DIVISION OF LOCAL GOVERNMENT AND SCHOOL ACCOUNTABILITY

REPORT OF EXAMINATION | 2022M-23

Cattaraugus-Little Valley Central School District

Financial Management

JULY 2022

OFFICE OF THE NEW YORK STATE COMPTROLLER
Thomas P. DiNapoli, State Comptroller

Contents

Report Highlights

Cattaraugus-Little Valley Central School District

Audit Objective

Determine whether the Cattaraugus-Little Valley Central School District's (District) Board and District officials effectively managed fund balance and reserve funds.

Key Findings

The Board and District officials did not properly manage fund balance and reserve funds. The Board and District officials:

- Did not implement our prior audit's recommendations[1] to improve their budgeting practices and ensure surplus fund balance is in compliance with the statutory limit.
- Consistently overestimated appropriations by an average of more than $2 million a year.
- Allowed surplus fund balance to exceed the statutory limit of 4 percent. As of June 30, 2021, it was nearly $7.8 million (28 percent of the 2021-22 appropriations), exceeding the limit by more than $6.6 million or 24 percentage points.
- Maintained an unemployment insurance reserve fund balance of $227,000 which can fund average unemployment expenditures for 78 years.
- Did not ensure $2.2 million was properly restricted in a debt reserve and did not use the funds to pay related debt as required.

As a result, the District was not transparent with taxpayers and has levied more taxes than necessary.

Key Recommendations

- Reduce surplus fund balance to comply with the statutory limit.
- Reduce the unemployment insurance reserve fund balance to a more reasonable level.
- Ensure that money residing in the debt service fund is restricted in a debt reserve and used to pay related debt.

District officials generally disagreed with our findings. Appendix B includes our comments on issues raised in the District's response.

Background

The District serves the Towns of Dayton, East Otto, Leon, Little Valley, Mansfield, Napoli, New Albion, Otto and Persia in Cattaraugus County.

The Board of Education (Board) is responsible for managing and controlling the District's financial and educational affairs. The Superintendent of Schools (Superintendent) is the chief executive officer and is responsible for the District's day-to-day management under the Board's direction.

The Business Executive is responsible for the administration and supervision of financial activities. The Board, Superintendent and Business Executive are responsible for developing the annual budget.

Quick Facts	
2021-22 Appropriations	$27.4 million
Three-Year Cumulative Operating Surplus	$2.2 million
Surplus Fund Balance as of June 30, 2021	$7.8 million
Student Enrollment	858

Audit Period

July 1, 2018 – December 8, 2021

1 *Cattaraugus-Little Valley Central School District – Financial Management (2016M-61),* which was released in June 2016

Financial Management

How Should Financial Condition be Effectively Managed?

To effectively manage financial condition, a school board (board) should adopt reasonably estimated and structurally balanced budgets based on historical data or known trends in which recurring revenues finance recurring expenditures. In preparing the budget, a board must estimate the amounts a school district will spend and receive, the amount of fund balance that will be available at fiscal year-end to use towards the next year's budget and the expected real property tax levy. Accurate estimates help ensure that the real property tax levy is not greater than necessary and that surplus fund balance is not excessive and over the legal limit.

Accurate estimates help ensure that the real property tax levy is not greater than necessary. …

A board is permitted to retain a specified amount of fund balance for cash flow needs or unexpected expenditures and reserves for other identified and planned needs. New York State Real Property Tax Law Section 1318 currently limits the amount of surplus fund balance that a school district can retain to 4 percent of the next year's budget. Any surplus fund balance over this percentage must be used to reduce the upcoming fiscal year's real property tax levy or to fund needed reserves.

The Board and District Officials Overestimated Appropriations

We compared budgeted appropriations and estimated revenues with actual operating results for 2018-19 through 2020-21. While revenue variances were generally reasonable, appropriations were overestimated by an annual average of more than $2 million (8.5 percent) each year, or a total of more than $6.1 million (Figure 1).

