



Chatham Central School District

Financial Management

2023M-11 | August 2023

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Report Highlights

Chatham Central School District

Audit Objective

Determine whether the Chatham Central School District (District) Board of Education (Board) and District officials properly managed fund balance and reserves.

Key Findings

The Board and District officials did not properly manage fund balance and reserves. The Board and District officials' consistent practice of appropriating fund balance that is not needed and maintaining unreasonable reserve balances circumvents the statutory limit on surplus fund balance and lacks transparency. The Board and District officials:

- Annually appropriated over \$1.3 million of fund balance they did not need or use to finance operations; therefore, taxpayers were taxed more than necessary.
- On average, annually over-estimated appropriations by \$3.2 million (9.9 percent).
- Maintained four reserves totaling \$6.6 million without demonstrating they were reasonably funded. For example, the
 - Unemployment insurance reserve has about \$747,000, enough to pay annual claims for 14 years.
 - Workers' compensation reserve has \$1.4 million, but the average annual workers' compensation expense is \$79,756.

Key Recommendations

- Use reasonable appropriation estimates and do not appropriate fund balance that is not needed.
- Maintain reserves at reasonable levels.

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.

Background

The Office of the State Comptroller (OSC) issued a prior audit report on the District's financial condition in October 2015. The audit found the District appropriated fund balance that was not used and overfunded reserves.

The District serves the Towns of Chatham, Ghent, Canaan, Austerlitz, Kinderhook and New Lebanon in Columbia County. The seven-member Board is responsible for managing and controlling 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 School Business Administrator (Administrator) oversees the District's Business Office and maintains its financial records. The Board, Superintendent and Administrator are responsible for developing the budget.

Quick Facts (Millions)

2022-23 Appropriations	\$33.6
Overestimated Appropriations	
2019-20	\$2.7
2020-21	\$3.3
2021-22	\$3.6
Total Reserves As of June 30, 2022	
10 Reserves	\$15.7

Audit Period

July 1, 2019 – September 30, 2022

Financial Management

How Should Fund Balance Be Properly Managed?

A school board should adopt realistic and structurally balanced budgets based on historical data or known trends in which recurring revenues finance recurring expenditures to properly manage fund balance. In preparing the budget, a school board and school district officials must estimate the amounts a school district will spend and receive, the amount of fund balance available for use at fiscal year-end to use toward the next year's budget and the expected real property tax levy needed to balance the budget. Reasonable estimates should be used to help ensure the tax levy is not greater than necessary. When fund balance is appropriated to finance operations, there should be a reasonable expectation of an operating deficit equal to the amount of fund balance that was appropriated. In other words, the school district is expected to use some, if not all, of the appropriated fund balance to finance budgeted appropriations.

A school board is permitted to retain both a specified amount of fund balance for cash flow needs or unexpected expenditures, and reserves for other identified or planned needs. Officials should comply with New York State Real Property Tax Law Section 1318 that limits the amount of surplus fund balance that a school district can retain to no more than 4 percent of the next year's budget. A school board must use any surplus fund balance over this percentage to reduce the upcoming fiscal year's real property levy or fund needed reserves.

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

OSC issued an audit report¹ in October 2015 that included findings that the District annually appropriated fund balance that was not used. The Board and District officials have generally maintained surplus fund balance levels in accordance with the statutory limit by appropriating fund balance that is not needed or used to finance operations. The Board appropriated \$1.3 million of fund balance to finance operations in each of the last three adopted budgets. However, the District did not use any of the appropriated fund balance because the Board adopted budgets that annually overestimated appropriations by an average of approximately \$3.2 million (approximately 10 percent) per year, or a cumulative total of \$9.6 million (Figure 1).

¹ Chatham Central School District *Financial Condition (2015M-161)*.

Figure 1: Overestimated Appropriations (in Millions)

	2019-20	2020-21	2021-22	Total
Appropriations^a	\$31.5	\$32.1	\$33.1	\$96.7
Less: Adjusted Expenditures^b	\$28.8	\$28.8	\$29.5	\$87.1
Overestimated Appropriations	\$2.7	\$3.3	\$3.6	\$9.6
Percentage Overestimated	8.7%	10.2%	10.8%	
Average Percentage Overestimated	9.9%			

a) Includes encumbrances (prior year funds scheduled to be paid or disbursed in the current fiscal year and recorded with the current year's expenditures) and does not include budgeted transfers of real property tax revenue to the library fund. The Chatham Public Library is fully funded by the District's budget through an allocation of real property taxes and is accounted for in a separate operating fund (library fund).

b) Does not include budgeted portion of transfers to the library fund.

We examined appropriations in the 2019-20 through 2021-22 fiscal years and determined the most significant overestimated appropriations were for:

- Medical insurance,
- Dental insurance,
- Social Security,
- BOCES services and
- Out of district tuition.

