

Port Jervis City School District

Financial Condition

NOVEMBER 2022



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

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Report Highlights

Port Jervis City School District

Audit Objective

Determine whether the Port Jervis City School District (District) officials and Board of Education (Board) effectively managed the District's general fund financial condition.

Key Findings

The Board and District officials did not effectively manage the District's financial condition. As a result, the District levied more taxes than needed to fund operations. The Board and District officials:

- Consistently overestimated general fund appropriations by an average of \$5.8 million each year from 2017-18 through 2020-21 and appropriated \$4.8 million of fund balance that was not used.
- As of June 30, 2021, maintained a recalculated surplus fund balance totaling \$23.6 million, exceeding the 4 percent statutory limit by 26 percentage points or \$20.4 million. We project that the District will generate another operating surplus of approximately \$9.3 million in 2021-22 and will not need to use \$903,000 in appropriated fund balance.
- Made unbudgeted year-end transfers to reserves and the capital projects fund totaling \$12.8 million and \$15.5 million, respectively. As a result, officials did not present the District's budget or fund balance in a transparent manner.

Key Recommendations

- Adopt realistic budgets and reduce surplus fund balance to comply with the statutory limit.
- Budget for the funding of reserves and capital projects rather than rely on unbudgeted transfers of year-end operating surpluses.
- Ensure that designated reserve funds are used to fund related expenditures.

District officials agreed with our recommendations and plan to take corrective action. Appendix B includes our comment on the District's response.

Background

The District serves the City of Port Jervis and the Towns of Deer Park and Mount Hope in Orange County and the Towns of Forestburgh and Mamakating in Sullivan County.

The elected nine-member Board is responsible for managing 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 Board, Superintendent and Assistant Superintendent for Business are responsible for developing and monitoring the District's annual budget.

Quick Facts

2022-23 Budgeted Appropriations	\$82.3 million
Operating Surplus July 1, 2017 through June 30, 2021 (excluding unplanned transfers)	\$23.3 million
Surplus Fund Balance as of June 30, 2021	\$18.3 million

Audit Period

July 1, 2020 – April 30, 2022. We extended the scope back to July 1, 2017 to perform trend analysis and forward to June 30, 2022 to review reserve fund activity.

Financial Condition Management

How Can a Board Adopt Realistic Budgets and Properly Manage Fund Balance?

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 and school district officials must estimate the amount a school district will spend and receive and the amount of fund balance that may be available at fiscal year-end to determine the expected tax levy. Accurate budget 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.

Fund balance represents the cumulative residual resources from prior fiscal years. School districts are 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 ensuing year's budgeted appropriations. 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. 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 is appropriated.

The Board and District Officials Overestimated Appropriations

We compared general fund budgeted appropriations and estimated revenues with actual operating results for 2017-18 through 2020-21 to determine whether budget estimates were reasonable. We found that while estimated revenues were generally reasonable, appropriations were overestimated by an average of \$5.8 million (8.6 percent) each year, or a total of more than \$23 million (Figure 1).

Figure 1: Overestimation of General Fund Appropriations by Year, in Millions^a

	2017-18	2018-19	2019-20	2020-21	Totals
Appropriations	\$70.2	\$72.2	\$75.2	\$75.4	\$293.1
Actual Expenditures	67.3	69.6	84.7	66.4	288.0
Less: Unplanned Year-End					
Transfers of Operating Surplus^b	0.4	2.5	\$5.3	0	18.2
Overestimated Appropriations	\$3.2	\$5.1	\$5.8	\$9.0	\$23.2
Percentage Overestimated	4.8%	7.6%	8.4%	13.6%	
Average overestimated appropriations over last 4 completed fiscal years					\$5.8
Average overestimated appropriations over last 4 completed fiscal years in %					8.6%

a) Some of the calculations do not foot due to rounding.

b) The District's practice of making unbudgeted transfers at fiscal year-end to reduce operating surplus gives the appearance that total operating expenditures were more in line with budgeted expenditures than they actually were. We backed out these unbudgeted transfers to accurately reflect budgeted versus actual operating expenditures.

The most significant overestimated appropriations were for:

- Teachers' and Other Union Employees' Salaries
- Board of Cooperative Educational Services (BOCES) Student Tuition Costs
- Contractual Expenditures for Transportation (Buses)
- Health Insurance
- Retirement

These appropriations were overestimated by a total of \$15.4 million from 2017-18 through 2020-21. Based on actual expenditures as of April 30, 2022,¹ District officials overestimated these appropriations for the 2021-22 fiscal year; District records indicate the overestimation may be approximately \$8.7 million.

