

Sharon Springs Central School District

Fund Balance Management

SEPTEMBER 2022



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

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Report Highlights

Sharon Springs Central School District

Audit Objective

Determine whether the Sharon Springs Central School District (District) Board of Education (Board) and officials effectively managed fund balance.

Key Findings

The Board and District officials did not effectively manage fund balance, and need to improve their budgeting practices and be more transparent with District residents and taxpayers. During the audit period, the Board and District officials:

- Annually overestimated appropriations by an average of \$1.6 million, or 17 percent.
- Informed residents and taxpayers the District would incur operating deficits totaling \$3.7 million but had operating surpluses totaling \$1.6 million.
- Allowed recalculated surplus fund balance to exceed the statutory limit by \$2.3 million, or 23.7 percentage points.

Annually overestimating appropriations and 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 circumvents the statutory limit. Although real property tax levies remained relatively flat during the audit period, maintaining surplus fund balance that exceeds the statutory limit results in tax levies being higher than necessary.

Key Recommendations

- Adopt budgets that include reasonable estimates for appropriations and the amount of fund balance that will be used to fund operations.
- Reduce surplus fund balance to comply with the statutory limit and use excess funds in a manner that benefits District taxpayers.

District officials generally agreed with our findings and indicated they plan to initiate corrective action.

Background

The District serves the Towns of Carlisle, Seward and Sharon in Schoharie County; the Towns of Cherry Valley and Roseboom in Otsego County; and the Towns of Canajoharie and Root in Montgomery County.

The District is governed by an elected seven-member Board responsible for the general management and control of the District's financial and educational affairs. The Superintendent of Schools (Superintendent) is the 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 Business Manager and Superintendent prepare the annual budget and present it to the Board for approval.

Quick Facts

2020-21 Total Fund Balance	\$4.3 million
2021-22 Budgeted Appropriations	\$9.9 million

Audit Period

July 1, 2018 – March 31, 2022.

We expanded our audit period through June 27, 2022, to review the building improvement capital project bond resolution.

Fund Balance Management

How Should Officials Effectively Manage Fund Balance?

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

A school district may retain a portion of surplus fund balance for cash flow needs or unexpected expenditures.¹ New York State Real Property Tax Law Section 1318 currently limits the amount of surplus fund balance that a school district can retain to no more than 4 percent of the next year's budgeted appropriations. Any surplus fund balance over this percentage must be used to reduce the next year's real property tax levy or fund needed reserves. When fund balance is appropriated in the budget to finance operations, a school district is budgeting for a planned operating deficit (expenditures exceeding revenues) equal to the amount of fund balance appropriated.

The Board Overestimated Appropriations

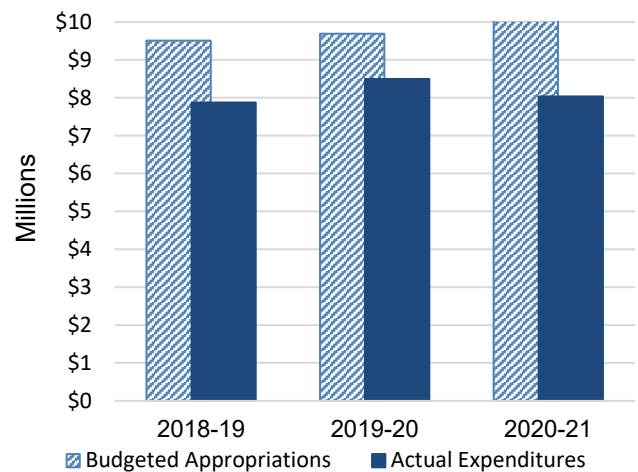
We compared estimated revenues and budgeted appropriations with actual operating results between 2018-19 and 2020-21. We found that estimated revenues were generally reasonable, but budgeted appropriations were overestimated by an average of \$1.6 million, or 17 percent (Figure 1).