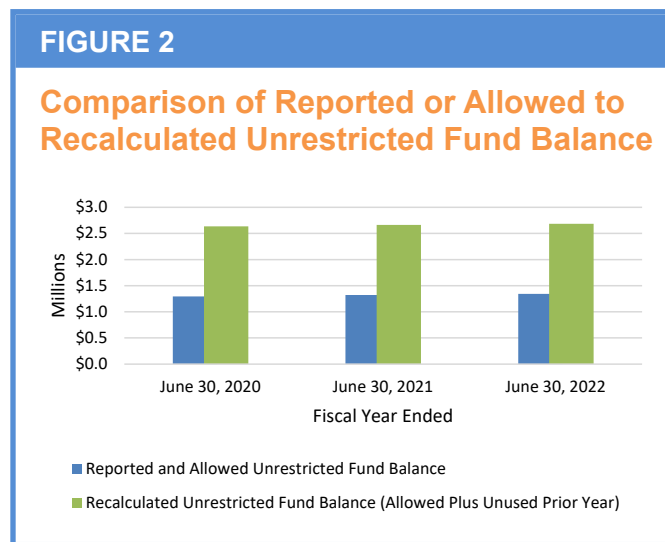
Total overestimation for these five appropriation accounts ranged between \$1.5 to \$1.8 million annually. For example, the largest overestimation was for medical insurance, averaging \$950,000 (21 percent) over the last three years. The Administrator told us that these five items are intentionally budgeted (i.e., overestimated) with 'contingencies' built in so that appropriated fund balance is not actually needed to fund operations. However, intentionally overestimating appropriations for the purpose of not using appropriated fund balance – while purporting to plan to use fund balance to cover an operating deficit – is both misleading to voters and interested parties and lacks transparency. From fiscal years 2019-20 through 2021-22, these five accounts have been significantly overestimated by a total of \$5 million (31 percent), thereby increasing the burden on taxpayers to fund these operating surpluses.

Because of the Board's misleading practice of intentionally overestimating appropriations, it appeared the District needed to use appropriated fund balance to close projected budget gaps totaling \$4 million for fiscal years 2019-20 through 2021-22. In reality, because the District's actual annual revenues were more than sufficient to cover annual expenditures, the District realized a \$6.9 million cumulative operating surplus.

The Board's and District officials' practice of historically appropriating unneeded fund balance is, in effect, a reservation of fund balance that is not provided for by statute and circumvents the statutory limit on surplus fund balance.

Additionally, appropriating fund balance that is not needed artificially reduces the amount of surplus fund balance subject to the statutory limit. For perspective, when unused appropriated fund balance is included in surplus fund balance, the District's surplus fund balance would have exceeded the statutory limit by approximately \$1.3 million or 4 percentage points in each of the last three years. Recalculated surplus fund balance ranged from \$2.6 million to \$2.7 million (8 percent) (Figure 2).

The Board adopted budgets that required fund balance totaling \$4 million to be appropriated to cover operating deficits. Instead, the unrealistic budgets resulted in a cumulative operating surplus of \$6.9 million and a cumulative budget variance (difference between budgeted and actual revenues and expenditures) of \$11.8 million over the three years reviewed.



Had the Board and District officials adopted more reasonable estimates for appropriations, they could have considered using excess funds towards paying one-time expenditures and/or funding needed reserves or reducing the tax levy. Furthermore, despite realizing annual operating surpluses, the Board continued to increase the tax levy by an average \$344,382, or 1.6 percent each year.

How Should the Board Properly Manage Reserves?

A school board should balance the intent for accumulating funds for identified future needs with the obligation to ensure real property taxes are not higher than necessary. School districts are allowed to establish reserves and accumulate funds for certain future purposes (e.g., unemployment or retirement expenditures). While school districts are generally not limited to the amount of funds that can be held in reserves, a board should ensure reserve balances are reasonable.

A school board should appropriately allocate funds to specific reserves for the reserves' intended purposes. To help ensure that reserve balances do not exceed the amount necessary to address long-term obligations or planned expenditures, a school board should adopt a comprehensive written policy clearly stating its rationale for establishing reserve funds and the objectives for each reserve, reasonable maximum funding levels, how and when the reserves will be utilized, and a periodic review of reserve balances to assess reasonableness. Reserve funds should not be merely a location to accumulate unneeded excess cash or fund balance.

Reserves Were Not Properly Managed, Were Overfunded and Were Not Being Used

OSC's prior District audit report included findings that the District overfunded its employee benefit accrued liability reserve (EBALR) and retained excessive balances in its workers' compensation, unemployment insurance, retirement contribution and insurance reserves. We found the District continues to maintain excessive balances in reserves; since our last audit, balances in reserves have grown from approximately \$5.9 million to approximately \$15.7 million, or an increase of \$9.8 million. We also found that the Board's annually adopted reserve fund policy, dated December 21, 2021, did not clearly state a reasonable rationale for maintaining reserves at their targeted levels and how and when the reserves would be used.

The Administrator provided us with the Board-adopted 2021-30 reserve plan (plan). The plan included the rationale for establishing reserves, targeted funding levels, stated rationales for those funding levels and scenarios in which the reserves could be used in the future. However, the rationale for funding levels in four of the reserves was not sufficient to support the amounts in those reserves.

OSC's prior audit recommended that officials take appropriate action to address overfunded reserves. In the District's written response to our previous audit, officials stated the District was using its reserves, and projected total balance and reserves to be at a level of approximately \$3 million by the 2021-22 fiscal year.

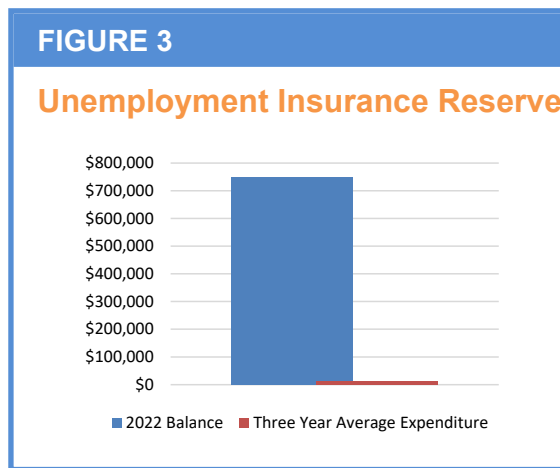
As of June 30, 2022, the District reported 10 reserves in the general fund totaling \$15.7 million. While the tax certiorari, teachers retirement contribution, and two capital reserves balances appear reasonable, these reserves are routinely funded by unplanned operating surpluses, rather than through the budget process. For example, the \$2.7 million unplanned operating surplus realized in the 2021-22 fiscal year was transferred to a newly created capital reserve. Also, the unemployment insurance, workers' compensation, employee retirement contribution and insurance reserves all had excessive balances.