Figure 1: Overestimated Appropriations[a]

	2018-19	2019-20	2020-21	Totals
Appropriations	$25,639,000	$25,677,000	$26,569,000	$77,885,000
Actual Expenditures	$23,200,000	$24,188,000	$24,363,000	$71,751,000
Overestimated Appropriations	$2,439,000	$1,489,000	$2,206,000	$6,134,000
Percentage Overestimated[b]	10.5%	6.2%	9.1%	8.5%

a Excludes unbudgeted transfer activity

b Overestimated appropriations divided by actual expenditures

The most significant overestimated appropriations were for employee benefits, totaling $2.6 million for the three fiscal years reviewed (or 17 percent) and instructional salaries, totaling $1.2 million for the three fiscal years (or 4 percent). The Business Executive told us that appropriations were overestimated because she develops budgets in a conservative manner. This included estimating base instructional salaries at a higher level for new hires to remain competitive with other school districts, and budgeting for changes in employees' annual health care coverage. Although officials have hired teachers at higher salary steps, appropriations for salaries were consistently overestimated by an average of $400,000 per year.

The Board, Superintendent and Business Executive should consider historic trends and other known factors when developing budget estimates for expenditures rather than basing appropriations on an assumption that all employees will need spousal or family health coverage or that all new hires will start at higher salary grades. Historical trends consistently demonstrated that actual expenditures in these line items have been less than appropriations. Furthermore, if unanticipated expenditures were to occur, District officials could make certain budget transfers from other unused appropriations rather than consistently overestimating appropriations.

As a result of consistently overestimating appropriations, the District was not transparent with taxpayers and has levied more taxes than necessary which resulted in the accumulation of significant surplus fund balance.

The Board and District Officials Appropriated Fund Balance That Was Not Needed

Because the Board and District officials overestimated appropriations, it appeared that they needed to appropriate fund balance to close projected budget gaps. In the 2018-19 and 2020-21 budgets, the Board appropriated $200,000 and $930,000, respectively. However, the District did not use fund balance as budgeted.

When fund balance is appropriated for the next year's budget, the expectation is that there will be a planned operating deficit equal to the amount of fund balance that was appropriated. The District experienced an operating surplus in all three fiscal years, totaling approximately $2.2 million. Because the Board appropriated fund balance as a funding source in the 2018-19 and 2020-21 budgets, the District should have incurred an operating deficit in these years. Further, the District used some of its annual operating surpluses to make unbudgeted transfers, totaling $1.3 million, to the capital projects fund and the special aid fund. As a result of these unbudgeted transfers, it appeared as though the District incurred an operating deficit one year as fund balance decreased.

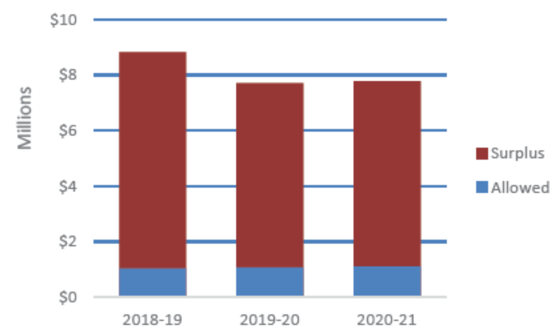
Although surplus fund balance decreased from $8.8 million as of June 30, 2019 to approximately $7.8 million as of June 30, 2021, surplus fund balance was still 28 percent of 2021-22 budgeted appropriations, exceeding the statutory limit by more than $6.6 million or 24 percentage points (Figure 2).

The Business Executive told us that they are aware that surplus fund balance is exceeding the statutory limit and have discussed plans to use the excess. However, currently the District does not have a formalized plan for its use.

Further, we reviewed the 2021-22 budget and determined that revenue and expenditure estimates are consistent with the last three fiscal years. As such, the District will most likely have an operating surplus that will result in higher surplus fund balance. Based on our review of the 2021-22 budget, we project that the District will generate another operating surplus in 2021-22 and will not need to use the $883,000 of fund balance appropriated in the budget.

