



# Oakfield-Alabama Central School District Budgeting

## Report of Examination

Period Covered:

July 1, 2011 – April 4, 2016

2016M-172



Thomas P. DiNapoli

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# State of New York Office of the State Comptroller

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## Division of Local Government and School Accountability

July 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 Oakfield-Alabama Central School District, entitled Budgeting. 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 Oakfield-Alabama Central School District (District) is located in the Towns of Oakfield, Alabama, Batavia, Pembroke and Elba in Genesee County and the Town of Barre in Orleans County. The District covers approximately 72 square miles. 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 (Superintendent) is the District's 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 responsibility for the District's finances and accounting records rests primarily with the Business Administrator.

There are three schools in operation within the District with approximately 870 students. The District's budgeted appropriations for the 2015-16 fiscal year totaled \$18.5 million and were funded primarily with State aid, real property taxes and grants.

## Objective

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

- Did the Board adopt realistic budgets and take appropriate action to address the reasonableness of fund balance, including reserves?

## Scope and Methodology

We examined the District's budgeting practices for the period July 1, 2011 through April 4, 2016.

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 plan to initiate 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.

# Budgeting

The annual operating budget represents the District's financial plan for a fiscal year and is an important tool for managing District finances. A good budget begins with sound estimates and well supported budgetary assumptions. The Board, Superintendent and Business Administrator are responsible for accurate and effective budgeting. Spending levels and financial resources should be accurately gauged at budget preparation time to ensure that planned services are properly funded.

The Board and District officials did not prepare accurate budgets for the 2011-12 through the 2014-15 fiscal years. While the District appropriated fund balance and reserves to help finance operations, it was not needed because the District's budgeting practices produced operating surpluses in three of the four fiscal years we reviewed. The District only used \$296,578 (9.6 percent) of the \$3.1 million of fund balance it appropriated during this time to finance operations. When unused appropriated fund balance was added back, the District's recalculated unrestricted fund balance exceeded the statutory limit by up to 5 percentage points.

Furthermore, the balance in the retirement contribution reserve was \$1.7 million as of June 30, 2015, which was more than five times the District's annual average contribution. Consequently, we question the reasonableness of the amount in this reserve. Finally, the debt reserve, with a balance of \$241,000 as of June 30, 2015, has not been used over the last four years. District officials were unsure of the source of the cash in this reserve. Unless the cash represents unexpended bond proceeds and the related debt remains outstanding, District officials should not have deposited the funds in a debt reserve. The funds should be returned to unrestricted fund balance and used for operations, to reduce the tax levy or both.

## Budget Estimates

The Board and District officials are responsible for accurately estimating revenues and appropriations in the annual budget. Accurate budget estimates help ensure that the real property tax levy is not greater than necessary.

We compared the adopted budgets with actual operating results for the 2011-12 through 2014-15 fiscal years and found that actual revenues were generally in line with budgeted estimates but budgeted appropriations were consistently more than expenditures. The District overestimated appropriations by \$5.8 million (8.1 percent) over this time period, as shown in Figure 1.

<b>Figure 1: Overestimated Appropriations</b>					
	2011-12	2012-13	2013-14	2014-15	Total
Appropriations	\$17,027,575	\$17,437,100	\$17,750,800	\$18,213,622	\$70,429,097
Encumbrances	\$150,054	\$430,984	\$309,338	\$211,541	\$1,101,917
Expenditures	\$15,895,043	\$15,860,784	\$16,891,053	\$17,064,185 <sup>a</sup>	\$65,711,065
Variance	\$1,282,586	\$2,007,300	\$1,169,085	\$1,360,978	\$5,819,949
Percentage	7.5%	11.2%	6.5%	7.4%	8.1%

<sup>a</sup> Excludes \$1,009,537 transfer from the capital reserve to the capital projects fund in 2014-15.

Appropriations that were overestimated over the four-year period included gas (\$563,000, or 63 percent), electricity (\$525,000, or 46 percent) and medical insurance (\$888,000, or 13 percent). The District also improperly included a contingency appropriation account in the adopted budget. For example, \$329,500 of contingency appropriations were included in the 2014-15 adopted budget (or 1.8 percent of the adopted budget). There is no authority for the District to include appropriations for contingencies in the adopted budget.

We reviewed the 2015-16 adopted budget and determined that the District again overestimated electricity by \$107,000 (49 percent) and gas by \$115,000 (72 percent). The District reduced budgeted appropriations for gas and electric from 2011-12 through 2016-17<sup>1</sup> but also continued to improperly include \$826,000 of contingency appropriations (4.5 percent of the adopted budget) in 2015-16 and \$514,000 (2.6 percent of the adopted budget) in 2016-17.

Overestimating appropriations has resulted in the levy of more real property taxes than necessary to fund operations.

## Fund Balance

The estimation of fund balance is an integral part of the budget process. The New York State Real Property Tax Law currently limits unrestricted fund balance to no more than 4 percent of the ensuing fiscal year's budget. Any surplus fund balance over this percentage should be used as a funding source. Due to the District's practice of overestimating appropriations, it has experienced an operating surplus in three of the last four fiscal years, as indicated in Figure 2. The District appropriated an average of \$768,000 in fund balance as a financing source in the annual budget for fiscal years 2011-12 through 2014-15. This appropriation of fund balance reduced the level of unrestricted fund balance at fiscal year end to the 4 percent limit.