[T]he rationale for funding levels in four of the reserves was not sufficient to support the amounts in those reserves.

The Board prepares and updates its plan each year in December. However, the plan lacks sufficient rationale for the funding targets and intended use of the four overfunded reserves mentioned above. Continuously funding reserves with excess fund balances results in unrestricted fund balance being reported at an artificially low level. The balances accumulated in these reserves are several times the average annual expenditure for their purpose.

Unemployment Insurance Reserve – The Board established an unemployment insurance reserve to reimburse the New York State Unemployment Fund for payments made to claimants on the District’s behalf. As of June 30, 2022, the reserve had a balance of approximately \$747,000 (Figure 3). Although District officials used only \$56,537 from the reserve since fiscal year 2019-20, they have increased the reserve by \$404,154 from fiscal year 2019-20 through 2021-22.

The plan presents possible occurrences rather than District trends, other known factors or expected needs as a justification for funding the reserve. The Board’s rationale for maintaining this reserve according to its plan is that it will help offset the cost to restructure the District’s work force if there are decreases in State aid and uncertainties regarding future State aid, property tax cap limits, enrollment decline and a stagnant economy.



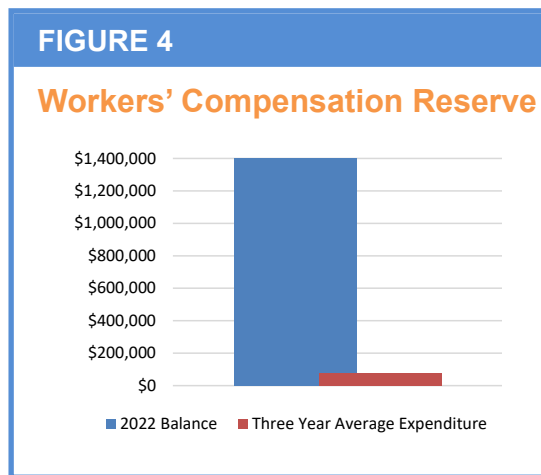
Also, the plan states that the District will continue to monitor and possibly increase this reserve in future years, as reduction in work force may be necessary to balance future budgets. However, officials could not provide an analysis that supported the current funding level. Further, their rationale does not sufficiently consider the District’s experience in paying claims and does not present a known or even sufficiently expected obligation for which funds are being accumulated.

According to the plan, the reserve balance target is 2 to 5 percent of payroll. However, the Administrator and Finance Committee Chair could not explain how the Finance Committee arrived at this target, other than stating it was a Committee decision. The unemployment insurance reserve is currently funded at 5 percent of payroll. Over the last three years, the District’s annual payment for unemployment insurance costs ranged from a low of \$0 in fiscal year 2021-22 to a high of \$52,000 in fiscal year 2020-21. Even if the District’s annual expenditures continued at \$52,000, the reserve would last more than 14 years without

replenishment. As a result, the District could, in accordance with statute, reduce the reserve to a reasonable level and use excess fund balance towards a purpose more beneficial to District taxpayers.

Workers' Compensation Reserve – The Board established a workers' compensation reserve fund to pay compensation and benefits, medical, hospital or other expenses authorized by Article 2 of the Workers' Compensation Law and to pay the costs of administering a self-insurance program. The current level of this reserve is not reasonable. From fiscal year ended June 30, 2020 to fiscal year ended June 30, 2022, the balance of the workers' compensation reserve has increased from \$1.1 million to \$1.4 million (Figure 4). Over the three years we reviewed, the District paid a total of \$239,268, averaging \$79,756 per year, for workers' compensation expenses.

The District plan does not present sufficient rationale for funding the reserve at its targeted levels of 5 to 10 percent of payroll. The Administrator stated this level of funding was a Finance Committee decision without further explanation. The plan states, "The District will hold this reserve to assist in the event a large spike occurs." It also states "A single catastrophic or serious event can cause a spike in costs that can as much as double premiums, as was experienced by another consortium member in 2016. The higher level of funding allows for such circumstances." However, the likelihood of a catastrophic event is questionable.



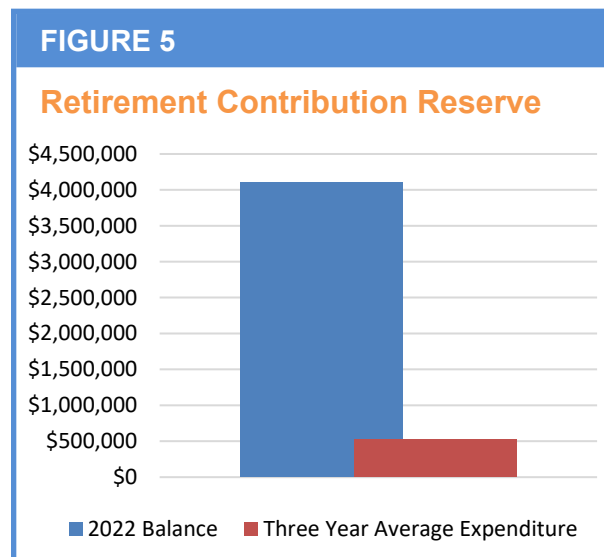
At the current level, premiums could more than double and the reserve's fund balance would be sufficient to cover the District's premiums for the next seven years, suggesting that District taxpayers may have been taxed more than necessary. As a result, the District could, in accordance with statute, reduce the reserve to a reasonable level and use excess fund balance towards a purpose more beneficial to District taxpayers.

