

# Quogue Union Free School District

## Financial Condition Management

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DECEMBER 2017

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

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# Report Highlights

## Quogue Union Free School District

### Audit Objective

Determine whether the Board and District officials effectively managed general fund balance.

### Key Findings

- Unrestricted fund balance increased to nearly \$3 million on June 30, 2017, or 37 percent of the ensuing year's budgeted appropriations, exceeding the statutory limit by 19 to 33 percentage points from 2012-13 through 2016-17.
- The District's budgeting practices included appropriating fund balance not needed to fund operations and adopting budgets that overestimated appropriations by an average of about \$795,000 (11 percent) from 2012-13 through 2016-17.
- The retirement contribution reserve may be overfunded.

### Key Recommendations

- Develop a plan to reduce the amount of unrestricted fund balance to the legal limit.
- Adopt realistic annual budgets based on historical or other known trends.
- Review the retirement contribution reserve to determine whether the amount retained is necessary and reasonable.

District Officials generally agreed with our recommendations and indicated they plan to initiate corrective action

### Background

The Quogue Union Free School District (District) is located in the Town of Southampton in Suffolk County.

The Board of Education (Board) is responsible for managing and controlling the District's financial and educational affairs. The Superintendent of Schools (Superintendent) is responsible for the District's day-to-day management. The Superintendent is also responsible, along with the District Treasurer, for developing and administering the budget.

#### Quick Facts

Employees	36
Enrollment	Approximately 110
2017-18 Appropriations	\$8.1 million
2016-17 Year-End Unrestricted Fund Balance	\$2.9 million

### Audit Period

July 1, 2012 – June 30, 2017

# Financial Condition Management

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## What is Effective Financial Condition Management?

To effectively manage financial condition, the Board should adopt realistic and structurally balanced budgets based on historical or known trends, in which recurring revenues finance recurring expenditures. In preparing the budget, the Board must estimate what the District will spend and the amounts it will receive in revenue (e.g., State aid), how much fund balance will be available at year-end and, to balance the budget, the expected tax levy. Accurate estimates help ensure that the real property tax levy is not greater than necessary.

The Board must also maintain reasonable fund balance levels. Fund balance is the difference between revenues and expenditures accumulated over time. New York State Real Property Tax Law currently limits the amount of unrestricted fund balance that a school district can retain to no more than 4 percent of the next fiscal year's budget. Additionally, school districts are allowed to legally set aside, or reserve, portions of fund balance to finance future costs for specific purposes (e.g., capital projects or retirement expenditures), and may also use a portion of fund balance to help finance the next year's budget (referred to as appropriated fund balance). The Board should adopt a formal written plan that indicates how reserves will be funded, how much should be accumulated in the reserves and when the money will be used to finance related costs. While school districts are generally not limited as to how much money can be held in reserves, the balances should be reasonable. The Board should weigh the accumulation of fund balance for future needs with their obligation to ensure that the District's real property tax levy is not greater than necessary.

## Unrestricted Fund Balance Exceeded the Statutory Limit.

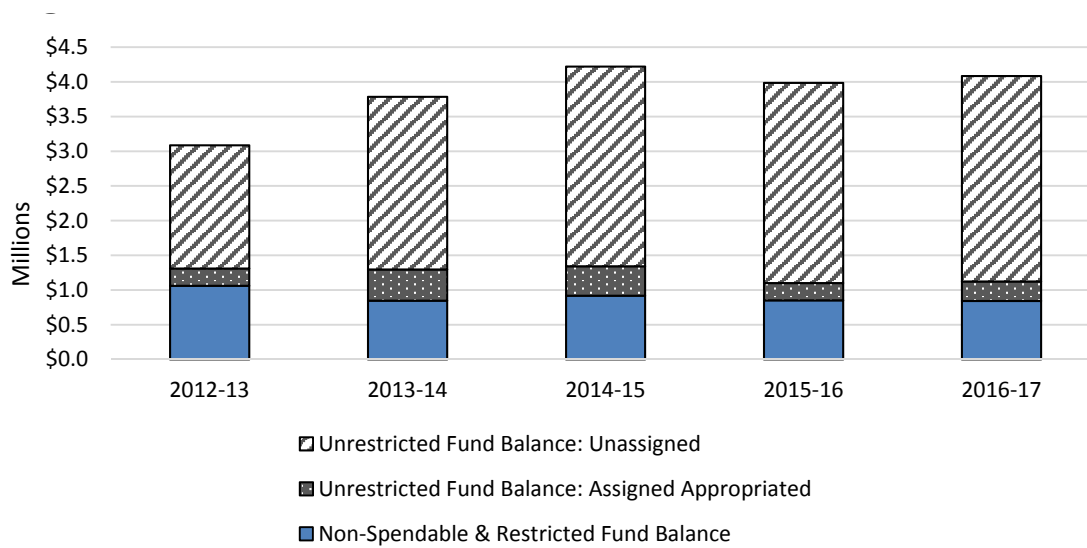
District officials need to improve budgeting practices to effectively manage the District's financial condition. Further, the Board and District officials have not implemented corrective action since our last report,<sup>1</sup> in which we found that the District had accumulated unrestricted fund balance that exceeded the statutory limit by 19 percentage points over the four years ended June 30, 2013. The District experienced operating surpluses averaging nearly \$598,000 in four of the past five years. As a result, total fund balance increased 32 percent: from \$3.1 million as of June 30, 2013 to \$4.1 million as of June 30, 2017 (Figure 1). While approximately \$708,500 of the fund balance is restricted in reserve funds, nearly \$3 million is unrestricted. During these five years, unrestricted fund balance exceeded the statutory limit by a range of \$1.5 million to \$2.6 million, or 18.7 to 32.8 percentage points.

