



Putnam Central School District Budgeting

Report of Examination

Period Covered:

July 1, 2013 — July 31, 2015

2015M-243



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 Putnam 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 Putnam Central School District (District) is located in the Towns of Putnam and Dresden in Washington County and in the Town of Ticonderoga in Essex County. The District is governed by the Board of Education (Board) which is composed of five 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 District operates one school for 20 students from kindergarten through sixth grade with 10 full-time employees. After sixth grade, the District's students attend the Ticonderoga Central School District (Ticonderoga). The District's budgeted appropriations for the 2015-16 fiscal year are \$2.5 million, which are funded primarily with State aid and real property taxes. Tuition costs for students to attend Ticonderoga account for \$822,399 of the budgeted appropriations.

Objective

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

- Does the Board adopt realistic budgets that are structurally balanced?

Scope and Methodology

We examined the District's budgeting process for the period July 1, 2013 through July 31, 2015.

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. 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. Except as specified in Appendix A, District officials generally agreed with our recommendations and indicated they planned to take corrective action. Appendix B includes our comments on 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.

Budgeting

Proper budget development begins with identifying and estimating the necessary expenditures to carry out the educational and other programs the District provides to students. The Board must next identify and estimate the revenues, other than real property taxes, that should be available to finance the planned expenditures. The Board must also estimate the amount of unrestricted fund balance (which represents resources remaining from prior fiscal years) that will be available at year-end, some or all of which may be used to pay for unexpected expenditures or fund the ensuing year's appropriations. After taking these factors into account, the Board establishes the expected tax levy necessary to fund operations. Accurate estimates help ensure that the real property tax levy is not greater than necessary.

Expenditure estimates should be developed based on prior years' operating results, past expenditure trends, anticipated future needs and available information related to projected changes in significant revenues or expenditures. Unrealistic budget estimates can mislead District voters and taxpayers and can significantly impact the District's year-end unrestricted fund balance and financial condition.

Unrestricted fund balance that exceeds the 4 percent statutory limit¹ should be used to lower real property taxes or pay for one-time expenditures. When fund balance is appropriated as a funding source, it reduces the fund balance included in the 4 percent calculation and the expectation is that there will be a planned operating deficit in the ensuing fiscal year, financed by the amount of the appropriated fund balance. Conversely, an operating surplus (when budgeted appropriations are not fully expended, expected revenues are greater than estimated or both) increases the total year-end fund balance and can indicate that budgets are not realistic.

The Board and District officials did not effectively manage the District's financial condition by ensuring budget estimates were reasonable and based on historical costs and trends. For the 2013-14 and 2014-15 fiscal years, the District overestimated expenditures by a total of \$682,398. This overestimation averages 15 percent of total appropriations for the two years. Due to the overestimation of expenditures, the District has accumulated an amount of unrestricted fund balance that exceeds the statutory limit of 4 percent of the ensuing year's budgeted appropriations. As of June 30, 2015, the District's unrestricted fund balance was 59 percent of the 2015-16 budgeted appropriations.

¹ New York State Real Property Tax Law Section 1318

Budgetary Estimates – We compared the District’s estimated revenues and appropriations with actual results of operations to determine if the estimates were reasonable. We found the estimates for revenues to be reasonable. However, District officials consistently presented, and the Board approved, budgets which overestimated appropriations for both the 2013-14 and 2014-15 fiscal years by a total of \$682,398 for these two years.

Figure 1: Overestimated Appropriations

Fiscal Year	Budgeted Appropriations	Actual Expenditures	Overestimated Appropriations	Percent Overestimated
2013-14	\$2,249,218	\$1,885,376	\$363,842	16%
2014-15	\$2,337,837	\$2,019,281	\$318,556	14%
Total	\$4,587,055	\$3,904,657	\$682,398	15%

We analyzed significant expenditures² to determine if the budgeted appropriations were reasonable based on actual expenditures. The appropriations for estimated tuition paid for students to attend Ticonderoga³ were significantly overestimated by \$152,314 for 2013-14 and \$119,200 for 2014-15 when compared to actual tuition expenditures. The 2014-15 budgeted tuition appropriations were \$737,928 while actual expenditures were \$618,728. In the 2015-16 budget, District officials appropriated \$822,399 for tuition, which is an increase of \$84,471 (11 percent). The District paid tuition for 42 students⁴ to attend Ticonderoga in both the 2013-14 and 2014-15 years. The tuition rate is based on Ticonderoga’s expenditures and the District budgeted for an increase in the rate.⁵ However, the District budgeted for an increase of 12 students for the 2013-14 year and 14 students for the 2014-15 year. This increase is unreasonable given the number of students remained unchanged for the two previous years and the planned increase represents approximately a 30 percent increase in the number of students attending Ticonderoga. The number of students for the 2015-16 school year decreased to 41, which includes regular, special education and BOCES enrollments.

² Significant expenditures are equal to or greater than 10 percent of total expenditures.

³ The District pays tuition to the Ticonderoga School District for students in grades 7-12. Tuition is also paid for students requiring special education services and students attending the Clinton-Essex-Warren-Washington Board of Cooperative Educational Services (BOCES).