Retirement Contribution Reserve – The Board established a retirement contribution reserve to pay retirement contributions to the New York State Local Employees Retirement System (ERS). The District plan presents a target for the balance in the reserve of 20 percent of ERS payroll multiplied by 6.34 years. The rationale presented refers to stock market declines, increasing contribution rates, and rates being based on five-year averages as justification for keeping enough of

a balance to pay contributions for five years. The plan also stated that operating surpluses in fiscal year 2020-21 were placed in the reserve and would be moved to the next capital project reserve pending voter approval. The reserves are required to be used for their stated purpose and not as a location to accumulate funds for other District purposes.

In the past three years, District officials included an annual appropriation in the adopted budgets for ERS contributions to be paid from current year revenues, and not from the retirement reserve. Further, the annual amount paid out is less than the appropriation each year. Because the District overestimates the appropriation and is able to pay the contribution amount without using reserve fund money each year, it is not reasonable to fund the reserve at the current level of \$4.1 million (Figure 5).

Furthermore, if ERS costs continue to average \$524,000 per year, as they have over the last three years, at its current funding level, the reserve would last more than seven years, suggesting that District taxpayers may have been taxed more than necessary. As a result, the District could, in accordance with statute, reduce the reserve to a reasonable level and use the excess funds for a purpose more beneficial to District taxpayers.

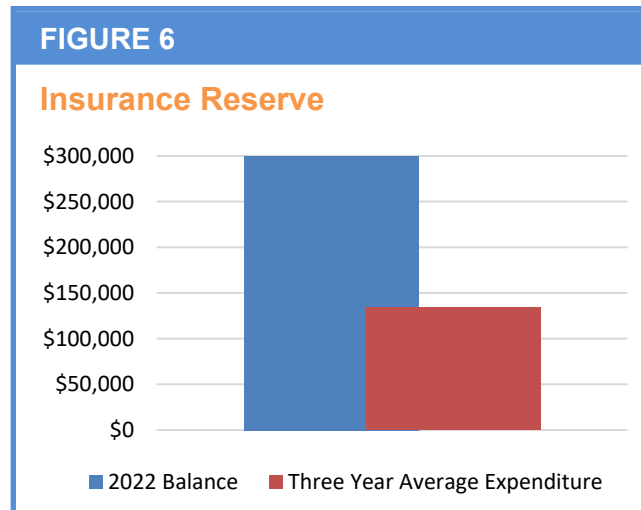


The reserves are required to be used for their stated purpose and not as a location to accumulate funds for other District purposes.

Insurance Reserve – The District’s insurance reserve was established to pay property damage costs to repair buildings that the District deems not necessary to insure due to age and condition, and any liability, casualty or other types of losses for which coverage may not be purchased. Even though the District’s insurance deductible is \$25,000 (i.e., the amount the District would pay for a covered insurance claim before the District’s insurance starts to pay), the District’s plan targets funding for this reserve between \$100,000 and \$300,000. The reserve has been funded at \$300,000 in each of the past three years (Figure 6) and no funds have been expended from it during this period. The District’s three-year average budgeted appropriation for general insurance costs was \$154,924, and the average expenditure was \$133,773. We question the need to fund this reserve at its current level, given the District budgets and pays for this expenditure as part of its annual budget, and has not expended any money from the reserve in the past three years.

The Administrator, Superintendent and Chair of the Finance Committee told us they feel funding reserves at current levels and conservative budgeting is sound fiscal management, and that the current plan for the excess balance in the reserves is to fund future capital projects. However, accumulating reserves with the intention to provide money for the worst-case

scenario, as stated in the District's plan – for events that may never happen – deprives the District of the use of these funds, which were raised through the District's taxpayers for specific purposes. In effect, this moves that money aside until the District decides to do something with it. As a result, the District continues to maintain excess reserve money raised through the tax levy that will not be used, which suggests more taxes are levied than necessary. Further, by overestimating appropriations to fund reserves, rather than appropriating to fund reserves for a planned use, the Board is not providing a transparent process to the taxpayers.



What Do We Recommend?

The Board 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, and will not be used, to fund operations.
3. Amend the District's plan to have more reasonable targeted funding levels of the unemployment insurance, workers' compensation and employee retirement contribution reserves.
4. Develop a plan to reduce the balances in the unemployment insurance, workers' compensation and employee retirement contribution reserves to reasonable levels. The surplus in these reserves can be used to:

-
- Fund one-time expenditures.
 - Fund needed reserves that are not already adequately funded.
 - Reduce District property taxes.
5. Consider whether an insurance reserve is necessary.
 6. Apply surplus results of operations at the end of the fiscal year in the same manner:
 - Fund one-time expenditures.
 - Fund needed reserves that are not already adequately funded.
 - Reduce District property taxes.

