internal controls and that there were no findings of fraud.

We respectfully submit this response to the audit. Thank you for affording us this opportunity to improve on our performance of the important work that we do.

Sincerely,

Chris Pettograsso
Superintendent of Schools

APPENDIX B

OSC COMMENTS ON THE DISTRICT'S RESPONSE

Note 1

Assessing the District's budget building process was not an objective of our audit.

Note 2

Instructional salaries were not included in our report. However, the instructional salaries variance cited by District officials occurred in 2014-15, while the employee benefits variances totaling $1.9 million occurred from 2012-13 through 2014-15.

Note 3

District officials overestimated the contractual expenditures from 2012-13 through 2014-15 by an average of 8 percent each year.

APPENDIX C

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 their fund balance management policies.

- We reviewed the total fund balance and reserve fund balances to determine the trends from 2012-13 through 2014-15.

- We compared the fund balance for 2012-13 through 2014-15 to the next year's appropriations to determine if the limits established by the RPTL were complied with.

- We compared the reserve fund balances as of June 30, 2015 to the average annual expenditures from 2012-13 through 2014-15 or other supporting documentation to determine if the balances were reasonable.

- We calculated the results of operations for 2012-13 through 2014-15 and compared our results with the amount of appropriated fund balance to determine the amount of appropriated fund balance used to finance operations.

- We compared the District's budgeted appropriations to the actual expenditures for 2012-13 through 2014-15 to determine if the appropriation estimates were reasonable and if any specific expenditure lines were consistently overbudgeted.

- We reviewed the real property tax levies for the 2012-13 through 2014-15 fiscal years to determine trends. We also compared the tax levies for the 2012-13 through 2015-16 fiscal years to the District's real property tax cap calculation to determine if the levies were within the statutory real property tax limits.

- We compared the trends of expenditures and non-real property tax revenues to the increases in the real property tax levy to determine if the total increases in real property tax levies from 2012-13 through 2014-15 were necessary.

We conducted this performance audit in accordance with GAGAS. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

APPENDIX D

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