⁴ The composition of students for which tuition was paid was 36 regular education students, two special education and four BOCES students for the 2013-14 year. For the 2014-15 year, the composition for tuition paid was 37 regular education students, two special education and three BOCES students.

⁵ Our analysis considered the increase in Ticonderoga’s rate per student.

The Superintendent told us the tuition expenditure is intentionally overestimated because it is difficult to predict and the District does not want to be short of funds to pay Ticonderoga. While it is reasonable to be conservative when making an estimate for a major portion of the District's appropriations, the 30 percent increase estimate is excessive when considering prior years' consistency in the number of students attending Ticonderoga.

In addition to tuition, there were 15 non-significant expenditure account⁶ balances that were overestimated by a total of \$129,683 (35 percent of appropriations) for the 2013-14 year and \$145,018 (33 percent of appropriations) for the 2014-15 year. For example, hospital and medical insurance was overestimated by \$62,221 (30 percent) in 2013-14 and \$43,263 (19 percent) in 2014-15.⁷ Because the number of participants and rates are known, this cost is predictable and should be accurately estimated. Also, expenditures for the line item Operation of Plant were overestimated by \$19,731 (51 percent) in 2013-14 and \$31,943 (61 percent) in 2014-15.⁸

The District's consistent overestimation of appropriations has resulted in annual surpluses that have resulted in the District accumulating unrestricted fund balance greater than the allowable limit of 4 percent of the ensuing year's appropriations.

Fund Balance – As a result of the excessive estimates for expenditures, the District has been realizing annual operating surpluses that have caused the unrestricted fund balance to be excessive at year end and for taxes to be higher than necessary. Although the District appropriates fund balance to finance a portion of the ensuing year's operations, the fund balance is only partially used to actually finance operations as a result of actual expenditures being significantly less than appropriations. The unrestricted fund balance was 64 percent and 59 percent of subsequent year's appropriations for the fiscal years ended June 30, 2014 and 2015, respectively.

⁶ The individual expenditure balances were less than 10 percent of total expenditures.

⁷ Overestimated expenditures for hospital and medical insurance includes employee and retiree health insurance and health reimbursement account plans (employer funded medical reimbursement plans).

⁸ Overestimated expenditures for Operation of Plant includes budgeted expenditures for non-instructional salaries and expenditures for heating oil.

Figure 2: Unrestricted Fund Balance

	2013-14	2014-15
Beginning Fund Balance	\$1,611,415	\$1,789,967
Add: Prior Period Adjustment	\$8,511	\$0
Add: Operating Surplus	\$170,041	\$63,751
Add: Capital Reserve from Capital Projects Fund ^a	\$80,026	\$100,059
Total Ending Fund Balance	\$1,869,993	\$1,953,777
Less: Fund Balance Appropriated for Ensuing Year's Operations	\$234,600	\$349,748
Less: Restricted Fund Balance ^b	\$138,072	\$158,111
Less: Encumbrances	\$0	\$2,347
Unrestricted Fund Balance at Year End	\$1,497,321	\$1,443,571
Ensuing Year's Budgeted Appropriations	\$2,337,837	\$2,451,407
Reported Unrestricted Funds as Percentage of Ensuing Year's Budgeted Appropriations	64%	59%
^a The District has incorrectly recorded the capital reserve in the capital projects fund. Accounting standards require this reserve to be included in the general fund. ^b Restricted fund balance is comprised of an unemployment insurance reserve (\$16,000), a reserve for tax certiorari (\$42,000) and the capital reserve.		

The District's last two independent audit reports contained findings related to the unrestricted fund balance being in excess of the statutory limit. However, District officials have not developed a corrective action plan to reduce the unrestricted fund balance to the statutory limit. Had District officials used more realistic appropriation estimates, they could have avoided the accumulation of excess fund balance and reduced the tax levy. Furthermore, the District's budget is not transparent to the District's taxpayers and other interested parties. By appropriating fund balance for amounts of \$234,600 for the 2014-15 year and \$349,748 for the 2015-16 year, it gives the appearance the District is returning a portion of excess funds to its taxpayers. However, the District's practice of consistently overestimating appropriations results in the District raising taxes in excess of what is actually necessary.

Recommendations

The Board should:

1. Adopt budgets that reflect the District's actual needs based on historical trends or other identified analysis, including a reasonable estimate of appropriated fund balance.
2. Ensure that the amount of unrestricted fund balance is in compliance with the statutory limit.

3. Develop a plan to reduce the amount of unrestricted fund balance in a manner that benefits District taxpayers. Such uses could include, but are not limited to, reducing District real property taxes, financing one-time expenditures and funding established reserves.

APPENDIX A

RESPONSE FROM DISTRICT OFFICIALS

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

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December 28, 2015

Chief Examiner
Office of State Comptroller
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Re: Audit Response Letter to Audit 2015M-243

Dear Auditing Official:

The Putnam Central School District is in receipt of Audit number 2015M-243 and are appreciative of the time and efforts of the Office of The State Comptroller and the auditor assigned to this audit.