Appendix A: Response From District Officials



June 14, 2023

NYS Office of the State Comptroller
One Broad Street Plaza
110 State Street, 12th Floor, Albany, NY 12236
Attention: Gary Gifford

RE: Audit Response

Dear Auditor and Taxpayers of the Chatham Central School District:

The Chatham Central School District is in receipt of the Draft Audit Report *Financial Management* for the period of July 1, 2019 through September 30, 2022, prepared by the Office of the State Comptroller. On behalf of the Board of Education and the District administration, we would like to thank the Comptroller's staff for their professionalism and courtesy in conducting their duties associated with this audit.

The Chatham Central School District is committed to providing an excellent educational program that prepares students for college and career success in the 21st century. To this end, our budget development is guided by our financial reserve plan's following principles, reviewed and adopted by the Board during each year's budget calendar:

- Stability and improvements in the educational program
- Maintenance of educational programming during economic downturns
- The ability to decrease volatility in the tax levy
- Cash flows that will allow increased investment earnings
- The ability to fund non-recurring items in the budget
- A long-term plan for preserving and updating its infrastructure and school buildings
- The ability to maintain and/or improve its bond rating, which will save taxpayers money at both the local and state level
- Cash flows that will eliminate the need to issue Revenue Anticipation Notes in the event state or federal aid is not paid timely

These principles have allowed us to maintain both educational excellence and financial stability through challenging economic times.

The Chatham Central School District has always welcomed the opportunity to review and strengthen our financial practices and oversight. We have worked diligently over the past several years to update policies, strengthen internal controls, and develop budgets that balance short-term financial priorities with the long-term financial well-being of the District. After the last state audit in 2015 the district followed the recommendations to develop comprehensive policies for establishing and using reserve funds. The District strengthened the reserve plan by including targeted reserve fund levels, and displayed different scenarios based on the District's long-term financial model. The District has formally adopted the reserve plan document each year after the plan is discussed by the finance committee. The finance reserve plan is

discussed each year publicly at a board of education meeting before adoption. The District has been extremely transparent with long-term financial planning and how reserves will be utilized to combat challenging times. Furthermore, the District has had tax levies under the tax cap eight times over the past 12 years, and the other four years were at the tax cap. The average tax rate has been 1.86% over this time period. This year the District went out with a tax levy that had the largest difference between the tax cap and the tax levy in the District's history. Public budget presentations discussed the goal of keeping the tax levy increase significantly lower than the tax cap. This planning stays in line with the long-range financial plan's goal of low stable tax increases and the avoidance of volatility.

The District has reallocated voter-approved capital reserves to offset the tax impact of voter-approved capital projects. Our reserve plan and long-term fiscal planning has benefited the District by allowing us to receive an upgrade in the Moody's Investors bond rating from Aa3 to Aa2 for the capital project approved by voters in 2018. This rating upgrade was based on strong financial reserves and the solid fiscal management the District has demonstrated. The newly issued debt and refinancing of previous debt resulted in over a million dollars in savings on interest costs for the taxpayer. The District will be issuing debt next year and is looking to maintain the current Aa2 rating to once again save the taxpayer significant interest costs over the term of the debt. The District has estimated \$3 million in savings over the life of the new bonds due to the combination of interest expense avoidance associated with utilizing capital reserves and this strong credit rating.

The Comptroller's audit stated that as of June 30, 2022 the District reported 10 reserves in the general fund totaling \$15.7 million. On February 14, 2022, District voters approved an approximately \$22 million capital project. The District is applying approximately \$8.4 million in capital reserves to offset the cost and reduce taxpayer costs. This will reduce the 10 reserves from \$15.7 million to approximately \$7.3 million, resulting in a decrease of approximately 54% of the reserves.

The State Comptroller's office spent several months at Chatham Central School District reviewing our procedures, processes, and policies. As expected, the audit did not uncover any instances of fraud or malfeasance with our business practices. The audit included a risk assessment of purchasing, information technology, payroll, internal controls, banking, transportation, inventory, fixed assets, business office, etc. We are pleased that the audit report contains no findings in these areas, which we interpret as confirmation of sound financial practices. We work closely with our outside independent auditors to review our management practices and oversight procedures. The District has reviewed the Comptroller's findings and recommendations of this audit and will take corrective action in certain areas. These will be outlined in our Corrective Action Plan.

The audit report focuses on the District's management of reserves, a topic on which the District and the Comptroller's office have a difference of opinion. The Comptroller is of the opinion that the School District should significantly reduce its reserves. The School District and its external auditors respectfully disagree. The audit report contains a number of conclusions and broad statements that we believe reflect subjective opinions of the Comptroller's Office with respect to the District's financial management, specifically as they relate to financial planning, reserve funds, and fund balance management. The Chatham Central School District utilizes a long-term budgeting strategy in which the reserve accounts mentioned in the Comptroller's audit play an important role. The Chatham Central School District is constrained for revenue based on receiving the minimum amount of foundation or operating aid each year and faces additional limits to our revenue posed by the New York State property tax cap. The District's reserves have served as a buffer account to weather shortfalls in revenue and unexpected cost increases. As a result of the District responsibly utilizing reserves, Chatham has avoided drastic cuts to the educational program and kept the tax increases at or below the limit set by the property tax cap. The Comptroller's claim that taxpayers paid higher than necessary taxes fails to take into account that the District's current revenue is not sufficiently sustainable and that the District projects that the reserves will be severely impacted over the next ten years. Furthermore, a significant amount of capital project work needs to be accomplished to maintain and

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Note 2
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upgrade the buildings as per the building condition survey. As has been seen throughout the State, districts that have not had adequate reserves have been forced to make drastic cuts to programs and services and or levy tax increases that exceed the tax cap.

