

Norwood-Norfolk Central School District

Financial Management

NOVEMBER 2022



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

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Report Highlights

Norwood-Norfolk Central School District

Audit Objective

Determine whether the Norwood-Norfolk 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 all reserves. The Board and District officials:

- Allowed surplus fund balance to exceed the 4 percent statutory limit. As of June 30, 2021, surplus fund balance was \$1.7 million, \$0.7 million or 2.9 percentage points over the limit. Surplus fund balance must be used to reduce the upcoming fiscal year's real property tax levy or to fund needed reserves.
- Maintained \$3 million in the New York State and Local Retirement System (NYSLRS) reserve fund, which is enough to fund average retirement expenditures for 10 years. This balance exceeds the Board's targeted funding level range by \$1.6 million to \$2.1 million.
- Did not use \$0.9 million restricted in a debt reserve to pay related debt as required.

Key Recommendations

- Reduce surplus fund balance to comply with the statutory limit.
- Ensure the NYSLRS reserve fund is reduced to a reasonable level.
- Use funds restricted in the debt reserve to make related debt payments as required.

District officials generally agreed with our recommendations and indicated they would take corrective action. Appendix B includes our comment on an issue raised in the District's response.

Background

The Norwood-Norfolk Central School District serves the Towns of Louisville, Madrid, Norfolk, Potsdam and Stockholm in St. Lawrence County. The District is governed by an elected nine-member Board, which is responsible for managing 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 day-to-day management under the Board's direction. The Business Administrator oversees the Business Office, maintains financial records and prepares financial reports.

The Board, Superintendent and Business Administrator are responsible for developing and monitoring the annual budget.

Quick Facts

Student Enrollment	1,003
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2021-22 Appropriations	\$25.1 million
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June 30, 2021 Balances

Surplus Fund Balance	\$1.7 million
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Total Reserves	\$6.2 million
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Audit Period

July 1, 2018 – July 28, 2022

Financial Management

Fund balance is the difference between revenues and expenditures accumulated over time. New York State Real Property Tax Law Section 1318 currently limits the amount of surplus fund balance¹ that a school district can retain to no more than 4 percent of the next year's budget. Any surplus fund balance over this percentage must be used to reduce the upcoming fiscal year's real property tax levy or to fund needed reserves.

School districts are legally allowed to establish reserves and accumulate funds for certain future purposes (e.g., capital projects, retirement expenditures). While school districts are generally not limited as to the amount of funds that can be held in reserves, the balances should be reasonable and routinely monitored by the board and school district officials.

How Should District Officials Properly Manage Fund Balance?

To effectively manage a school district's fund balance, a school board should adopt reasonably estimated and structurally balanced budgets based on historical data or known trends in which recurring revenues finance recurring expenditures. In preparing the budget, a school board must estimate the amounts a school district will spend and receive, how much fund balance will be available at fiscal year-end to use (appropriate) in 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 and surplus fund balance does not exceed the statutory limit.

When fund balance and reserve funds are appropriated for the next year's budget, there is an expectation that the funds will be used to finance the next school year's operations. This allows a school district to use excess fund balance and reserves accumulated in prior years. However, if the school district experiences an operating surplus, the amount of appropriated fund balance and reserves will not actually be used to finance operations.

Officials Overestimated Appropriations and Surplus Fund Balance Exceeded the Statutory Limit

We compared estimated revenues and appropriations in adopted general fund budgets with actual operating results for 2018-19 through 2020-21. We found that, while revenue estimates were generally reasonable, appropriations were overestimated by \$4.4 million or 6.1 percent during the three-year period (Figure 1).

¹ Surplus fund balance is defined as unrestricted fund balance minus appropriated fund balance and encumbrances included in committed and assigned fund balance.

**Figure 1: Budget-to-Actual Expenditure Comparison
(In Millions)**

	2018-19	2019-20	2020-21	Total
Appropriations	\$23.6	\$24.2	\$24.6	\$72.4
Actual Expenditures	\$22.9	\$22.5*	\$22.6	\$68.0
Amount Under Budget	\$0.7	\$1.7	\$2.0	\$4.4
Percentage Under Budget	3.0%	7.0%	8.1%	6.1%

*Excludes an unbudgeted transfer to the capital projects fund of \$1 million.