The former Superintendent indicated that budgeting practices included provisions for 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. However, appropriations were consistently overestimated for these expenditures year after year. For example, appropriations for health insurance costs were overestimated by \$308,405 in 2020-21 despite being overestimated by approximately \$556,000 in 2019-20. In addition, budgeted appropriations for teachers' salaries were consistently overestimated by an average of \$900,140 per year within our audit period.

The former Superintendent further indicated that many budgeted appropriations were overestimated due to pandemic-related circumstances. For example, District officials stated that due to the COVID-19 pandemic (pandemic), there was a reduction in the number of students attending BOCES, which resulted in expenditures for BOCES being less than expected. Similarly, transportation expenditures were much less than anticipated because students were not transported to school during the remote learning period. According to District officials, teachers' salaries were also affected by the pandemic as the District had a reduction in teachers, which resulted in appropriations for salaries being overestimated for the last three fiscal years. However, the pandemic would not have been a factor in overestimated appropriations during the 2017-18 and 2018-19 fiscal years.

District officials should consider historical trends and other known factors when developing budget estimates for expenditures. 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

¹ See *Appendix C* for further details regarding how we projected expenditures for the 2021-22 fiscal year.

rather than consistently overestimating appropriations. The Board should adopt more accurate estimates of anticipated expenditures to help ensure that the real property tax levy is not greater than necessary.

By consistently overestimating appropriations, the District was not transparent with taxpayers. Although District officials have not raised the tax levy in recent fiscal years, they had the opportunity to decrease the tax levy, but did not, and maintaining the same tax levy has contributed to the accumulation of significant surplus fund balance.

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

A pattern of overestimating appropriations resulted in the District generating operating surpluses from 2017-18 through 2020-21 totaling \$23.3 million, averaging \$5.8 million per year. This resulted in appropriated fund balance totaling \$4.8 million from 2017-18 through 2020-21 that was not actually used to finance operations (Figure 2).

Figure 2: Results of Operations and Appropriated Fund Balance, in Millions^a

Fiscal Year	Revenues	Expenditures ^b	Operating Surplus	Appropriated Fund Balance	Operations Better than Budgeted
2017-18	\$70.2	\$67.0	\$3.2	(\$1.1)	\$4.3
2018-19	72.3	67.1	5.2	(1.1)	6.3
2019-20	75.2	69.3	5.8	(0.9)	6.7
2020-21	75.5	66.4	9.2	(1.7)	10.8
Total	\$293.2	\$269.8	\$23.3	(\$4.8)	\$28.1
a) Some of the calculations do not foot due to rounding.					
b) Excluding unplanned transfers					

In an attempt to mitigate significant operating surpluses, District officials made year-end transfers of operating surpluses to reserves and the capital projects fund, instead of planning for the funding of reserves and the capital projects fund through the budget preparation process. For example, in the 2019-20 fiscal year, the Board approved a year-end transfer of \$15,325,000 to the capital projects fund to reduce a \$5,810,100 operating surplus to a \$9,514,900 operating deficit. By not including transfers of operating surpluses in the voter-approved budgets, District officials did not present the District’s surplus and overall financial condition in a transparent manner.

Based on our review of the 2021-22 budget and year-to-date operating results as of April 30, 2022, we project that the District will generate another operating

surplus of approximately \$9.3 million in 2021-22 and will not need to use the \$903,000 in fund balance appropriated in the budget.

Annually appropriating fund balance that is not needed to fund operations is, in effect, a reservation of fund balance that is not provided for by statute and circumvents the statutory limit imposed on the level of surplus fund balance. By continually appropriating fund balance that is not needed or used, and overestimating budgeted expenditures, the District is not presenting its fund balance or budget in a transparent manner.

Surplus Fund Balance Exceeded the Statutory Limit

The District's reported surplus fund balance in the general fund exceeded the 4 percent statutory limit from 2017-18 through 2020-21. As of June 30, 2021, surplus fund balance totaled \$18.3 million, or 23 percent of the 2021-22 budgeted appropriations (Figure 3), which exceeded the statutory limit by approximately \$15.2 million, or 19 percentage points.