In aggregate, these variances contributed to an increase in surplus fund balance over the past three years. For example, during this period, the Board overestimated expenditures for the:

- New York State Teachers' Retirement System each year by an average of \$168,000 (41 percent),

FIGURE 1

Comparison of Budgeted Appropriations to Actual Expenditures



¹ Surplus fund balance is defined as unrestricted fund balance minus appropriated fund balance and encumbrances included in committed and assigned fund balance. Refer to our accounting bulletin at <https://osc.state.ny.us/localgov/pubs/releases/gasb54.pdf>.

- Board of Cooperative Educational Services (BOCES) contractual teaching services by an average of \$127,000 (35 percent) and
- Electricity by an average of \$104,000 (63 percent).

According to the Business Official, these overestimations were caused by the District not being able to fill open positions, not receiving estimates from BOCES in a timely manner and the District joining an energy consortium that reduced energy bills. However, the District joined the energy consortium in 2015, several years before the beginning of our audit period.

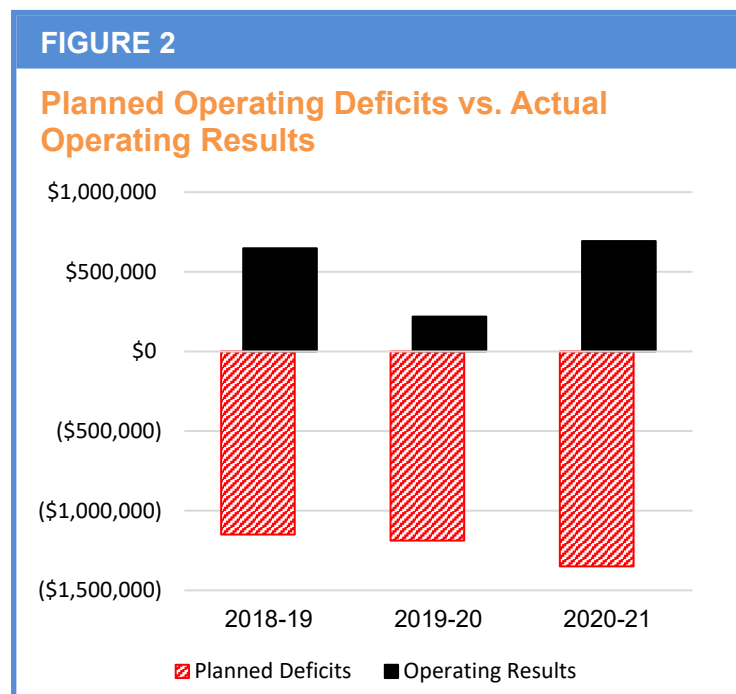
Because the Board and District officials overestimated appropriations, it appeared that more revenue and financing sources (fund balance) were needed to maintain a structurally balanced budget and address operating deficits (more expenditures than revenues), despite historical trends showing otherwise. Had the Board and officials used previous years' actual results of operations to develop their budget estimates, they would have likely estimated more accurately.

The Board Appropriated Unneeded Fund Balance and Exceeded the Statutory Limit

The Board appropriated fund balance totaling \$3.7 million over the last three fiscal years. However, the Board's budgeting practices resulted in variances that offset the planned operating deficits created by the amounts appropriated. As a result, the District incurred operating surpluses totaling \$1.6 million (Figure 2).

Furthermore, District officials reported surplus fund balance that exceeded the 4 percent statutory limit in two of the last three fiscal years. As of June 30, 2021, surplus fund balance was 14 percent of the next year's budgeted appropriations. After adding back unused appropriated fund balance, recalculated surplus fund balance is 27.7 percent (Figure 3). The Business Official, Superintendent and Board President were aware of the District's surplus fund balance.

According to the Business Official, the District's expenditures, including utilities, cleaning staff, fuel, education and sports programs, and BOCES expenditures, decreased as a result of the COVID-19 pandemic. Based on our review of annual expenditures, we confirmed that utilities, fuel and BOCES expenditures decreased over the three-year period. However, the District's operating surplus in



2018-19 (prior to the COVID-19 pandemic) was larger than the operating surplus in 2019-20 and nearly as large as the operating surplus in 2020-21.

