



Hastings-on-Hudson Union Free School District

Financial Condition

Report of Examination

Period Covered:

July 1, 2014 – February 29, 2016

2016M-275



Thomas P. DiNapoli

Table of Contents

	Page
AUTHORITY LETTER	1
INTRODUCTION	2
Background	2
Objective	2
Scope and Methodology	2
Comments of District Officials and Corrective Action	2
FINANCIAL CONDITION	4
Fund Balance	4
Reserves	5
Recommendations	6
APPENDIX A Response From District Officials	7
APPENDIX B OSC Comment on the District's Response	11
APPENDIX C Audit Methodology and Standards	12
APPENDIX D How to Obtain Additional Copies of the Report	13
APPENDIX E Local Regional Office Listing	14

State of New York Office of the State Comptroller

Division of Local Government and School Accountability

November 2016

Dear School District Officials:

A top priority of the Office of the State Comptroller is to help school district officials manage their districts efficiently and effectively and, by so doing, provide accountability for tax dollars spent to support district operations. The Comptroller oversees the fiscal affairs of districts statewide, as well as districts' compliance with relevant statutes and observance of good business practices. This fiscal oversight is accomplished, in part, through our audits, which identify opportunities for improving district operations and Board of Education governance. Audits also can identify strategies to reduce district costs and to strengthen controls intended to safeguard district assets.

Following is a report of our audit of the Hastings-on-Hudson Union Free School District, entitled Financial Condition. This audit was conducted 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.

This audit's results and recommendation are resources for district officials to use in effectively managing operations and in meeting the expectations of their constituents. If you have questions about this report, please feel free to contact the local regional office for your county, as listed at the end of this report.

Respectfully submitted,

*Office of the State Comptroller
Division of Local Government
and School Accountability*

Introduction

Background

The Hastings-on-Hudson Union Free School District (District) is located in the Village of Hastings-on-Hudson in Westchester County. The District is governed by the Board of Education (Board), which is composed of seven elected members. The Board is responsible for the general management and control of District financial and educational affairs. The Superintendent of Schools is the chief executive officer and is responsible, along with other administrative staff, for the District's day-to-day management under the Board's direction.

The District operates three schools with approximately 1,600 students and 270 employees. The District's budgeted appropriations for the 2016-17 fiscal year are approximately \$47 million, funded primarily with real property taxes and State aid.

Objective

The objective of our audit was to review the District's financial condition. Our audit addressed the following related question:

- Did District officials ensure fund balance was maintained in accordance with statutory requirements and reserve levels were reasonable?

Scope and Methodology

We examined the District's financial condition for the period July 1, 2014 through February 29, 2016. We extended our scope period back to July 1, 2010 to analyze fund balance and reserve trends in prior years. Additionally, we calculated the amount of the tax levy increase through the 2015-16 fiscal year using the 2015-16 budget.

We conducted our audit in accordance with generally accepted government auditing standards (GAGAS). More information on such standards and the methodology used in performing this audit are included in Appendix C of this report.

Comments of District Officials and Corrective Action

The results of our audit and recommendations have been discussed with District officials, and their comments, which appear in Appendix A, have been considered in preparing this report. District officials generally agreed with our recommendations and indicated they planned to initiate corrective action. Appendix B includes our comment on an issue raised in the District's response letter.

The Board has the responsibility to initiate corrective action. 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, 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, with a copy forwarded to 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 Board should make the CAP available for public review in the District Clerk's office.

Financial Condition

The Board is responsible for making sound financial decisions that are in the best interests of the District, the students it serves and the residents who fund the District's programs and operations. Prudent fund balance management can help ensure the real property tax levy is not greater than necessary. New York State Real Property Tax Law limits the amount of unrestricted fund balance to no more than 4 percent of the subsequent year's budget.

Additionally, school districts are legally allowed to establish reserves and accumulate funds for certain future purposes (for example, capital projects or retirement expenditures). However, funding reserves at greater than reasonable levels can contribute to real property tax levies that are higher than necessary because excessive reserve balances are not being used to fund operations.