The Board of Education of the Putnam Central School District disagrees with some of the findings of the audit. For example, the audit states "The Board and District officials did not effectively manage the District's financial condition by ensuring budget estimates were reasonable and based on historical costs and trends". With a tax levy of five dollars per thousand of assessed valuation, which is one of the lowest in the State of New York, we find it difficult to accept the premise that the Board and District officials did not effectively manage budget estimates. Also, the Board has put forth budgets that have not even approached the tax cap limits during this time. We find it difficult to understand how this could be accomplished if the auditor's statements were accurate. The auditor references overestimation of expenditures, but makes no reference to considerable cost savings accrued after the budgets had been adopted.

The auditor's statements concerning tuition costs show no understanding of the actual conditions the District encounters. There is no mention of the Seneca Falls Formula or how the timeliness of its implementation as related to year to year budgeting effects the expenditure calculations. To simply state that (x) number of students were budgeted is failing to factor rate increases, transient population movement, and the local contractual agreement with the District receiving students from Putnam.

The auditor stated that hospital and medical insurance expenditures were overestimated and could be easily determined passed on participation. The District uses the estimates provided to it

See
Note 1
Page 12

See
Note 2
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See
Note 3
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by its insurance broker BCI. The District is governed by Community Rating Rules which can change at any moment. We believe that the auditor's understanding of the difference in Community Rating and large group health insurance is limited and therefore this section is based on a false premise.

See
Note 4
Page 12

The auditor highlights the Districts level of unrestricted fund balance. While in agreement that the fund balance is at a level much higher than the recommendations from the Office of The State Comptroller, we vehemently disagree on the statements by the auditor in regards to how the fund balance was built. There was no effort on the part of the auditor to understand the cost saving initiatives employed by the District or the impact of the High Tax Aid as a never before realized revenue source.

See
Note 5
Page 12

See
Note 6
Page 12

Finally, while it is not the job of the auditor to discuss the lack of a tuition reserve for Special Education, this line makes up a majority of the unrestricted fund balance. Until the State of New York Legislature passes a tuition reserve bill, this will be a difficult proposition for small districts especially. The four percent unrestricted fund balance level recommended by the Office of the State Comptroller is insufficient to fund the expenditure of even one (1) high needs special education student placement in the Putnam Central School District.

See
Note 5
Page 12

The District has been monitoring this level of unrestricted fund balance and has formulated a plan to reduce the unrestricted fund balance to be at a level more commensurate with the recommendations of the Office of the State Comptroller given the items previously discussed.

Respectfully,

Matthew Boucher
Superintendent of Schools
Putnam Central School District

APPENDIX B

OSC COMMENTS ON THE DISTRICT'S RESPONSE

Note 1

As noted in the report, the District's adopted budgets consistently included overestimated appropriations. As a result, none of the fund balance appropriated in the 2013-14 and 2014-15 budgets was actually used to finance operations and the already excessive fund balance levels continued to increase rather than decrease.

Note 2

The annual budget process should begin with realistic and supported estimates of appropriations. Cost saving measures being considered or implemented by the District should be considered when making these estimates. Additionally, if the District does achieve cost savings, the savings should be reflected in the next year's budgetary estimates. However, the District consistently overestimated appropriations from one year to the next.

Note 3

We compared the amount spent on tuition in prior years to the budget estimates and considered rate increases in our analysis.

Note 4

The appropriation for hospital and medical insurance was consistently overestimated. As noted in the report, this appropriation was overestimated by 30 percent in the 2013-14 fiscal year and 19 percent in the 2014-15 fiscal year. We acknowledge that the insurance rates can increase and the District should use the estimates provided by its insurance broker in developing a budget estimate. However, the District should also consider the level of prior years' actual costs for the insurance and develop more reasonable estimates for the cost of its hospital and medical insurance.

Note 5

New York State Real Property Tax Law Section 1318 limits the amount of unrestricted fund balance a District can carry over to the following year. This is a legal requirement all school districts are required to adhere to and not an Office of the State Comptroller recommendation.

Note 6

Each District became eligible to receive a high tax aid apportionment in the 2008-09 school year and is eligible to receive this aid through the 2015-16 school year. This revenue source would not have been a new source for the 2013-14 and 2014-15 budget years. Therefore, District officials should have had an estimate of this aid prior to completing the budget for the following year.

APPENDIX C

AUDIT METHODOLOGY AND STANDARDS

Our overall goal was to assess the District's budgeting process. To accomplish our objective, we interviewed District officials and employees, tested selected records and examined pertinent documents.

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

- We interviewed District officials and employees to gain an understanding of the budget process and determine reasons for large expenditure variances.
- We reviewed District policies and procedures.
- We reviewed and analyzed reported fund balance levels in comparison to amounts appropriated in adopted budgets for fiscal years 2013-14 through 2014-15.
- We calculated the unrestricted fund balance as a percentage of the next year's budget.
- We compared budgeted revenues and appropriations to actual revenues and expenditures for the 2013-14 and 2014-15 fiscal years. We also compared the 2014-15 actual revenues and expenditures to the 2015-16 budgeted revenues and appropriations.

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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