The Board of Education and administration are transparent with the public regarding the budget and finances of the District. The Board and administration have addressed budget and long-term financial plans in numerous public and community meetings over the past decade. The District attempts to keep the public continually informed through Board meetings, budget presentations, town hall meetings, and long-term planning sessions. These meetings routinely include discussions about long-term financial projections and the use of reserves. This information regarding the District's long-range plans and use of reserves is formally adopted each year, posted on the website, and provided in an annual budget newsletter. The Board and administration take great pride in having open discussions with the public regarding the finances of the District.

As stated in the previous Comptroller's audit of 2105, The Board of Education adopts a motion at the end of each year which requires that any balance in unrestricted fund balance over the State allowed 4% goes into specific reserve funds, typically replenishing funds expended during the year. This mechanism prevents the District from exceeding the allowable amount in unrestricted fund balance. The reserves are then used to cover certain expenses from savings instead of using our limited revenues. The District's external auditors annually audit the School District records and have never criticized the District's plan or use of reserves. In Figure 2 of the Comptroller's report the mistaken assumption is that appropriated fund balance would never be needed, and that the appropriated money would be placed in the unrestricted fund balance account, which is not the case. There are multiple other appropriate possibilities for use of funds in excess accounts, and the Comptroller is inaccurate in assuming that Chatham will exceed the 4% statutory limit for the unrestricted fund balance. Indeed, the District has, per our annual resolution, done just the opposite. Furthermore, the money is appropriated to reduce taxpayer burden the following year, and would be needed on worst-case scenarios. If the money was not appropriated and the contingencies were removed, the excess surplus per the annual Board motions would place the money in a reserve account.

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Note 3
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Recommendation 1:

The Board should develop and adopt budgets that include reasonable estimates for appropriations and the amount of fund balance that will be used to fund operations

Response:

The District budgets for expenses that may be volatile and subject to external forces beyond the District's control. The budget is expected to fund educational programs to meet the needs of the students and community regardless of any changes in external factors which can lead to unexpected increases in the budget.

The Board of Education systematically reviews every budget line of the appropriations and adopts realistic estimates for expenditures. In addition, the Board of Education has built contingencies into the budget to account for unexpected expenses. The contingencies allow the District to be prepared for unforeseeable increases to the budget due to various items such as increases in the number of special education students, fluctuations in utility prices, or health insurance premium increases, etc.

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The Board's philosophy is to leave enough flexibility in the budget to meet any worst-case financial demands which may arise during the school year. Any contingent money that goes unspent is applied to reduce the taxpayers' burden the following year or is placed in a reserve account to offset expenses in future years. The District wants to reiterate that this practice is publicly discussed and in the financial reserve plan.

The information in **Comptroller's Figure 3: Overestimated Expenditures** is more accurately represented in **District Figure 1A: Budget to Actual Expenses**, represented below. We have adjusted the Comptroller's

numbers to reflect the contingent expenditures that were applied to reduce the tax levy increase in the following year's budget. As shown in **District Figure 1A's** revised numbers below, the percentage of budget to actual expenditure is 5.57% for the three-year timeframe. One major factor contributing to larger surpluses than the historical norm over this timeframe is COVID. During COVID there was a tremendous amount of uncertainty coupled with the governor stating that 20% reductions to State Aid were going to occur. This resulted in the District proactively freezing spending for non-essential purchases. Furthermore, field trips, athletics, and numerous other events were significantly curtailed during COVID. Due to all of the uncertainty, the District proactively took steps to reduce expenses to match State aid reductions. During this timeframe there was a significant amount of federal funds offered to Chatham over a few years that allowed the District to offset expenses, resulting in a greater difference than normal between budgeted and actual expenditures. This federal money will expire next year.

See
Note 5
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District Figure 1A : Budget to Actual Expense (millions)						
Fiscal Year	Budgeted Expenditures	Actual Expenditures	Comparison Budget to Actual Expenditures	Appropriated Fund Balance to reduce taxes	Budget to Actual Expenditures	Percentage Budget to Actual
2019-20	\$31.5	\$28.8	\$2.7	\$1.34	\$1.36	4.32%
2020-21	\$32.1	\$28.8	\$3.3	\$1.34	\$2.0	6.11%
2021-22	\$33.1	\$29.5	\$3.6	\$1.34	\$2.3	6.83%
Totals	\$96.7	\$87.1	\$9.6	\$4.0	\$5.6	5.77%

Recommendation 2:

Discontinue the practice of appropriating fund balance that is not needed, and will not be used, to fund operations.

Response:

As stated in Response #1, the Board of Education has built contingencies into the budget to account for unexpected expenses. The contingencies allow the District to be prepared for unforeseeable increases to the budget due to various items such as increases in the number of special education students, fluctuations in utility prices, or health insurance premium increases, etc.

See
Note 6
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The Board's philosophy is to leave enough flexibility in the budget to meet any worst-case financial demands, which may arise during the school year. During difficult financial times appropriated fund balance will be utilized and needed to offset significant negative impacts on instruction. Any contingent money that goes unspent is applied to reduce the taxpayers' burden the following year or is placed in a reserve account to offset expenses in future years. The District wants to reiterate that this practice is publicly discussed and in the financial reserve plan.

Recommendation 3:

Amend the District's plan to have more reasonable targeted funding levels of the unemployment insurance, worker's compensation, and employee retirement contribution reserves.

Response:

The District recognized the need to fund the capital reserve to the maximum voter approved level to be utilized for the recently approved capital project and reallocated the following amounts out of those

reserves. The unemployment reserve was reduced by \$250,000, the worker's compensation reserve was reduced by \$300,000, and the employee retirement contribution reserve was reduced by \$1,001,016. The result was that \$1,551,016 was reallocated from these reserves to the capital reserve to offset the tax impact for our new capital project. While the District believes the target levels are justifiable, it will discuss these levels during the review of the reserve plan.