The Board and District officials need to improve the budget process to help ensure fund balance is maintained in accordance with statutory requirements and reserves balances are reasonable. From 2010-11 through 2014-15, the Board appropriated an average of almost \$2.2 million as a financing source in the District's annual budgets. However, because the District incurred operating surpluses in four of these years, the District used only about 2 percent of the fund balance appropriated to fund operations.

The Board has also overfunded reserves by \$4.7 million (88 percent of total reserves) as of June 30, 2015. When the unused appropriated fund balance and excess reserves are added back, the District's recalculated fund balance exceeded the statutory limit, ranging from 19 to 21 percent for the five-year period.

Fund Balance

School districts may retain a portion of fund balance but must do so within the statutory limit. Fund balance represents resources remaining from prior fiscal years. The District may use fund balance to fund operating costs, increase or establish necessary reserves for a specific purpose, pay down debt or pay for one-time expenditures.

Over the past five years (2010-11 through 2014-15), the Board appropriated about \$11.1 million of fund balance in the District's annual budgets. This appropriation of fund balance made it appear that the District's unrestricted fund balance complied with the 4 percent statutory limit. However, the District actually used only about \$216,000 or 2 percent of the appropriated fund balance to finance operations over the same period. When unused appropriated

fund balance and excess reserves are added back, the District's recalculated unrestricted fund balance exceeded the statutory limit, ranging between 19 and 21 percent of the ensuing year's budget.

Figure 1: Unrestricted Fund Balance at Year-End and Unused Fund Balance					
	2010-11	2011-12	2012-13	2013-14	2014-15
Total Unrestricted Funds at Year-End	\$2,683,436	\$2,148,397	\$1,741,581	\$1,600,108	\$1,858,808
Add: Appropriated Fund Balance Not Used to Fund Ensuing Year's Budget	\$1,400,000	\$1,400,000	\$2,250,000	\$2,554,904	\$3,300,000
Add: Excess Reserves	\$4,668,173	\$4,668,173	\$4,964,971	\$5,119,936	\$4,735,556
Total Recalculated Unrestricted Funds	\$8,751,609	\$8,216,570	\$8,956,552	\$9,274,948	\$9,894,364
Recalculated Unrestricted Funds as Percentage of Ensuing Year's Budget	21%	19%	20%	21%	21%

The Board's practice of appropriating fund balance each year that is not needed to finance operations, in effect, circumvents the statutory limit imposed on the level of unrestricted fund balance. Additionally, from 2011-12 through 2015-16, District officials increased the tax levy by approximately 8 percent. As a result, District officials have levied real property taxes that were higher than necessary to fund District operations.

Reserves

The Board may establish reserve funds for specific purposes. It is important that the Board develops a plan for funding the reserves, identifies how much should be accumulated and how and when the funds will be used to finance related costs. School districts should, when necessary, fund reserves in a transparent manner and maintain reserve balances that are reasonable. The Board should review the District's reserves, at least annually, and fund them through budget appropriations to help ensure the amounts reserved are necessary and to provide transparency to District residents. Funding reserves at greater than reasonable levels can result in real property tax levies that are higher than necessary.

As of June 30, 2015, the District had six reserve funds totaling about \$5.3 million, composed of tax certiorari (\$3 million), retirement contribution (\$1.7 million), employee benefit accrued liability (\$252,800), repair (\$200,000), capital (\$150,000) and debt (\$20,200) reserves. While the capital reserve fund was properly established, District officials were unable to provide Board resolutions establishing the remaining reserves. In addition, the amounts maintained in the retirement contribution and tax certiorari reserves were in excess of what the District needs. Finally, the Board generally transferred surplus funds at year-end to fund these reserves instead of funding them through the annual budgets to provide transparency for District residents.

For example, even though the Board had available retirement contribution reserves, it budgeted for and levied real property taxes to fund retirement expenditures. From 2010-11 through 2014-15, the District's budgets included \$3.8 million for the New York State and Local Retirement System and the District made payments totaling \$3.3 million from general fund appropriations, even though the District's retirement contribution reserve had an average balance of \$1.5 million.

Additionally, the Board did not include amounts for tax certiorari payments in the District's annual budgets. The District made payments totaling \$1.1 million from 2010-11 through 2014-15 for these expenditures from the annual operating budgets, even though the District had an average of \$3.2 million in the tax certiorari reserve.