FIGURE 2

Surplus Fund Balance at Fiscal Year End



The Board and District officials' practice of 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 and is a circumvention of the statutory limit imposed on the level of surplus fund balance. When unused appropriated fund balance is added back, surplus fund balance exceeded the limit by approximately $7.6 million to $7.8 million, or 32 to 34 percentage points during the three-year period (Figure 3).

Figure 3: Recalculated Surplus Fund Balance

	2018-19	2019-20	2020-21
Surplus Fund Balance	$8,828,000	$7,706,000	$7,770,000
Add: Unused Appropriated Fund Balance	0	$930,000	$883,000
Recalculated Surplus Fund Balance	$8,828,000	$8,636,000	$8,653,000
Maximum Surplus Fund Balance Allowed	$1,027,000	$1,063,000	$1,097,000
Fund Balance in Excess of Limit	$7,801,000	$7,573,000	$7,556,000
Recalculated Surplus Fund Balance as a Percentage of Next Year's Budget	34%	33%	32%

2 *Cattaraugus-Little Valley Central School District – Financial Management (2016M-61)*, which was released in June 2016.

The previous audit report issued by our office[2] informed District officials that the District's surplus fund balance exceeded the statutory limit by 10 to 14 percentage points and recommended that the District improve its budgeting practices. In response to our previous audit, the Board developed a corrective action plan which indicated that the District would work with a financial consultant to assist in improving its short- and long-term budgeting practices. However, since then the District has continued to overestimate appropriations each year, and surplus fund balance has continued to exceed the limit. The Superintendent and Business Executive told us that the District contracted with a financial consultant after our previous audit. However, the consultant left her position and ended the contract with the District in 2018. The District did not contract with another financial consultant. Officials were unable to provide a reasonable explanation for why they did not contract with another financial consultant to implement the prior audit recommendations.

Although the real property tax levy decreased by $140,375 from the 2018-19 to 2021-22 fiscal years, had the Board and officials adopted more reasonable budgets, they could have considered using these excess funds to fund one-time expenditures, fund needed reserves, pay off debt or reduce the tax levy and provide an even greater benefit to taxpayers.

…[T]he District has continued to overestimate appropriations each year, and surplus fund balance has continued to exceed the limit.

What Is Proper Management of Reserve Funds?

School districts are legally allowed to establish reserves and accumulate funds for certain future purposes (e.g., unemployment expenditures). A board should plan for the funding and use of reserve funds by balancing the desire to accumulate funds for future needs with the obligation to make sure real property taxes are not higher than necessary. It is important that the board adopt a comprehensive written policy that states its rationale for establishing reserve funds, objectives for each reserve, maximum targeted funding levels and conditions under which reserves will be used or replenished.

New York State Local Finance Law, Section 165.00 and New York State General Municipal Law, Section 6-l require a debt reserve to be established if unexpended bond proceeds remain on a capital improvement or when a capital improvement has outstanding debt remaining at the time of sale. These funds must be restricted and used for related debt principal and interest payments.

The Board Did Not Adopt an Adequate Written Reserve Fund Policy

The Board adopted a written reserve fund policy in 2017. The policy requires that an annual report be provided to the Board that includes a description of the reserve funds, the date of establishment, interest earned, withdrawal details, ending balances and an analysis of projected needs for the reserve funds in the upcoming fiscal year with a recommendation regarding funding those needs. However, the policy does not address circumstances under which reserve funds would be used or replenished. Such information is necessary for officials when determining how and when to use reserve funds.

The Business Executive prepared an annual reserve report; however, the report did not include a description of the reserve funds, date of establishment, an analysis of projected needs for the reserve funds in the upcoming fiscal year, or a recommendation regarding funding those needs. The Business Executive told us that by providing the annual report and discussing reserve funds with the Board she believed she was complying with District policy. Without a comprehensive annual report that contains all required and recommended components, the Board's ability to make informed decisions regarding the funding and use of the reserve funds is limited and its intentions for reserves are not transparent to District taxpayers.