Figure 3: Surplus Fund Balance

	2018-19	2019-20	2020-21
Reported by Officials	\$388,000	\$856,000	\$1,387,000
Add: Unused Appropriated Fund Balance	1,188,000	1,350,000	1,346,000 ^a
Recalculated by OSC	\$1,576,000	\$2,206,000	\$2,733,000 ^a
Percentage of Next Year’s Budgeted Appropriations - Legal Limit 4%			
Reported by Officials	4.0%	8.5%	14.0%
Recalculated by OSC	16.3%	22.0%	27.7% ^a

a) We estimated the appropriated fund balance that will not be used to finance the 2021-22 fiscal year based on the previous three-year total of unused appropriated fund balance as a percentage of total budgeted appropriated fund balance.

Annually 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 circumvents the statutory limit imposed on the level of surplus fund balance. Although real property tax levies remained relatively flat during these years, maintaining surplus fund balance that exceeds the statutory limit results in tax levies being higher than necessary. In addition, including appropriated fund balance in the annual budgets that have a history of not being needed or used does not afford a transparent budget process to taxpayers. District officials plan to use \$500,000 of surplus funds, as outlined as a funding source in a Board-approved bond resolution on June 27, 2022, to finance a building improvement capital project approved in the 2022-23 budget.

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 in a manner that benefits District taxpayers. Surplus funds can be used for:
 - Funding one-time expenditures such as capital improvements,
 - Funding needed reserves,
 - Paying off debt, and/or
 - Reducing District real property taxes.

Appendix A: Response From District Officials



Sharon Springs Central School

PO Box 218, 514 State Route 20
Sharon Springs, New York 13459

District Office
518-284-2266
Fax 518-284-9033

Main/Guidance Office
518-284-2267
Fax 518-284-9075

Bus Garage
518-284-9047
Fax 518-284-9073



September 21, 2022

Ann C. Singer, Chief Examiner
Office of the New York State Comptroller
Division of Local Government and School Accountability
State Office Building, Suite 1702
44 Hawley Street
Binghamton, New York 13901-4417

RE: Response to Preliminary Draft Findings and Formal Corrective Action Plan

Dear Ann C. Singer,

On behalf of the District, I would like to thank you for the comments and recommendations resulting from the recent OSC Fund Balance Management review. During the previous audit, there were recommendations regarding our budget philosophy and overall management of reserve balances. As a result of those recommendations, the school developed an annual review process for evaluating appropriate reserves and management of reserves. Many of the recommendations from the findings of this review are already in operation as a result of this annual review by the Board of Education. While these actions will not completely result in compliance with the legislated maximum unallocated fund balance, our periodic review through this process are moving us towards that end.

The District is very pleased that the examination has resulted in no findings of a material weakness, operational improprieties, fraud, waste, or abuse. As such, the primary focus of the audit was our Fund Balance Management, which resulted in recommendations regarding budget estimates for revenues and expenditures; and use of surplus fund balance. We respond to these recommendations as follows:

- 1. Develop and adopt budgets for appropriations and the amount of fund balance that will be used to fund operations.**

District Response and Corrective Action Plan:

The District believes that responsible budgeting requires contingencies for unexpected expenditures. It has always been the practice of the District to be conservative when estimating certain expenditures over which the district has little control such as fuel and utility costs, Special Education placements, staffing requirements and transportation costs. We acknowledge that being conservative with all of these expenditures will likely result in unexpended budget numbers, but we continue to believe it is best to estimate a “worst case scenario”, whereby giving our voters the choice to approve the budget as is and accept that if we were to expend all of the money in the budget it would result in expending the amount allocated from fund balance.