The most significant appropriation variances were for Board of Cooperative Educational Services (BOCES) special education services (\$1.4 million), instructional and student support salaries (\$1.3 million) and employee benefits (\$1.1 million). The Business Administrator and Superintendent stated that generally these variances occurred due to circumstances beyond the District’s control and measures the District took during the COVID-19 pandemic (pandemic) to control expenditures. For example:

- Variances for special education services occurred because students whose special education services were included in the budget subsequently moved out of the District during the school year or did not enroll. For example, in 2019-20, two students transferred out of BOCES programming to be home-schooled. Anticipating the students may reenroll, officials included the student’s cost for services in the 2020-21 budget. However, these students did not reenroll.
- The District instituted a hiring freeze during the 2019-20 school year due to the pandemic and chose not to fill positions that were vacated by staff turnover, decisions which reduced employee salary and benefits expenditures. Furthermore, anticipating normal operations would resume during the 2020-21 school year, officials planned for increased staffing levels and corresponding employee benefits in that year’s budget. However, facing the possibility of a reduction in State aid and the continued inability to resume full operations because of the pandemic, officials continued to reduce staffing levels, which led to further decreases in salaries paid and employee benefit expenditures. Financial records show the District reduced instructional and student support salaries by \$0.4 million or 5.8 percent between 2018-19 and 2020-21, with reductions in directly-related expenditures such as the District’s share of employee retirement and social security contributions totaling \$0.1 million or 9 percent.

The Board and District officials kept the real property tax levy flat from 2018-19 through 2020-21. They also continued the practice of not increasing real property taxes in the 2021-22 and 2022-23 budgets. However, between 2018-19 and 2020-21, officials appropriated a total of \$3.2 million in fund balance and reserves,

expecting planned operating deficits in that amount. Yet, because of officials' cost-cutting measures, the District spent less than budgeted and generated a total operating surplus of \$1.4 million (including interfund transfers) during the same period. This operating surplus would have been \$2.4 million over the three-year period had officials not made an unbudgeted fiscal year-end transfer of \$1.0 million to the capital projects fund in 2019-20 (Figure 2).

Figure 2: Planned Operating Deficits vs. Operating Results After Transfers (in Millions)

Fiscal Year	Planned Operating Deficit*	Operating Surplus Before Transfers	Unbudgeted Transfers to Capital Projects Fund	Operating Surplus (Deficit) After Transfers	Variance
2018-19	\$1.0	\$0.3	\$0.0	\$0.3	\$1.3
2019-20	0.9	0.9	1.0	(0.1)	0.8
2020-21	1.3	1.2	0.0	1.2	2.5
Total	\$3.2	\$2.4	\$1.0	\$1.4	\$4.6

*The amount of fund balance and reserves appropriated as a financing source in the budget

Since appropriated fund balance was not needed to finance operations, the District has accumulated and maintained surplus fund balance in excess of the statutory limit. The District's reported surplus fund balance in the general fund exceeded the 4 percent statutory limit each year from 2018-19 through 2020-21 and ranged from 6.7 to 8.5 percent of the next year's budget. As of June 30, 2021, surplus fund balance exceeded the statutory limit by approximately \$0.7 million or 2.9 percentage points (Figure 3).

Figure 3: Surplus Fund Balance (In Millions)

	2018-19	2019-20	2020-21
Reported Year-End	\$2.0	\$1.6	\$1.7
Reported as Percentage of Next Year's Budget	8.5%	6.7%	6.9%
Maximum Allowed	\$1.0	\$1.0	\$1.0
Excess of Limit	\$1.0	\$0.6	\$0.7

Based on the Business Manager's fiscal year-end projections as of April 11, 2022, the District is expected to generate an operating surplus of \$1.3 million in 2021-22 and will not need to use the \$0.7 million of fund balance appropriated in the budget. This surplus is largely due to the receipt of federal COVID-19 relief funding, which officials used to offset previously budgeted expenditures. Although

District officials knew they were going to receive these funds, they had not developed the plan for spending the funds until after the budget's adoption.

In April 2022, District officials, in conjunction with a hired consultant, developed a written multiyear financial plan. In May 2022, District voters approved the establishment of two capital reserves to finance the cost of future bus and equipment purchases. Combined, these reserves were approved with a \$3.8 million funding limit. The Superintendent and Business Administrator stated they plan to use surplus fund balance to fund newly established reserves.