Figure 3: Surplus Fund Balance as a Percentage of Ensuing Year's Budget, in Millions

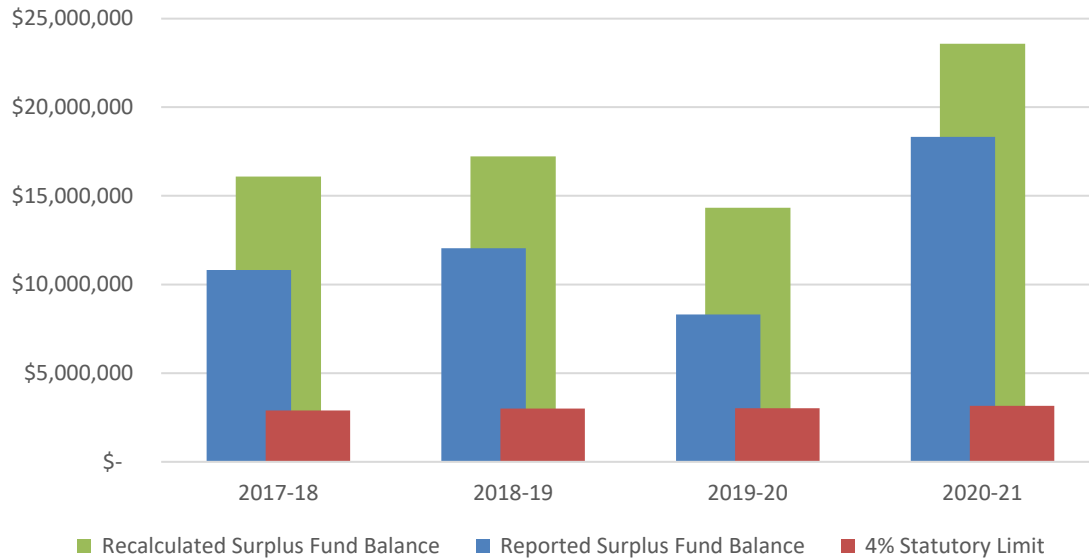
Year	Surplus Fund Balance	Ensuing Year's Budgeted Appropriations	Excess Fund Balance %
2017-18	\$10.8	\$72.2	15.0%
2018-19	\$12.0	\$75.2	16.0%
2019-20	\$8.3	\$75.4	11.0%
2020-21	\$18.3	\$79.0	23.2%

When unused appropriated fund balance and unused workers' compensation and capital reserve funds² totaling \$5.25 million are added back, the recalculated surplus fund balance of \$23.6 million exceeds the 4 percent statutory limit by 26 percentage points, or \$20.4 million (Figure 4).

² See section entitled *Reserves Were Not Always Funded or Used Properly* for further details.

FIGURE 4

Recalculated Surplus Fund Balance By Year



The Assistant Superintendent for Business indicated that he felt maintaining a fund balance of 4 percent would leave the District financially vulnerable should any major or emergency expense arise. Further, he indicated that fund balance increased significantly in the past few years during the pandemic because the District, being a high-needs district, received more State and federal aid than anticipated, resulting in significant operating surpluses. District revenues are primarily funded by aid and real property taxes.

At the beginning of the pandemic, District officials were under the impression that State aid was to be reduced by 20 percent, which would have disproportionately affected the District. The resulting unanticipated influx of aid money resulted in significant surpluses. However, we found that operating surpluses were not driven by unanticipated revenues and State aid was only underestimated by an average of \$67,794 during fiscal years 2017-18 through 2020-21. Similarly, real property taxes (including STAR reimbursements) were overestimated by an average of \$14,666 during the same fiscal years.

By maintaining surplus fund balance in excess of the statutory limit, District officials withheld funds from productive use, which resulted in property taxes being higher than necessary. While surplus fund balance continued to increase, District officials maintained the tax levy instead of reducing taxes to ease taxpayer burden. Had the Board and District officials developed and adopted more reasonable budgets, they could have considered using these excess funds to fund one-time expenditures, such as the District's current school building

renovations, and/or needed reserves, pay off debt or reduce the tax levy. Maintaining fund balance within statutory limits would mean the District would have approximately \$3.2 million in surplus fund balance to cover unanticipated expenditures.

How Should a Board Ensure Reserves Are Properly Managed and Funded?

A board may establish reserves to restrict a portion of fund balance in accordance with statutory requirements to provide financing for specific purposes. To ensure transparency and as a matter of best practice, a board should adopt a formal written policy that communicates the board's purpose for each reserve, optimal funding goals, and conditions under which the assets will be used and replenished. Ideally, amounts to be placed in reserve funds should be included in the annual budget. Therefore, the board should develop a plan for future funding and use of reserve funds. By making provisions to raise resources for reserve funds explicit in the proposed budget, the board gives voters and residents an opportunity to know the board's plan for funding its reserves.