…[T]he reserve balance as of June 30, 2021 was $227,000, more than 78 times the average annual expenditure.

Reserve Funds Were Overfunded and Not Used

As of June 30, 2021, the District reported four general fund reserve funds totaling $1.8 million. We reviewed the reserve funds and found that although reserve funds were properly established, two were overfunded by as much as $389,000 as of June 30, 2021. The remaining two reserve funds were reasonably funded but were not used.

Employee Benefit Accrued Liability Reserve (EBALR) – The Board established this reserve with the intent to make payments to employees for accrued time due to them upon leaving District employment. As of June 30, 2021, the reserve had a balance of $659,000, while the District's related liability was $497,000. Therefore, the reserve is overfunded by $162,000. During our audit period, the District incurred $155,000 of expenditures which could have been paid using this reserve fund but instead the District continually budgeted for the expenditures out of the general fund budget. The Business Executive told us the reserve was funded at $517,000 in 2003, because of the estimated liability at that time. However, since then the reserve has grown due to interest earned on the funds and because the funds were not used for allowed expenditures.

Unemployment Insurance Reserve – The Board established this reserve with the intent to reimburse the New York State Unemployment Insurance Fund for payments made to claimants. Over that last three fiscal years, unemployment expenditures have averaged $2,900 per year. However, the reserve balance as of June 30, 2021 was $227,000, more than 78 times the average annual expenditure. The District did not use reserve funds to pay for these expenditures and continually budgeted for the expenditures out of the general fund budget.

The Business Executive told us that the reserve was funded at $179,000 in 2004 to provide funding for a potential unemployment insurance liability. At that time, the District had merged with another school district and was anticipating the elimination of 31 employees' positions in three years. Although the District terminated these employees, the District did not end up having to pay unemployment claims. In addition, the District budgeted and levied taxes for annual unemployment claims against the District, instead of the reserve, to pay for unemployment claims. As a result, the reserve fund's balance continued to grow through the accumulation of interest earnings.

Further, our previous report indicated that the unemployment insurance reserve had a balance of $223,000 as of June 30, 2015, that would have funded 12 years of expenditures.

With no activity in the reserves and given the lack of a detailed policy, we question the levels at which these reserves are funded. Had the Board adopted an adequate written reserve fund policy and received comprehensive annual reserve reports, the Board may have noticed that these reserves had excessive balances and were not being used. Funding reserves at levels higher than necessary contributes to a higher than necessary real property tax levy.

…[T]he District had approximately $2.2 million in the debt service fund, which has not been properly restricted in a debt reserve and is not being used to pay related debt. ...

Remaining Bond Proceeds Were Not Properly Restricted or Being Used

The District accounts for and reports a debt service fund, which is separate from the general fund. As of June 30, 2021, the District had approximately $2.2 million in the debt service fund, which has not been properly restricted in a debt reserve and is not being used to pay related debt as required.

According to the Superintendent and Business Executive, the majority of this balance is bond proceeds remaining from a $59 million capital project approved by the voters in 2007. These funds should be used to pay the debt associated with this capital project.

Our previous report recommended that the District ensure the approximately $2 million in the debt service fund was restricted in a debt reserve and used to pay outstanding debt. In their corrective action plan, District officials said that they would work with a financial consultant to ensure the funds were properly restricted and used to pay outstanding debt. However, District officials did not follow through on this corrective action.

The Business Executive told us she knew that the money had to be used to pay related outstanding debt but was unaware that the money had to be restricted in a debt reserve and thought it was enough to record the money in the debt service fund as unrestricted fund balance. Additionally, she did not want to use the money in the debt service fund for debt service payments, because doing so would result in larger operating surpluses and more surplus fund balance in the general fund. However, by not using these funds for debt service payments, the District is levying taxes each year for this purpose which has resulted in the real property tax levy being higher than necessary.

What Do We Recommend?