<sup>1</sup> The District budgeted \$250,000 for gas in 2011-12 and 2012-13, \$200,000 from 2013-14 through 2015-16 and \$150,000 in 2016-17. The District budgeted \$300,000 for electricity in 2011-12 through 2013-14, \$240,000 in 2014-15 and 2015-16 and \$205,000 in 2016-17.

<b>Figure 2: Unrestricted Fund Balance at Year-End</b>				
	<b>2011-12</b>	<b>2012-13</b>	<b>2013-14</b>	<b>2014-15</b>
Beginning Fund Balance	\$4,239,827	\$5,085,219	\$5,685,093	\$5,388,515
Add: Operating Surplus/(Deficit)	\$845,392	\$599,874	(\$296,578)	\$8,321
Less: Transfers From the Capital Reserve to the Capital Projects Fund	\$0	\$0	\$0	\$1,009,537
Ending Fund Balance	\$5,085,219	\$5,685,093	\$5,388,515	\$4,387,299
Less: Restricted Fund Balance	\$3,221,234	\$3,675,539	\$3,461,636	\$2,404,041
Less: Encumbrances	\$430,984	\$309,338	\$211,541	\$242,456
Less: Appropriated Fund Balance for the Ensuing Year	\$736,000	\$1,000,000	\$1,000,000	\$1,000,000
Unrestricted Fund Balance at Year-End	\$697,001	\$700,216	\$715,338	\$740,802
Ensuing Year's Budgeted Appropriations	\$17,437,100	\$17,750,800	\$18,213,622	\$18,511,398
Unrestricted Fund Balance as Percentage of Ensuing Year's Budget	4%	4%	4%	4%

However, the District only needed a minor amount of the appropriated fund balance to finance operations (\$296,578 in 2013-14 or 9.6 percent of total appropriated during the four years reviewed<sup>2</sup>). When unused appropriated fund balance was added back, the District's recalculated unrestricted fund balance exceeded the 4 percent statutory limit by up to 5 percentage points, as indicated in Figure 3.

<b>Figure 3 : Unused Fund Balance</b>				
	<b>2011-12</b>	<b>2012-13</b>	<b>2013-14</b>	<b>2014-15</b>
Unrestricted Fund Balance at Year-End	\$697,001	\$700,216	\$715,338	\$740,802
Add: Appropriated Fund Balance Not Used to Fund Ensuing Year's Budget	\$736,000	\$703,422	\$1,000,000	\$1,000,000
Recalculated Unrestricted Fund Balance	\$1,433,001	\$1,403,638	\$1,715,338	\$1,740,802
Recalculated Unrestricted Fund Balance as Percentage of Ensuing Year's Budget	8%	8%	9%	9%

The District appropriated \$1 million as a financing source in the 2015-16 budget and \$807,000 in the 2016-17 budget. We estimate that it likely will not be needed to help finance operations. Therefore, we expect unrestricted fund balance will continue to exceed the statutory limit.

While the District has realized operating surpluses and retained excessive fund balance, it also consistently levied real property taxes averaging \$5 million from fiscal years 2011-12 through 2014-15.

<sup>2</sup> This total amount includes \$336,000 appropriated to finance the 2011-12 budget.



Furthermore, the District's practice of consistently appropriating fund balance that is not needed to finance operations is, in effect, a reservation of fund balance that is not provided for by statute.

## Reserves

A school district can legally set aside and reserve portions of fund balance to finance future costs for a variety of specified objects or purposes. The Board should balance the intent for accumulating money for future identified needs with the obligation to ensure that District residents are not overburdened. Money set aside in reserves must be used only in compliance with statutory provisions that determine how reserves are established, funded, expended and discontinued. The District should also have a policy establishing the intended funding levels of reserves and when they will be used. School districts should maintain reserve balances that are reasonable and consistent with the Board policy. Funding reserves at greater than reasonable levels contributes to real property tax levies that are higher than necessary because the excessive reserve balances are not being used to fund operations.

As of June 30, 2015, the District reported four reserves in the general fund totaling \$2.4 million. The District appropriates reserves as a funding source in the annual budget but does not use them. We also found that the Board did not establish an appropriate funding level for the retirement contribution reserve. Consequently, we question the reasonableness of the amount in this reserve. Furthermore, the funds in the debt reserve should be returned to unrestricted fund balance and used for operations, to reduce the tax levy or both.

Appropriation of Reserves – From 2013-14 through 2015-16, the District appropriated an average of \$367,000 from reserves as a funding source in the annual budget but did not actually use them. Specifically, in the 2013-14 budget, the District appropriated \$360,000 from the retirement contribution reserve and \$20,000 from the unemployment reserve. For 2014-15, the District appropriated \$360,000 from the retirement contribution reserve and \$10,000 from the unemployment reserve. The District again appropriated \$350,000 from the retirement contribution reserve in 2015-16. However, the District did not charge any expenditures to the reserves. As a result, none of the reserves were used to fund appropriations as planned in the budgets. This budgeting practice gives residents the false impression that the District is using reserves to help fund the budget and keeping the tax levy down.