Given that the District's level of surplus fund balance has exceeded the 4 percent statutory limit in each of the past three years and the District has a combined total of \$6.2 million in reserves set aside for debt service and future expenditures,² and in light of the \$1.4 million operating surplus incurred from 2018-19 through 2020-21 and the \$1.3 million operating surplus projected for 2021-22, the Board and District officials should review their budgeting practices.

If officials continue the same budgeting practices, they will continue to generate annual operating surpluses and not use the fund balance that is appropriated. This would lead to the continued accumulation of surplus fund balance in excess of the statutory limit. As a result, significant funds could be withheld from productive uses, such as funding one-time expenditures and/or needed reserves, paying off debt or reducing the tax levy to provide relief to taxpayers.

How Should District Officials Properly Manage Reserve Funds?

To help ensure that reserve balances do not exceed the amount necessary to address long-term obligations or planned expenditures, a board should adopt a comprehensive written policy that communicates its rationale for establishing reserve funds, objectives for each reserve, maximum targeted funding levels and conditions under which reserves will be used or replenished.

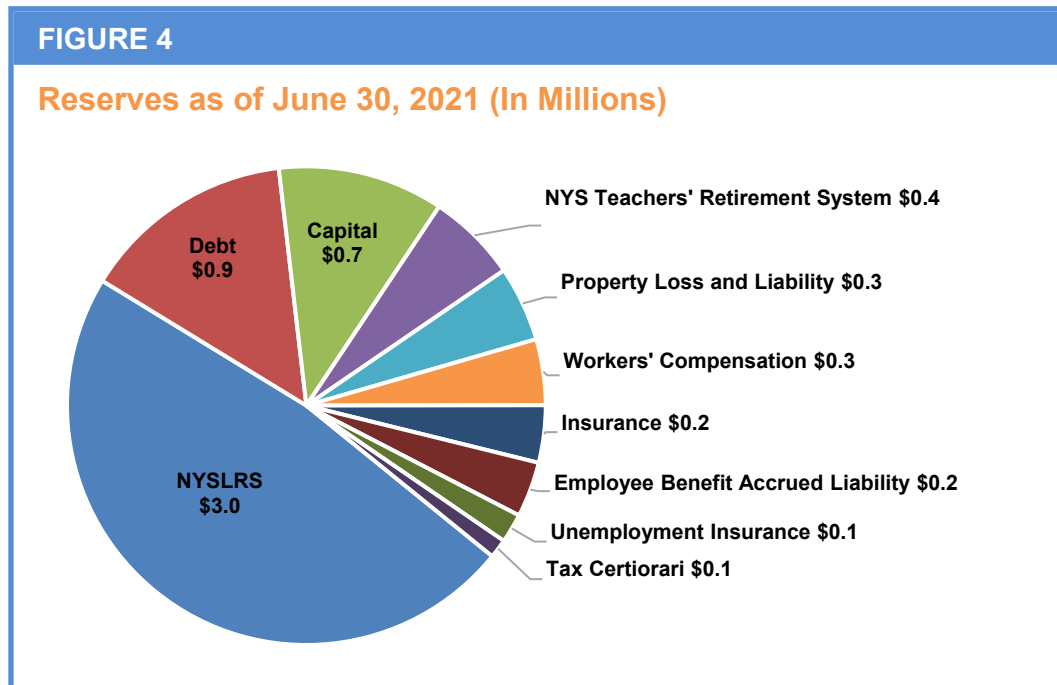
New York State Local Finance Law, Section 165.00 and New York State General Municipal Law, Section 6-I require a debt reserve to be established if unexpended bond proceeds remain on a capital improvement or when a capital improvement has outstanding debt remaining at the time of sale. These funds must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

Officials Did Not Properly Manage Two of 10 Reserve Funds

The Board and District officials developed and adopted a comprehensive reserve plan that provides a list of the District's reserves, including creation date, purpose, funding methods, intended use, targeted funding level and current balance. The

² Refer to the report section entitled Officials Did Not Properly Manage Two of 10 Reserve Funds.

Business Administrator annually updates the plan and submits it to the Board for approval. As of June 30, 2021, the District reported nine general fund reserves with cumulative balances totaling \$5.3 million and a debt reserve of \$0.9 million (Figure 4).