The Board and District officials should:

1. Develop and adopt budgets that include reasonable estimates for appropriations and the amount of fund balance that will be used to fund operations.
2. Develop a plan to reduce surplus fund balance to comply with the statutory limit. Surplus funds can be used for:
   - Reducing District property taxes,
   - Funding one-time expenditures,
   - Funding needed reserves, and
   - Paying off debt.
3. Adopt a comprehensive written reserve policy that addresses the objective of each reserve, targeted funding levels, conditions under which reserves will be used and replenished, and provide a detailed annual report to the Board.
4. Ensure a comprehensive annual report on reserves, including all elements required by the reserve policy is prepared and provided to the Board.
5. Review the EBALR balance and develop a plan to better align the funding level with the District's long-term liability.
6. Review the unemployment insurance reserve balance and develop a plan to reduce the balance to a more reasonable level.
7. Ensure that money residing in the debt service fund is restricted in a debt reserve and used to pay related debt.

Appendix A: Response From District Officials

Cattaraugus-Little Valley Central School

"Home of the Timberwolves"

PRIDE • EXCELLENCE • WELLNESS

6/10/2022

State of New York
Office of the State Comptroller
BUFFALO REGIONAL OFFICE
Melissa A. Myers, Chief Examiner
295 Main Street, Suite 1032
Buffalo, NY 14203-2510

Dear Ms. Myers:

Response to the recommendations made in the external audit report dated May 12, 2022 for the Cattaraugus–Little Valley Central School District from July 1, 2018 – December 8, 2021.

The Board and District Officials Overestimated Appropriations

Response:
The District is conservative in the approach to estimation of appropriations taking into consideration unknown factors for example, gap elimination adjustment beginning in 2010, a proposed "pandemic adjustment" approved by New York's Governor and Legislature in 2020 of over $1 billion in state K-12 support statewide and other unanticipated costs related to health insurance and other contractual obligations. Most recently, the pandemic has resulted in escalating costs for fuel, utilities, food, bus parts, and materials and supplies supporting educational programming. Education Law §1718 prohibits a school District from exceeding the legally authorized limits it sets by the budget process. Therefore, the District's attempts to build in flexibility to address unanticipated expenditures. The District will take into consideration the recommendations of the auditor with regards to expenditures and budgeting practices.

The Board and District Officials Appropriated Fund Balance That Was Not Needed

Response:

The District reduced the surplus fund balance from $9 million to $7.8 million from 2019 to 2021 in order to minimize the tax levy impact on taxpayers. The district was working with a financial consultant and when the consultant was no longer available, transitioned to another financial planning platform through a COSER with BOCES. The District has and plans to continue to utilize this platform to complete required reports and in the development of multiyear budget plans to project budget scenarios and to improve budget accuracy.

MIDDLE-HIGH BUILDING	ELEMENTARY BUILDING	DISTRICT OFFICE
25 Franklin Street N	25 Franklin Street N	25 Franklin Street N
Cattaraugus, New York 14719-1199	Cattaraugus, New York 14719-1199	Cattaraugus, New York 14719-1199
Phone: (716) 257-3483	Phone: (716) 257-3436	Phone: (716) 257-5293
Fax: (716) 257-5108	Fax: (716) 257-5237	Fax: (716) 257-5298

Prepared

Reserve Funds Were Overfunded and Not Used

Response:

Each year the District provides the Board of Education an annual reserve report in accordance with a policy adopted in 2017. According to the audit findings, reserve funds were properly established, two funds were reasonably funded but not used and two were overfunded. The District will review the 2017 reserve fund policy and make revisions based upon the recommendations including circumstances under which reserve funds would be used or replenished. The District will consult with school attorney and internal auditors on possible future adjustments to the overfunded reserve funds

See Note 1 Page 11

Remaining Bond Proceeds Were Not Properly Restricted or Being Used

Response:

In consultation with the Independent Auditor's reports, the District's debt reserve was properly recorded in the audit report as restricted cash and restricted fund balance. The District will take into consideration the position of the audit report.