Retirement Contribution Reserve – General Municipal Law authorizes the establishment of this type of reserve to pay contributions for employees covered by the New York State and Local Retirement System. The balance of this reserve as of June 30, 2015 was \$1.7 million, which was more than five times the District's annual average

contribution of approximately \$293,000 over three years. There was no indication that the Board established an appropriate funding level for this reserve. Consequently, we question the reasonableness of the amount in this reserve.

Debt Reserve – In certain circumstances, money must be restricted in a debt reserve. For example, unexpended bond proceeds and related interest earnings must be restricted and used to pay debt service costs on that debt issue or for the related capital expenditures. School districts are not allowed to establish a debt reserve for any other purpose.

The District maintains a debt reserve in the general fund with a balance of \$241,000 as of June 30, 2015. The balance in this reserve has not been used over the last four fiscal years. District officials were unsure of the source of the cash in this reserve. Unless the cash represents money required to be restricted for debt service, District officials should not have deposited the funds in a debt reserve. The funds should be returned to unrestricted fund balance and used for operations, to reduce the tax levy or both.

The Board adopted a reserve fund policy that states the Board should periodically review all reserve funds. Furthermore, the policy states the District should prepare an annual report of all reserve funds for presentation to the Board. While the Business Administrator prepared an annual report of reserves and the Board approved the funding and use of reserves, there was no evidence in the minutes to indicate that the Board discussed optimal funding levels for reserves or periodically assessed the reasonableness of the amounts accumulated.

## Recommendations

The Board and District officials should:

1. Develop realistic estimates of appropriations and the use of fund balance in the annual budget.
2. Discontinue the use of a contingency account within the annual budget.
3. Ensure that the amount of unrestricted fund balance is in compliance with the statutory limit and develop a plan to use excess fund balance in a manner that benefits residents. Such uses of surplus funds as a financing source could include:
  - Funding one-time expenditures;
  - Funding needed reserves; and
  - Reducing District property taxes.

4. Return money improperly residing in the debt reserve to unrestricted fund balance in the general fund.
5. Review all reserves at least annually to determine if the amounts reserved are necessary and reasonable. Any excess funds should be transferred to unrestricted fund balance (where allowed by law) or to other reserves established and maintained in compliance with statutory directives.
6. Periodically review and update the reserve fund policy to ensure it clearly describes the Board's intended use and funding levels of the reserves.

## **APPENDIX A**

### **RESPONSE FROM DISTRICT OFFICIALS**

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



## Oakfield–Alabama Central School

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July 11, 2016

Jeffrey D. Mazula, Chief Examiner  
295 Main Street, Suite 1032  
Buffalo, New York 14203-2510

Dear Mr. Mazula,

The Oakfield-Alabama Central School District is in receipt of the draft Budgeting audit report prepared by the Office of the State Comptroller for the period covering July 1, 2011- April 4, 2016. The Board of Education, on behalf of the District, would like to thank the Comptroller's Office for their guidance throughout this process.

The District is pleased to respond to an audit that highlights conservative budgeting practices which have resulted in the preservation of educational programs for students despite frozen Foundation Aid and a Gap Elimination Adjustment that cost the District a combined total of \$17.8 million over the past six years. District Officials and the Board of Education work hard to create a sensible budget, despite the devastating impact of reduced state funding in a school district that receives 65% of their revenues through state aid. Our community has supported this approach as taxpayers have overwhelmingly supported our budgets by passing the last five budgets by an average of 80%.

The District and Board of Education are committed to continuously improving their operations, strengthening their financial practices and increasing accountability. Therefore, we have outlined the Corrective Action Plan below to address the recommendations of the Comptroller's audit.

### Corrective Action Plan

In an effort to further strengthen our budgeting practices, District Officials and the Board of Education will review the need for appropriated fund balance each fiscal year while preparing the budget and continue to prepare a budget that recognizes the variables (including regular and special education instruction) that must be considered in order to protect the District's operations. District Officials have already reduced the appropriated fund balance for the 2016-17 fiscal-year by \$200,000.

The District and Board of Education will continue to monitor the fund balance throughout the year to ensure compliance with statutory limits. The District agrees that the Debt Reserve should be returned to the General Fund and used to pay down outstanding debt. The Board of Education will continue to review Reserve balances annually and create a policy that reflects the financial goals of the District.

Again, thank you for the insight and recommendations.

Sincerely,

Mark Alexander

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Learn Today for Tomorrow

## **APPENDIX B**

### **AUDIT METHODOLOGY AND STANDARDS**

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

- We interviewed District officials to obtain an understanding of the District's financial condition, budgeting practices and the use of reserve funds.
- We compared budgets with actual operating results for fiscal years 2011-12 through 2014-15 and analyzed accounts with significant variances.
- We reviewed Board minutes and accounting records to determine whether reserves reported as of June 30, 2015 were reasonably funded.
- We analyzed unrestricted fund balance levels from 2011-12 through 2014-15.

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.

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