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<sup>1</sup> Report 2013M-274, Financial Condition and Cash Receipts, December 2013

**FIGURE 1**

**Total Year-End Fund Balance**



Despite these fund balance levels, the Board appropriated relatively little fund balance in the adopted budgets, appropriating as little as \$250,000 (2012-13, 2015-16) and no more than \$450,000 (2013-14), with the annual appropriation averaging \$331,000 over the five years examined. Furthermore, except for 2015-16 when the District experienced an operating deficit, none of the appropriated fund balance was actually used. When unused appropriated fund balance was added back, the District’s recalculated unrestricted fund balance ranged from 25.9 to 40 percent of the subsequent year’s budget (Figure 2).

**Figure 2: Unused Fund Balance**

	2012-13	2013-14	2014-15	2015-16	2016-17
<b>Reported Unrestricted Fund Balance</b>	\$1,775,515	\$2,488,002	\$2,877,678	\$2,883,399	\$2,959,226
<b>Ensuing Year's Budget</b>	\$7,824,085	\$7,737,099	\$7,844,539	\$7,839,014	\$8,059,754
<b>Reported Unrestricted Fund Balance as a Percentage of Ensuing Year's Appropriations</b>	22.7%	32.2%	36.7%	36.8%	36.7%
<b>Add: Appropriated Fund Balance Not Used to Fund Ensuing Year's Budget</b>	\$250,000	\$450,000	\$189,185	\$250,000	\$0 <sup>a</sup>
<b>Recalculated Unrestricted Fund Balance</b>	<b>\$2,025,515</b>	<b>\$2,938,002</b>	<b>\$3,066,863</b>	<b>\$3,133,399</b>	<b>\$2,959,226</b>
<b>Recalculated Unrestricted Fund Balance as a Percentage of Ensuing Year's Appropriations</b>	25.9%	38.0%	39.1%	40.0%	36.7%

<sup>a</sup> This assumes that the amount appropriated to the 2017-18 budget is used

Adopting budgets that result in the appropriation of fund balance that will not be used causes the District to retain more fund balance and levy more real property taxes than needed. As a result, the District accumulated unrestricted fund balance in excess of the statutory limit and continued to accumulate additional amounts of restricted and unrestricted fund balance during our audit period.

We reviewed the District's budgets for the 2012-13 through 2016-17 fiscal years (Figure 3) and found that District officials overestimated appropriations, spending nearly \$4 million less than planned during this five-year period. While revenue estimates were generally close to the actual revenues received, the budget variances each year contributed to a 32 percent (\$1 million) increase in total fund balance from 2012-13 through 2016-17. If the Board continues its current budget practices, fund balance in the general fund will continue to accumulate.