Recommendation 4:

Develop a plan to reduce the balances in the unemployment, insurance, workers' compensation and employee retirement contribution reserves to reasonable levels. The surplus in these reserves can be used to:

- Fund one-time expenditures
- Fund needed reserves that are not already adequately funded
- Reduce District property taxes

Response:

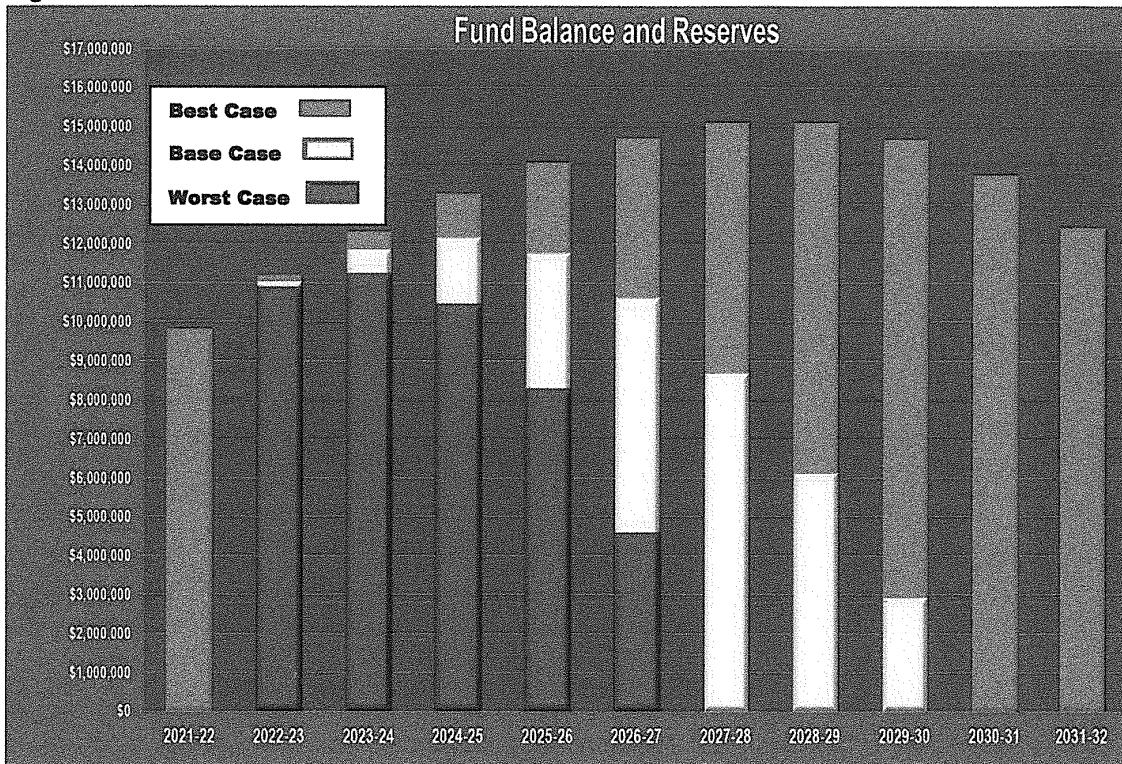
The District believes these reserves are appropriately funded and will be essential for long-term planning and the future financial stability of the District. Furthermore, the District has implemented numerous efficiencies and savings to reduce expenses and allow our reserve accounts to last longer.

The goal of having these reserves is to keep taxes at or below the tax cap and maintain strong educational programming for our students. As displayed in **District Figure A** from the District's financial model (shown below), Chatham is using its reserves and, absent a significant reduction in expenses and/or substantial increases in revenue, the projection is the District will have major financial challenges in approximately 8 years. Not having reserves would result in a "financial cliff" meaning that the District would not have enough funds to fully support our operations. This would lead to devastating cuts to the school program and/or a need to pass a high tax levy. Our concern with the Comptroller's recommendation is that if the District had pursued a strategy resulting in limited reserves, we could, like too many other districts, be facing this "financial cliff" now rather than in the future. Furthermore, the District would not have been able to create capital reserves that were essential to offset tax increases in the recently approved capital project.

See Note 1 Page 18

The District did recognize that the reserves were fully funded at the high range of the target levels. This resulted in following the Comptroller's recommendation to fund needed reserves that are not adequately funded. The District moved money from the unemployment, workers' compensation, and employee retirement contribution reserves to the capital reserve in the amount of \$1,551,016. The capital reserve was fully funded to offset the capital project voters recently approved.

Figure A



The District currently uses the workers' compensation reserve for premiums, unemployment reserve to pay claims, and tax certiorari reserve to pay tax claims.

Recommendation 5:

Consider whether an insurance reserve is necessary.

Response:

The District believes the insurance reserve is necessary due to the District increasing the deductible to \$25,000 (which resulted in savings to the District) and due to the possibility of higher premiums. The audit stated the District funds insurance in the budget and questioned the need for the reserve. The District sets up reserves as part of our long-term financial plan. The District did not use the reserve over the last few years, but that does not mean that the reserve will never be utilized. As shown in the graph in Recommendation 4, if the District starts to utilize reserves and creates a deficit then all reserves will be utilized if required. The amount is not significant to the stated average expenditure of \$133,773.