2. Discontinue the practice of appropriating fund balance that is not needed or used to fund operations.

The District has always believed that conservative Revenue forecasting is necessary. In 2011, the State imposed the “Gap Elimination Adjustment”, which resulted in more than \$1.7 million loss in aid over a 5-year period. The school was fortunate to have the proper planning in place to be able to survive fiscally during that period without sacrificing program. Sharon Springs is highly dependent on State aid, with 56% of our current budget being funded through total State aid. A shift in aid could be very difficult for the District to recover from. Under the current State Aid formulas, Sharon Springs is considered a fully funded school. Over the past two years, the State has adjusted its formula for State Aid to ensure the “underfunded” schools become fully funded under the complex State Aid calculations and fully funded schools have received minimal increases.

While the District does not dispute the findings of the field staff of the Comptroller’s Office, we believe a cautious approach should be taken to reduce budgeted contingencies for unexpected expenditures and revenue forecasting. We will continue to implement a thorough budget process whereby expenditures can be identified and appropriate budget allocations can be made. The implementation of this plan is immediate and will be continuous with each budget process.

3. Develop a plan to reduce surplus fund balance in a manner that benefits District taxpayers.

A. The Comptroller’s Office recommends “one-time expenditures such as capital improvements”.

Through our annual and periodic review of reserves, the Board of Education has already acted appropriately with a capital project (\$500,000) approved by the taxpayers on May 17, 2022, and an emergency project (\$175,000) approved by the Board on: August 8, 2022. While these transfers will reduce current unallocated fund balance immediately, the State Aid associated with this will return a portion of these funds over the legislated time periods. It should be noted that this process will immediately impact unallocated fund balance; however, the District will need to continue to consider the impact on future building aid.

B. The Comptroller's Office recommends "Funding needed reserves".

We are working on bringing the 2021-22 fiscal audit to a close and the Board of Education has approved a transfer \$47,330 to the Insurance Reserve; \$51,009 to the Teacher Retirement Reserve (still to be funded, but there are legislated caps on annual contributions); and \$150,000 to the Employee Benefits Reserve. After all of these transfers are made, the unassigned/unallocated fund balance will be \$1,053,966.

C. The Comptroller's Office recommends "paying off debt".

This is a complex recommendation that the district will continue to consider in line with our regular review of fund balance. First, paying off debt can be complicated, as the districts bonds/debt that has been issued is not "callable" or allowed to be paid early. Additionally, paying off debt has implications on long term planning in terms of future property tax cap calculations, and other budgetary considerations. The District will evaluate all of the implications, and determine if there is action that can be taken to benefit the District and our tax payers.

D. The Comptroller's Office recommends "reducing real property taxes".

The District's tax levy for 2022-23 is \$2,399,766. The tax levy in 2010-12 was \$2,403,485. Over the last 10 years, the Board has not increased the tax levy. Reducing the tax levy can be uncorrectable for a district in a year where there is no surplus fund balance to fund it in future years. While we understand this is an alternative solution, we believe that would be a short-term fix that could cause future irreversible implications.

In closing, I would like to once again thank the field staff of the Comptroller's Office for their kind and professional assistance throughout the examination process. If you should have any further questions or problems with our response, please feel free to contact me any time.

Very truly yours,

Thomas Yorke
Superintendent of Schools

TAY:AMD:kb
PC: Board of Education

Appendix B: 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 and policies to gain an understanding of the financial management policies and procedures.
- We reviewed the adopted general fund budgets from 2018-19 through 2020-21 to determine whether they were reasonable and structurally balanced by comparing adopted budgets with actual results of operations.
- We calculated surplus fund balance as a percentage of the next year's appropriations for 2018-19 through 2020-21 to determine whether it was within the statutory limit.
- We recalculated surplus fund balance as a percentage of the next year's appropriations by adding back the unused appropriated fund balance for 2018-19 through 2020-21. We estimated the amount of unused appropriated fund balance to finance the 2021-22 fiscal year based on the previous three-year total of unused appropriated fund balance as a percentage of total budgeted appropriated fund balance.

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 C: Resources and Services

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

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