We analyzed reserve balances for reasonableness and adherence to requirements in statute and the District's reserve plan. We found the New York State and Local Retirement System (NYSLRS) reserve was overfunded and the debt reserve had not been used, as required, for debt service payments. The District's other eight reserves were reasonably funded.

NYSLRS Reserve – Annual payments to NYSLRS averaged \$0.3 million between 2018-19 and 2020-21. However, the balance of the NYSLRS reserve as of June 30, 2021 was \$3 million or nearly 10 times the average annual expenditure. Furthermore, the District's reserve plan establishes a targeted funding level for the reserve of between \$0.9 and \$1.4 million. As a result, the reserve is overfunded by approximately \$2.1 to \$1.6 million. The reserve plan includes a schedule of recommended annual appropriations from the reserve totaling \$2.3 million between fiscal years 2023-24 and 2028-29, with the stated goal of using 75 percent of the current balance by June 30, 2029.

Debt Reserve – Although the District paid \$6 million in debt service between 2018-19 and 2020-21, funds in the debt reserve were not applied to these payments as required because the District experienced operating surpluses and

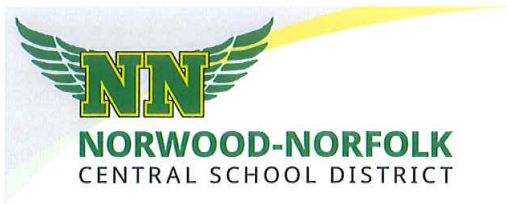
did not use the debt reserve as officials had indicated in the budget. As of June 30, 2021, the reserve had a balance of \$0.9 million. The balance was comprised of unexpended bond proceeds and interest earnings. District officials applied \$79,000 from this reserve toward debt service in 2021-22 and appropriated \$122,200 from this reserve in the 2022-23 budget. The District's multiyear financial plan includes additional annual appropriations from this reserve through 2026-27.

While it is prudent to plan and save for future expenditures and unanticipated events, by overfunding and/or not using reserves, District officials may not be using reserve funds in a manner that best benefits taxpayers.

What Do We Recommend?

1. Adopt budgets that include reasonable estimates of appropriations and discontinue the practice of appropriating fund balance that will not be used to fund operations.
2. Develop a plan to reduce surplus fund balance to within the statutory limit and use excess funds in a manner that benefits District taxpayers. Surplus fund balance can be used for:
 - Funding one-time expenditures,
 - Funding needed reserves,
 - Paying off debt and
 - Reducing District property taxes.
3. Ensure the NYSLRS reserve fund is reduced to a reasonable level in accordance with the District's reserve plan and applicable statute.
4. Use funds restricted in the debt reserve to make related debt payments as required.

Appendix A: Response From District Officials



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James Cruikshank, Superintendent of Schools
Lisa Mitras, Business Manager

October 26, 2022

New York State Office of Comptroller
Syracuse Regional Office
Rebecca Wilcox, Chief Examiner
333 E. Washington Street, Room 409
Syracuse, NY 13202-1428

Dear Ms. Wilcox

The Norwood-Norfolk Central School District is in receipt of the State Comptroller's Office Draft Report of examination of financial management for fiscal years 2018-19 to 2020-21. District Management thanks the Comptroller's Office for their diligence and professionalism throughout the audit process. Below you will find the Norwood-Norfolk Central School District response to the audit findings made in the draft report.

Finding:

Officials overestimated appropriations and surplus fund balance exceeded the statutory limit

Response:

District Officials agree the surplus fund balance exceeds the statutory limit under Section 1318 of the Real Property Tax Law. The Real Property Tax Law limits surplus balances to an amount equal to 4% of the upcoming year's budget. Managing fund balances is often a very difficult task in the budget process; budgets are an estimation of expenditures and anticipated revenues. During the 2021-2022 Fiscal Year, the district accomplished three (3) of the audit recommendations with regards to reducing fund balance. The District funded one-time expenditures, created two new reserves and funded needed reserves. In addition, the Board of Education approved a 0% change to the tax levy for the fourth consecutive year. The District ended the Fiscal Year June 30, 2022 with a 5.03% surplus, unappropriated, fund balance, a decrease over the prior year June 30, 2021 balance of 6.82%. In addition, the district decreased the appropriated fund balance from \$731,781 in the 21-22 Fiscal Year to \$305,878 in the 22-23 Fiscal Year.