We question the necessity for these two reserves because the Board budgeted for retirement expenditures and paid for certiorari expenditures from the operating budgets each year. We calculated the District was retaining \$4.7 million in reserves as of June 30, 2015 that appeared to be excessive.

Figure 2: Excess Reserves					
	2010-11	2011-12	2012-13	2013-14	2014-15
Retirement Contribution Reserve	\$1,408,000	\$1,408,000	\$1,672,115	\$1,723,787	\$1,736,011
Reserve for Tax Certiorari	\$3,260,173	\$3,260,173	\$3,292,856	\$3,396,149	\$2,999,545
Total Excess Reserves	\$4,668,173	\$4,668,173	\$4,964,971	\$5,119,936	\$4,735,556

The Board has retained excess funds in the reserves rather than use them to fund related expenditures. By not funding reserves through budgeted appropriations and not using reserves for their intended purposes, the Board may have missed the opportunity to use fund balance as a financing source to fund one-time expenditures, fund needed reserves or reduce the tax levy.

Recommendations

The Board should:

1. Discontinue the practice of adopting budgets that result in the appropriation of unrestricted fund balance that will not be used to fund District operations.
2. Review reserves to determine if the amounts reserved are necessary and reasonable. To the extent that they are not, reserves should be properly reduced.

APPENDIX A

RESPONSE FROM DISTRICT OFFICIALS

The District officials' response to this audit can be found on the following pages.

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Roy Montesano
Superintendent of Schools
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November 9, 2016

NYS Comptroller
Thomas P. DiNapoli
Office of the State Comptroller
110 State Street
Albany, NY 12236

Re: District Response to the Comptrollers Audit Report

Dear Comptroller DiNapoli,

The Hastings on Hudson Union Free School is in receipt of the Audit Report "Financial Condition-Period Covered: July 1, 2014 - February 29, 2016".

We would like to thank the Comptrollers local field staff for their professional and courteous manner in which they conducted their audit in the Hastings on Hudson USFSD. The District is pleased that the extensive work of the auditors from your office resulted in no findings of operational improprieties, fraud, waste or abuse.

The District has been mindful in keeping budgets within the tax cap. This approach has allowed our school District to maintain and grow academic and co-curricular programs during the most challenging of economic times. The restrictive nature of a tax levy cap was a major concern in developing budgets. In order to manage the unpredictable future and to maintain a sound education for our students, as well as maintaining a favorable bond rating from Moody's, the Hastings on Hudson UFSD has done what many Districts have done - adopted a very conservative economic philosophy. This philosophy included the use of our reserves and a constant search for efficiencies in the current budget. We have discussed this in detail at public meetings, have made public presentations on the topic and have informed the public about the District's funding and the use of the reserves. Once a budget is adopted, the District continues to strive for any and all efficiencies for the programs and projects that were part of our budget plan. Not only is that approach in the best interest of our taxpayers and students, it is sound economics. The positive balances that are achieved through this process are used to pay it forward in the next year's budget process. This has been a practice in Hastings on Hudson and we feel that it has allowed us to create budgets that do not fluctuate greatly on a year to year basis.

Although it may appear based on the audit period that the District has not needed to maintain the tax certiorari reserve, at its current level, we knew that in the 2016 - 2017 school year we would be paying out over 1 million in settlements that were in the final stages of negotiations. Failure for us to be conservative would have led to a possible depletion of reserves and resulted in a need to bond for repayment on these known

obligations. The board has made an effort to keep the reserve at a reasonable level. The District also does have over thirteen million dollars' worth of current filings outstanding. We feel that the balance as of June 30, 2016 of 2.6 million dollars is an appropriate amount based on the current liabilities. We will continue to monitor our use and level of this reserve to make sure that the appropriate balance is reserved.

The District has been conservative with our use of the Retirement Reserve over the past few years as well. We are very appreciative of the State allowing Districts to reserve funds for future pension obligations. We believe this will allow us to handle the increased liabilities and help keep taxes under the tax cap in the upcoming budget year. The District will be using a large amount of this reserve in the next two budget cycles, to enable the District in keeping tax increases at a minimum, as well as to insure the programs in our schools remain intact. We will be mindful to review the amount kept in this reserve and make sure to release it if we feel it exceeds our needs.