Recommendation 6:

Develop a plan for the use of excess fund balances and reserve funds in a manner that benefits District taxpayers. Such uses could include, but are not limited to:

- a. Reducing real property taxes
- b. Increasing other necessary reserves
- c. Paying off debt
- d. Financing one-time expenditures

Response:

The District respectfully disagrees with the Comptroller's opinion that the District holds too much money in

reserves. It is the Board and administration's position that the District's long-range plan benefits taxpayers and students for the long term.

Because State aid has not kept up with cost increases in recent years, the District has utilized reserves and fund balance in the budget to reduce property tax increases over the past few years. Furthermore, the risks of economic recession, extremely high inflation, and a stock market downturn make strong financial planning with reserves essential to mitigate a negative impact on educational opportunities for the students. After reviewing the strength of the financial reserve plan, the District's goal this year was to reduce the tax levy relative to the tax cap. Compared to the tax cap's allowable tax levy increase of 3.52%, the tax levy increase of 1.98% included in the 2023-24 budget is the single largest difference between the dollar amount the cap allowed for and what the District actually asked for since the tax cap became law. The tax levy was also significantly below inflation of 8% last year.

See Note 7 Page 19

During the last few school years, the District developed a plan to utilize budget surpluses due to one-time revenues, and lowered expenditures to fund two capital reserves. These capital reserves will be used to offset costs and reduce the burden on taxpayers pertaining to the District's recently approved \$22 million capital project. As previously discussed, as of June 30, 2022 the 10 reserves will be lowered approximately 54% from \$15.7 million to \$7.3 million as the capital reserves are transferred to the capital fund to pay for the upcoming capital project.

Conclusion


We would like to thank the Comptroller's Office for their thoroughness and professionalism over the course of their time that they spent in Chatham.

The audit provides us with strategies to review our reserve targets in our reserves plan and consider re-establishing another capital reserve for future capital projects. The District does not believe that the purpose of the Comptroller's audit should be to substitute their judgment for that of the Board of Education and its administration in terms of overall financial management for the District. We reassert that Chatham Central School District has a transparent and prudent approach to utilizing reserves and fund balance to maintain the financial stability and program opportunity in our District, now and in the future. While we respect the Comptroller's opinions as to appropriate reserve levels, we strongly feel that our approach has and will continue to provide the best possible education for our students in a fiscally responsible manner.

Sincerely,

CHATHAM CENTRAL SCHOOL DISTRICT
BOARD OF EDUCATION

Matthew Fisch
President

Salvatore DeAngelo 
Superintendent of Schools

Chatham Central School District, 50 Woodbridge Ave, Chatham, NY 12037

Salvatore DeAngelo, Ed.D., MBA
Superintendent of Schools
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Appendix B: OSC Comments on the District's Response

Note 1

While disagreeing with our recommendation to maintain reserves at reasonable levels, District officials did not provide any financial analysis or basis to support the District's funding and accumulation of the unemployment, worker's compensation and retirement contribution reserve balances represented in Figures 3, 4 and 5 of the audit report.

Note 2

When the District plans for an operating deficit by appropriating fund balance, but instead realizes an operating surplus due to consistently overestimating expenditures, taxpayers pay higher than necessary taxes. Our audit scope did not include a determination of the sustainability of the District's revenues.

Note 3

The District's annual financial results have shown that appropriated fund balance has not been needed or used. Appropriated fund balance is intended to fund the budget gap between current year appropriations and anticipated revenue, and should not be used as a mechanism to allow for the accumulation of additional fund balance and to fund reserves.

The audit report does not state that the District exceeded the 4 percent fund balance statutory limit. However, the District avoids exceeding the 4 percent limit each year by making unbudgeted transfers of the excess unrestricted fund balance to reserves.

Note 4

Although officials said the Board systematically reviewed every budget line of appropriation, the audit found that, for fiscal years 2019-20 through 2021-22, five appropriation accounts were significantly overestimated by a total of \$5 million (31 percent).

Note 5

Figure 1A in the District's response does not clearly represent the effect of overestimating expenditures. While "Appropriated Fund Balance to reduce taxes" would have theoretically reduced the amount of taxes levied, the District did not use the amounts appropriated because it had surpluses during each of the three years indicated due to its consistent practice of overestimating expenditures. Therefore, the District did not use the amounts appropriated to reduce taxes.

Note 6

Budgeting for contingencies within the actual budget line items does not provide transparency to District taxpayers. Unrestricted fund balance is designated to be used for contingencies. By overestimating expenditures, the District generated surpluses totaling \$6.9 million during our audit period, which District officials did not use to fund District operations or reduce taxes.

Note 7

As demonstrated in our audit report, the District experienced operating surpluses totaling \$6.9 million, did not use appropriated fund balance, and increased reserve balances during the audit period.

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 financial management policies, procedures and budgeting practices.
- We analyzed general fund financial records for fiscal years 2019-20 through 2021-22 to identify trends in operating results, fund balance and the real property tax levy.
- We reviewed the adopted general fund budgets for fiscal years 2019-20 through 2021-22 to determine 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 District's results of operations for fiscal years 2019-20 through 2021- 22 and calculated surplus fund balance as a percentage of the next year's appropriations for compliance with the statutory limit.
- We recalculated surplus fund balance as a percentage of the next year's appropriations after adding back appropriated fund balance not used and the overfunded portion of reserves to fund the next year's operations.
- We reviewed reserve fund balances since June 30, 2020 to understand the trend and to assess whether they were 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.

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

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Cost-Saving Ideas – Resources, advice and assistance on cost-saving ideas

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

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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

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

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