See Note 2 Page 11

Sincerely,

Dr. Sharon Huff
Superintendent

Appendix B: OSC Comments on the District's Response

Note 1

The annual reserve report provided to the Board did not include all components required by the District's policy.

Note 2

The $2.2 million in the debt service fund is not properly recorded in the District's accounting records and was not reported correctly in the District's annual financial report (ST-3) filed with the Office of the State Comptroller (OSC); it was recorded as unrestricted cash and classified as assigned fund balance.

Appendix C: Audit Methodology and Standards

We conducted this audit 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. To achieve the audit objective and obtain valid audit evidence, our audit procedures included the following:

- We interviewed District officials and reviewed Board meeting minutes, resolutions and District policies to gain an understanding of the District's financial management policies, procedures and budgeting practices.
- We analyzed general fund financial records from 2018-19 through 2020-21 and evaluated any factors contributing to fluctuations in fund balance including real property tax levy fluctuations and trends.
- We reviewed the adopted general fund budgets from 2018-19 through 2020-21 to assess whether they were reasonable and structurally balanced by comparing adopted budgets with actual results of operations and analyzing significant budget-to-actual variances.
- We reviewed the adopted 2021-22 general fund budget to determine whether any significant changes had been made to the District's budgeting practices.
- We reviewed the District's results of operations from 2018-19 through 2020-21 and calculated surplus fund balance as a percentage of the next year's appropriations to assess whether the District complied with statute.
- We recalculated surplus fund balance as a percentage of the next year's appropriations after adding back unused appropriated fund balance.
- We reviewed reserve fund balances as of June 30, 2021 to assess whether they were properly established, used appropriately and reasonably funded.

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

The Board has the responsibility to initiate corrective action. 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, 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. 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 CAP should be posted on the District's website for public review.

Appendix D: Resources and Services

Regional Office Directory
www.osc.state.ny.us/files/local-government/pdf/regional-directory.pdf

Cost-Saving Ideas – Resources, advice and assistance on cost-saving ideas
www.osc.state.ny.us/local-government/publications

Fiscal Stress Monitoring – Resources for local government officials experiencing fiscal problems
www.osc.state.ny.us/local-government/fiscal-monitoring

Local Government Management Guides – Series of publications that include technical information and suggested practices for local government management
www.osc.state.ny.us/local-government/publications

Planning and Budgeting Guides – Resources for developing multiyear financial, capital, strategic and other plans
www.osc.state.ny.us/local-government/resources/planning-resources

Protecting Sensitive Data and Other Local Government Assets – A non-technical cybersecurity guide for local government leaders
www.osc.state.ny.us/files/local-government/publications/pdf/cyber-security-guide.pdf

Required Reporting – Information and resources for reports and forms that are filed with the Office of the State Comptroller
www.osc.state.ny.us/local-government/required-reporting

Research Reports/Publications – Reports on major policy issues facing local governments and State policy-makers
www.osc.state.ny.us/local-government/publications

Training – Resources for local government officials on in-person and online training opportunities on a wide range of topics
www.osc.state.ny.us/local-government/academy

Contact

Office of the New York State Comptroller
Division of Local Government and School Accountability
110 State Street, 12th Floor, Albany, New York 12236

Tel: (518) 474-4037 • Fax: (518) 486-6479 • Email: localgov@osc.ny.gov

www.osc.state.ny.us/local-government

Local Government and School Accountability Help Line: (866) 321-8503

BUFFALO REGIONAL OFFICE – Melissa A. Myers, Chief Examiner

295 Main Street, Suite 1032 • Buffalo, New York 14203-2510

Tel (716) 847-3647 • Fax (716) 847-3643 • Email: Muni-Buffalo@osc.ny.gov

Serving: Allegany, Cattaraugus, Chautauqua, Erie, Genesee, Niagara, Orleans, Wyoming counties

Like us on Facebook at facebook.com/nyscomptroller
Follow us on Twitter @nyscomptroller