**Figure 3: General Fund Budget-to-Actual Comparison**

	2012-13	2013-14	2014-15	2015-16	2016-17
<b>Appropriations</b>	\$7,711,580	\$7,862,539	\$7,767,187	\$7,875,565	\$7,856,977
<b>Actual Expenditures</b>	\$6,176,464	\$6,931,103	\$6,897,642	\$7,823,535	\$7,268,463
<b>Variance</b>	\$1,535,116	\$931,436	\$869,545	\$52,030	\$588,514
<b>Percentage Variance</b>	24.9%	13.4%	12.6%	0.7%	8.1%
<b>Estimated Revenues</b>	<b>\$7,436,325</b>	<b>\$7,674,085</b>	<b>\$7,287,099</b>	<b>\$7,369,539</b>	<b>\$7,364,014</b>
<b>Actual Revenues</b>	\$7,323,845	\$7,640,033	\$7,333,173	\$7,587,720	\$7,368,107
<b>Variance</b>	\$112,480	\$34,052	(\$46,074)	(\$218,181)	(\$4,093)
<b>Percentage Variance</b>	1.5%	0.4%	-0.6%	-2.9%	-0.1%
<b>Operating Surplus/(Deficit)</b>	\$1,147,381	\$708,930	\$435,531	(\$235,815)	\$99,644

The District expended less than budgeted, in part, because the Board adopted budgets with overly conservative estimates for certain appropriations. Over the last five years, the Board overestimated appropriations for teaching – regular school<sup>2</sup> by an average of \$380,193 (12.2 percent) each year and central services by an average of \$182,448 (28.2 percent). Special education programs were overestimated by an average of \$275,401 (23.6 percent) from 2012-13 through 2015-16; this category was underestimated by \$96,634 (8.9 percent) in 2016-17.

The Superintendent, who started at the District in 2016-17, had no explanation for the budget variances. He said that no one is left of the prior administration, but it appears that budgets were increased by a flat percentage each year without considering the actual expenditures incurred. The Superintendent told us that he is working on revising the District's budgeting process.

<sup>2</sup> This includes, among other things, teachers' salaries.

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## **The Retirement Contribution Reserve May Be Overfunded.**

As of June 30, 2017, the District reported four general fund reserves (retirement contribution, repairs, workers' compensation and employee benefit accrued liability) with balances totaling approximately \$708,500. The Board has not developed a formal plan stating how much would be set aside in each reserve, how each reserve should be funded or when the balances would be used. We examined the District's plans for funding and using these reserves. We did not find any significant concerns with the employee benefit accrued liability, repair and workers' compensation reserves. However, we believe the retirement contribution reserve may be overfunded.

The Board originally funded the retirement contribution reserve in the 2010-11 fiscal year with \$172,000 to fund future payments to the New York State and Local Retirement System. The balance as of June 30, 2017 was \$309,287, sufficient to cover more than four years of retirement costs, which averaged \$78,000 over the last five years. Except for \$4,600 used in 2013-14, the District has not used any reserve funds to pay for these expenditures over the last five years. Instead, the District included appropriations in the annual budgets and levied taxes to fund them. As a result, this reserve may be overfunded.

## **What Do We Recommend?**

The Board and District officials should:

1. Ensure that the amount of unrestricted fund balance is in compliance with the statutory limit and develop a plan to use surplus funds as a financing source for:
  - Funding one-time expenditures
  - Funding needed reserves
  - Reducing District property taxes.
2. Adopt annual budgets that contain realistic estimates for appropriations based on historical or other known factors.
3. Review all reserves at least annually to determine whether the amounts reserved are necessary and reasonable, and use excess amounts in accordance with applicable statutes in a manner that benefits residents.
4. Adopt a written reserve fund policy that includes how the reserves will be funded, the optimal funding levels for each reserve and the conditions under which reserves will be used to finance related costs.

# Appendix A: Response From District Officials

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Jeffrey E. Ryvicker  
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November 20, 2017

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Dear Mr. McCracken:

The Quogue Union Free School District is in receipt of the draft report titled “*Financial Condition Management – Report Examination – 2017M-196.*” The correspondence herein is the official response from the District and includes a preliminary written corrective action plan (CAP) required by applicable sections of New York State’s General Municipal Law, Education Law and the Regulations of the Commissioner of Education. The final corrective action plan will be submitted within the next 60 days.

The Board of Education and Administration have reviewed the findings of this draft report and have given significant consideration to the information contained within. We accept the findings, and agree with the accuracy of the calculations contained in this report. We take note of the fact that your review covers the period from July 1, 2012 – June 30, 2017.

The following represents the District’s response to the findings contained in the draft report and the required corrective action plan.

### **Audit Recommendation:**

1. Ensure that the amount of unrestricted fund balance is in compliance with the statutory limit and develop a plan to use surplus funds as a financing source for:
  - Funding one-time expenditures
  - Funding needed reserves
  - Reducing District Property Taxes

### **Corrective Action:**

The District recognizes the importance of maintaining proper levels of fund balance in accordance with applicable laws and regulations. Prior to the start of this audit, during the 2016-2017 school year, the Quogue UFSD took corrective action. In May, 2017, voters approved the establishment of a new capital projects reserve and repair reserve. The district intends to seek voter approval to use unrestricted fund balance to fund capital projects and repairs based on needs identified in the District’s Five-Year Facilities Plan. This plan was developed during the 2016-2017 school year with *BBS Architects and Engineers*.