New York State Education Law Section 3653 requires a board to expressly authorize by resolution money transferred into any reserve fund for the purpose of increasing the funding of such reserve fund. Generally, school districts are not limited as to how much money can be held in reserves; however, reserve balances should be reasonable and supported. Thus, the board should periodically analyze the reasonableness of the balances in its reserves based upon the district's needs and historical usage. Money set aside in reserves must be used only in compliance with statutory provisions which determine how reserves are established and how they may be funded, expended and discontinued.

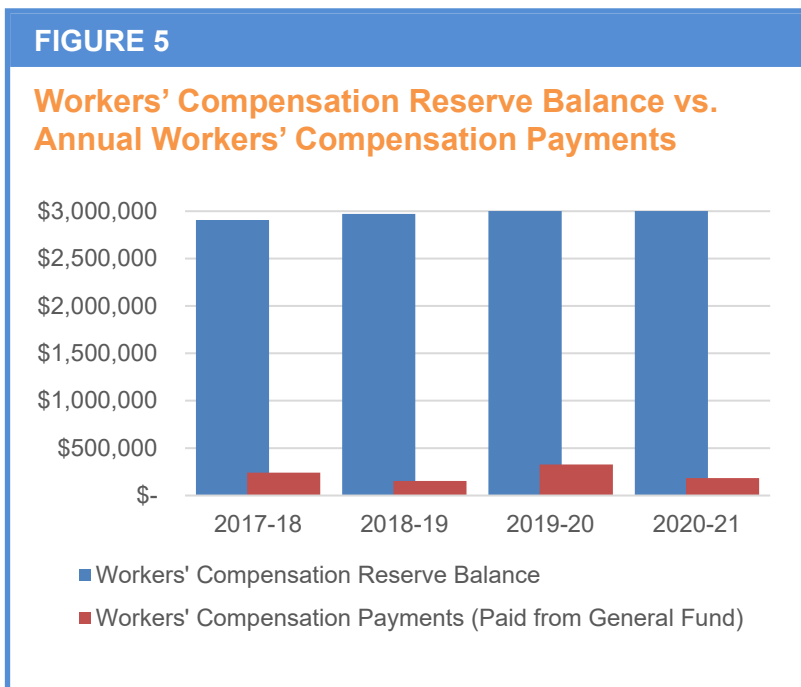
Reserves Were Not Always Funded or Used Properly

The Board did not ensure that reserves were funded in a transparent manner. From fiscal years 2017-18 through 2020-21, the Board approved year-end transfers totaling \$2.7 million to fund the District's employee benefits and capital project reserves. This funding was not planned for in the District's budget, but instead funded with unplanned year-end transfers of operating surpluses.

The former Superintendent indicated that the funding of reserves has historically been done periodically at year-end with available operating surpluses rather than being budgeted for. They have continued this practice, presumably to mitigate excessive operating surpluses. At the end of fiscal year 2021-22, the District transferred \$10,067,435 to a capital reserve alleviating a potential operating surplus for the year.

By not making provisions to raise resources for reserve funds explicit in the proposed budget, the Board failed to provide transparency to voters and residents to know the Board's plan for funding its reserves.

Also, the Board did not ensure that reserve funds were used to finance related District expenditures. For example, from fiscal years 2017-18 through 2020-21, District officials paid \$904,236 in workers' compensation claims using general fund appropriations, despite sufficient funds existing in the District's workers' compensation reserve (Figure 5).



The Treasurer indicated that historically, workers' compensation payments were made from general fund appropriations instead of using workers' compensation reserve funds and current District officials continued this past practice. Given the intention of the District officials is to finance workers' compensation payments with general fund appropriations, it is questionable as to why the officials would maintain a workers' compensation reserve.

By not using reserve funds and instead relying on general fund appropriations to finance workers' compensation expenditures, the District financed \$904,236 in workers' compensation expenditures between 2017-18 and 2020-21 through budgeted appropriations raised by property taxes instead of designated workers' compensation reserve funds.

We also determined that the District maintained a dormant capital reserve fund established in 1993 for a prior capital project. As of June 30, 2021, the reserve

balance totaled more than \$1.3 million. District officials were unaware of how old the reserve was or for what project the reserve had been established. From fiscal years 2017-18 through 2020-21, the reserve had no activity besides the accrual of interest.