District Officials understand the expenditure budget created positive variances from budget to actual. District Officials implement a conservative budget approach when estimating appropriations; budgets are reasonable, thoughtful and thoroughly calculated. During the audit process, the district provided substantial detailed information for each fiscal year audited, categorized by function and object area, as to why appropriations resulted in large variances from budget to actual. The budgeting process did not include an intentional act of overestimating appropriations. Appropriations were overestimated mainly due to circumstances beyond the District's control. District Officials appreciate the New York State Comptroller audit discussed a few circumstances in their report. District Officials will discontinue appropriating fund balance during the budget building process *when* revenue projections equal estimated appropriations. If the budget process results in a gap between revenue estimates and appropriation projections where expenditures are greater than revenues, District Officials will appropriate fund balance to maintain a stable tax levy.



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Finding:

Officials Did Not Properly Manage Two of Ten Reserve Funds

Response:

District Officials agree with the recommendation to utilize debt reserve funds to offset related debt payments. The District utilized \$79,633 in the 2021-2022 Fiscal Year and will further reduce the debt reserve annually by \$122,200, until depleted, starting in Fiscal Year 2022-2023.

District Officials generally agree the New York State and Local Retirement System (NYSLRS) reserve fund is overfunded, however, we do not deem it overfunded to the extent stated in the audit report of \$1.6 to \$2.1 million. Management believes the wording in the existing reserve plan was misperceived from the intent of the plan. The objective of the reserve plan for NYSLRS as written was to maintain a two to three year balance equal to the projected annual liability of the Employee's Retirement Expense *after* the 5-6 year annual allocation was depleted. The resulting affect would be a total balance equal to 7 to 9 years of annual expenditures. The balance in the NYSLRS reserve fund at June 30, 2022 was just over \$3 million. In order to carry out the intention of the long-term reserve plan as written, the NYSLRS reserve fund would currently need a balance of 2.9 million to 3.6 million. After reviewing the NYSLRS reserve fund, District Officials estimate the fund could be reduced by \$600,000 to \$1,100,000. District Management will review the NYSLRS Retirement Reserve in greater detail, modify the existing reserve plan to a feasible and realistic funding level and amend any wording to distinctly state and execute the long-term appropriation objectives. Unfortunately, the statute does not reference an appropriate funding level for the NYSLRS Reserve Fund.

See
Note 1
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Respectfully,

James Cruikshank
Superintendent

Appendix B: OSC Comment on the District's Response

Note 1

Based on the District's anticipated NYSLRS payments, its goal to maintain the NYSLRS reserve balance at a level equal to two to three years of the District's NYSLRS payments and the reserve's \$3 million balance in 2020-21, the District's excess reserve balance is between \$1.6 to \$2.1 million.

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, District policies, audited financial statements, budgets and financial and reserve plans to gain an understanding of how officials manage fund balance and reserves.
- 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 and assessing whether appropriated fund balance was used to fund operations as planned. We reviewed the 2021-22 budget-to-actual results as of April 11, 2022 and discussed projections with officials to evaluate whether the District will need to use the fund balance appropriated.
- We analyzed the trend in total general fund balance for 2018-19 through 2020-21 and also compared surplus fund balance with the next year's budgeted appropriations to determine whether the District complied with the statutory limit on surplus fund balance.
- We reviewed tax warrants and adopted budgets to identify the trend in the tax levy from 2018-19 through 2022-23.
- We reviewed reserve balances as of June 30, 2021 and compared them to related expenditures and targeted funding levels within the District's reserve policy to assess the reasonableness of reserve amounts.

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

The Board has the responsibility to initiate corrective action. A written corrective action plan (CAP) that addresses the findings and recommendations in this report must be prepared and provided to our office within 90 days, pursuant to Section 35 of General Municipal Law, Section 2116-a (3)(c) of New York State Education Law and Section 170.12 of the Regulations of the Commissioner of Education. To the extent practicable, implementation of the CAP must begin by the end of the next fiscal year. For more information on preparing and filing your CAP, please refer to our brochure, *Responding to an OSC Audit Report*, which you received with the draft audit report. The CAP should be posted on the District's website for public review.

Appendix D: Resources and Services

Regional Office Directory

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

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

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

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www.osc.state.ny.us/files/local-government/publications/pdf/cyber-security-guide.pdf

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