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**Audit Recommendation:**

2. Adopt annual budgets that contain realistic estimates for appropriations based on historical or other known factors.

**Corrective Action:**

During the 2016-2017 school year, the business office began analyzing actual expenditure data from past years in order to develop budgets which are more closely aligned with actual expenses. This process was reviewed with the senior examiner from the Office of the State Comptroller as it pertained to the development of the 2017-2018 budget. In particular, we are analyzing codes associated with teacher's salaries, special education programs, transportation, tuition for secondary students and central services. As detailed in the draft report, surpluses in these areas varied from year to year during the period under audit. Therefore, our corrective action plan is to systematically review and correct these budget appropriations as needed on an annual basis.

**Audit Recommendation:**

3. Review all reserves at least annually to determine whether the amounts reserved are necessary and reasonable, and use excess amounts in accordance with applicable statutes in a manner that benefits residents.

**Corrective Action:**

The District acknowledges the information presented in the Draft Audit Report regarding the District's reserves, and we are pleased that the examination "...did not find any significant concerns with the employee benefit accrued liability, repair and workers' compensation reserves." The District plans to review the retirement contribution reserve, as well as the other reserves annually, to determine whether the amounts reserved are necessary and reasonable.

**Audit Recommendation:**

4. Adopt a written reserve fund policy that includes how the reserves will be funded, the optimal funding levels for each reserve and the conditions under which reserves will be used to finance related costs.

**Corrective Action:**

The District recognizes the importance of maintaining a well-organized board of education policy manual that sets forth guidelines for district operations in accordance with applicable laws and regulations. Prior to the start of this audit, the Quogue UFSD took corrective action during the development of the 2017-2018 budget by appropriating \$8,600 to account A1010.49 for the Policy Manual Development Service provided by Erie BOCES. The Cross Contract for this service was signed on July 24, 2017. The District will consider the development and adoption of a written reserve fund policy as recommended.

On behalf of the Quogue UFSD, we would like to acknowledge the professionalism of the field auditors who were courteous and cooperative throughout the engagement and demonstrated the utmost respect for our time and workflow while in district.

Sincerely,

Jeffrey E. Ryvicker  
Superintendent of Schools

## Appendix B: Audit Methodology and Standards

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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, we performed the following audit procedures:

- We interviewed District officials and reviewed the Board meeting minutes, resolutions and budget policies to gain an understanding of their budget process.
- We calculated the results of operations over the last five years by comparing actual revenues with actual expenditures.
- We analyzed the trend in total fund balance in the general fund for the 2012-13 through 2016-17 fiscal years. We compared unrestricted fund balance with the next years' budget appropriations to determine whether the District was within the statutory limit.
- We compared the general fund's total estimated revenues and budget appropriations with the actual revenues and expenditures for the 2012-13 through 2016-17 fiscal years to determine whether District budgets were reasonable. We followed up with District officials on significant budget variances.
- We reviewed reserve fund balances to determine whether they were reasonable and funded in a transparent manner.

We conducted this performance audit in accordance with GAGAS (generally accepted government auditing standards). 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.

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 2116-1(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 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. We encourage the Board to make the CAP available for public review in the Clerk's office.

## Appendix C: Resources and Services

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### **Regional Office Directory**

[www.osc.state.ny.us/localgov/regional\\_directory.pdf](http://www.osc.state.ny.us/localgov/regional_directory.pdf)

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

[www.osc.state.ny.us/localgov/costsavings/index.htm](http://www.osc.state.ny.us/localgov/costsavings/index.htm)

### **Fiscal Stress Monitoring** – Resources for local government officials experiencing fiscal problems

[www.osc.state.ny.us/localgov/fiscalmonitoring/index.htm](http://www.osc.state.ny.us/localgov/fiscalmonitoring/index.htm)

### **Local Government Management Guides** – Series of publications that include technical information and suggested practices for local government management

[www.osc.state.ny.us/localgov/pubs/listacctg.htm#lgmg](http://www.osc.state.ny.us/localgov/pubs/listacctg.htm#lgmg)

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[www.osc.state.ny.us/localgov/lgli/pdf/cybersecurityguide.pdf](http://www.osc.state.ny.us/localgov/lgli/pdf/cybersecurityguide.pdf)

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