The Treasurer indicated that the reserve fund was not being used because they were unaware of how to liquidate the remaining capital project reserve funds after completion of the related project. She also indicated that an attorney was consulted prior to our audit scope who was unable to provide guidance on how to liquidate the reserve funds to another reserve or to the District's general fund.

Additionally, although the District had a reserve fund policy, it did not state how much should be set aside, how each reserve would be funded, or when the reserve funds should be used. As a result, District officials did not have clear guidance on the purpose for each reserve, optimal funding goals, and conditions under which the assets would be used and replenished. Further, by failing to reallocate excess reserve funds from prior capital projects to fund current District liabilities or capital projects, the District placed an additional unnecessary tax burden on taxpayers.

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. Discontinue the practice of appropriating fund balance that is not needed or used to fund operations.
3. 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 such as capital projects,
 - Funding needed reserves, and
 - Paying off debt.
4. Review all reserves and determine if the amounts reserved are necessary and reasonable. To the extent that they are not, transfers should be made to unrestricted fund balance, where allowed by law, or to other reserves established and maintained in compliance with statute.

-
5. Plan for the funding of reserves and capital projects fund during the budget process rather than through year-end transfers of operating surplus to improve the transparency of reserve funding.
 6. Revise the reserve fund policy to include clear guidance on the purpose for each reserve, optimal funding goals, and conditions under which each reserve will be used and replenished.

Appendix A: Response From District Officials



Port Jervis
CITY SCHOOL DISTRICT

Administrative Offices
9 Thompson Street
Port Jervis, New York 12771
District Office Tel 845-858-3100

Proud Past, Bright Future

Dr. John Bell, Superintendent of Schools ~ John Timm, Asst. Superintendent for Business ~ Dr. Natasha Walkowicz, Asst. Superintendent for Instruction

November 1, 2022

Dara Disko-McCagg
Chief Examiner, Newburgh Regional Office
33 Airport Center Drive, Suite 103
New Windsor, NY 12553

Dear Ms. Disko-McCagg,

The Port Jervis City School District is in receipt of the State Comptroller's Office Draft Report of Examination for Financial Condition for the period July 1, 2017 through June 30, 2022. On behalf of the District, I would like to thank the Comptroller's Office, who we found to be professional and courteous throughout the audit process. As always, the District welcomes feedback, and appreciates the opportunity to improve its practices based on reflection of your observations.

The District is pleased that the report does not suggest any malfeasance or legal impropriety with respect to general business operations. To the extent the Comptroller's audit represents a review of the operations, practices, and policies for compliance, the District generally agrees with the findings.

See
Note 1
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The District looks forward to submitting its Corrective Action Plan, identifying our plan to correct the findings and implement the recommendations in our finalized audit report.

Sincerely,


Dr. John J. Bell
Superintendent of Schools

Appendix B: OSC Comment on the District's Response

Note 1

We did not audit the District's general business operations. The audit focused on the District's management of general fund financial condition. Therefore, the audit cannot be used to draw any conclusions on other District business operations.

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 policies to gain an understanding of the District's controls over budgeting and fund balance and reserves management.
- We reviewed the adopted general fund budgets from 2017-18 through 2020-21 to determine whether they were reasonable and structurally balanced by comparing adopted budgets with actual results of operations.
- We reviewed 2020-21 operating results and compared them to operating results as of April 30, 2022. To estimate operating results for 2021-2022, we projected revenues and expenditures as of April 30, 2022 by using the percentage of revenues received and expenditures made as of April 30, 2021 in comparison to year-end actuals.
- We calculated surplus fund balance as a percentage of the ensuing year's budgeted appropriations for 2017-18 through 2020-21 to assess the District's compliance with statutory requirements.
- We recalculated surplus fund balance as a percentage of the ensuing year's budgeted appropriations after adding back unused appropriated fund balance and unsupported or unused reserve funds or unplanned end-of-year transfers.
- We examined Board resolutions, bank statements and reserve accounting records to determine if reserves were legally established, funded and properly used and if balances were maintained in accordance with statutory requirements.
- We compared reserve balances with expenditures from 2017-18 through 2020-21 to determine the reasonableness of reserve balances.

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.

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.

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

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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

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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

NEWBURGH REGIONAL OFFICE – Dara Disko-McCagg, Chief of Municipal Audits

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