The District believes it is important, and a matter of transparency, to outline the expenditures and revenues that were not included in the Comptrollers Report without the detail it doesn't tell the entire story. The District has tried to keep tax increases at what we feel has been a responsible level. Although it may appear that the District underestimated revenues and overestimated expenditures in the audit scope, we believe we were being financially prudent during these economic times. The District has been very fortunate that over the audit scope we have been able to realize more revenue in it's out of district tuition line. We are never sure at the time of creating the budget what other school districts may be sending students to our programs, because of this we have budgeted the minimum as these placements are not finalized till June. The District was very fortunate to have such a positive reputation that we began to have more students returning and entering our programs during this time. We also were able to expand programs for our special needs students (instead of sending them out of District This is not only a sound educational decision, it also saved the District expenditures in terms of sending those children to an outside program. In addition to these expenditures, the Districts also budgeted very conservatively in the area of healthcare. There were unknown costs associated with the Affordable Health Care roll out as well as budgeted increases in health insurance based upon mid-year estimates that ended up coming in lower than expected. The district also anticipated out of district tuition and residential placements for a small number of our special education students that ended up not being expended. The District also have had unanticipated retirements in some years as well as more favorable contract negotiations that originally thought. We have also been able to save considerably on transportation contracts by rebidding and combining routes. We have been very fortunate to have found cost efficiencies and have been able to use appropriated fund balances to stay within the tax cap.

The Districts has worked closely with our board and community to communicate our philosophy on the use of our reserves. We have been very public and transparent in the amount of fund balance we have and the reason we feel it is important. We have had an overall change in fund balance of 1.1 million dollars from the 2014/2015 school year to the 2015/2016 school year. In response to the comptroller's audit the Districts we anticipate of stepping down the reserve another 1.3 million this year as well as using an additional 1 to 1.2 million dollars to pay off tax certiorari settlements in the 2016/2017 school year. The District also will be using over 500k of the retirement reserve to offset the Employee Retirement System obligations it will have as part of the upcoming school budget.

The Comptrollers Report listed 2 recommendations for the Hasting UFSD. The following is the Districts corrective action plan/response to those recommendations:

- 1) The Board will review past budgets and make adjustments in its estimates in future budgets as deemed to be appropriate.
- 2) The Board intends to use reserves in the development of the 2016-17 budget.

Sincerely,


Roy Montesano
Superintendent of Schools


Eileen Baecher
President, Board of Education

APPENDIX B

OSC COMMENT ON THE DISTRICT'S RESPONSE

Note 1

Our review of District tax certiorari claims indicated that the average settlement rate was approximately 22 percent, bringing the estimated exposure of tax certiorari claims to approximately \$3 million. Although the District has claims outstanding at any given time, during the audit period the District paid \$1.1 million in tax certiorari claims from the operating budget with claims ranging between \$145,000 and \$312,000 each year. The District did not use the reserve during the last five years.

APPENDIX C

AUDIT METHODOLOGY AND STANDARDS

The objective of our audit was to review the District's financial condition. To achieve our audit objective and obtain valid evidence, we performed the following procedures:

- We reviewed the general fund's results of operations and analyzed changes in fund balance for the period July 1, 2010 through June 30, 2015.
- We reviewed the appropriation of fund balance and reserves from July 1, 2010 through June 30, 2015.
- We tested the reliability of the accounting records by comparing the District's independently audited financial statements to the annual financial reports filed with the Office of the State Comptroller.
- We reviewed Board minutes and interviewed officials to determine whether the District's management was involved in financial matters. We also inquired whether management received and reviewed financial reports, analyzed the need for and establishment of reserves and otherwise monitored the District's financial condition.
- We reviewed Board minutes and resolutions to determine if reserve funds were properly established.
- We reviewed the reserve balances for reasonableness and reviewed the activity in each of the reserve funds from July 1, 2010 through June 30, 2015.

We conducted this performance audit in accordance with 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.

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