Office of the New York State Comptroller

Division of Local Government & School Accountability

Rush-Henrietta Central School District

Financial Management and Separation Payments

Report of Examination

Period Covered:

July 1, 2012 – October 30, 2015

2016M-49

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State of New York
Office of the State Comptroller

Division of Local Government
and School Accountability

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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 Rush-Henrietta Central School District, entitled Financial Management and Separation Payments. 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 recommendations 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

State of New York
Office of the State Comptroller

EXECUTIVE SUMMARY

The Rush-Henrietta Central School District (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 the District's financial and educational affairs. The Superintendent of Schools 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 District operates nine schools with approximately 5,300 students and 1,100 employees. The District's budgeted appropriations for the 2015-16 fiscal year were $112.5 million, funded primarily with real property taxes and State aid.

The Assistant Superintendent for Finance supervises all business office functions including the payroll department. The Assistant Superintendent for Human Resources (HR) supervises all functions of the HR department,[1] which is responsible for calculating and approving separation payments.

<u>Scope and Objectives</u>

The objectives of our audit were to review the District's financial management and calculation of separation payments for the period July 1, 2012 through October 30, 2015. Our audit addressed the following related questions:

- Did the Board and District officials effectively manage the District's finances by ensuring that budget estimates and fund balances were reasonable?

- Were separation payments calculated correctly?

<u>Audit Results</u>

The Board did not adopt realistic budgets based on historical or known trends. The Board appropriated fund balance and reserves averaging $5 million each year (5 percent of average appropriations) from fiscal years 2012-13 through 2014-15, which should have resulted in operating deficits and reduced fund balances. However, the Board underestimated non-property tax revenues by 16 to 23 percent and overestimated expenditures by 3 to 7 percent during this time, for total budget variances of more than $35 million. The Board-adopted budgets generated operating surpluses totaling over $20 million over

[1] The Assistant Superintendent for HR started in February 2014 and the personnel clerk started in that position in September 2014. The Assistant Director of HR held that position during the entire audit period.

these three years. As a result, the total $14.9 million in appropriated fund balance and reserves was not needed or used to fund operations. District officials also made unbudgeted interfund transfers totaling $38 million from the capital reserves (reported in the general fund) to the capital projects fund and also made unbudgeted transfers to the District's reserves. Along with the budgeted appropriation of fund balance that has not been used, this has reduced reported year-end fund balance to within the 4 percent limit established by New York State Real Property Tax Law. When adding back unused appropriated fund balance, the District's recalculated unrestricted fund balance has ranged from 5.9 to 6.6 percent of the ensuing year's budget, exceeding the 4 percent statutory limit in each year.

These actions diminish the transparency of District finances. Consequently, two of the District's six general fund reserves, which had balances totaling more than $4 million as of June 30, 2015, are overfunded or potentially unnecessary. The District generally has not used its reserves and instead has covered related costs with tax levies. These results are consistent with the trends we reported on in our audit issued in January 2010.[2]

District officials have not developed written policies or procedures to formalize the process for calculating, reviewing, approving and making separation payments. While payments generally conformed to the terms of the collective bargaining agreements (CBAs), we found that the District paid three retirees $31,603 (5 percent) for payments approved for benefits beyond what was authorized in the CBAs. This includes two employees who were ineligible for separation payments of $25,270 based on their applicable CBAs and one employee who was overpaid $6,333 for more leave time carried over from the previous year than provided for by the CBA. We also question payments to six administrators totaling $18,012 (3 percent) for vacation days carried over from the previous year without Superintendent approval as provided for in the CBA.

Comments of District Officials

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. 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.

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[2] *Rush-Henrietta Central School District – Financial Condition and Internal Controls Over Payroll and Purchasing* (2009M-212), January 2010.

Introduction

Background

The Rush-Henrietta Central School District (District) is located in the Towns of Brighton, Henrietta, Pittsford and Rush in Monroe 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 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 District operates nine schools with approximately 5,300 students and 1,100 employees. The District's budgeted appropriations for the 2015-16 fiscal year were $112.5 million, funded primarily with real property taxes and State aid.

The Assistant Superintendent for Finance supervises all business office functions including the payroll department. The Assistant Superintendent for Human Resources (HR) supervises all functions of the HR department,[3] which is responsible for calculating and approving separation payments.

Objectives

The objectives of our audit were to review the District's financial management and calculation of separation payments. Our audit addressed the following related questions:

- Did the Board and District officials effectively manage the District's finances by ensuring that budget estimates and fund balances were reasonable?

- Were separation payments calculated correctly?

Scope and Methodology

We examined the District's financial management and calculation of separation payments for the period July 1, 2012 through October 30, 2015.

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. Unless otherwise indicated in this report, samples for testing were selected based on professional

[3] The Assistant Superintendent for HR started in February 2014 and the personnel clerk started in that position in September 2014. The Assistant Director of HR held that position during the entire audit period.

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.

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. 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 the issues 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 Management

The Board, Superintendent and Assistant Superintendent for Finance are accountable to District residents for the use of District resources and are responsible for effectively planning and managing the District's operations. One of the most important tools for managing the District's finances is the budget process. District officials must ensure that budgets accurately depict the District's financial activity and effectively use available resources. Prudent fiscal management includes maintaining sufficient and appropriate reserve balances that are needed to address long-term obligations or planned future expenditures. Budget transparency is important for public participation and accountability and allows residents to provide feedback on the quality and adequacy of services as well as decisions that impact the District's long-term financial stability. Presenting complete and accurate budget information to District residents allows them the opportunity to make informed decisions when voting on the budget.

The Board did not adopt realistic budgets based on historical or known trends. The Board appropriated fund balance and reserves averaging $5 million each year from fiscal year 2012-13 through 2014-15, which should have resulted in operating deficits and reduced fund balances. However, the Board underestimated non-property tax revenues by 16 to 23 percent and overestimated expenditures by 3 to 7 percent during this time, for total budget variances of more than $35 million.

The Board-adopted budgets actually generated operating surpluses totaling more than $20 million over these three years. As a result, the total $14.9 million in appropriated fund balance and reserves was not needed or used to fund operations. District officials also made unbudgeted interfund transfers totaling $38 million from the capital reserves (reported in the general fund) to the capital projects fund and also made unbudgeted transfers to the District's reserves. Along with the budgeted appropriation of fund balance that has not been used, this has reduced reported year-end fund balance to within the 4 percent limit established by New York State Real Property Tax Law (RPTL). When adding back unused appropriated fund balance, the District's recalculated unrestricted fund balance has ranged from 5.9 to 6.6 percent of the ensuing year's budget, exceeding the statutory limit in each year.

These actions diminish the transparency of District finances. Consequently, two of the District's six general fund reserves, which had balances totaling more than $4 million as of June 30, 2015, are overfunded or potentially unnecessary. The District generally has not used its reserves and instead has covered related costs with tax levies. These results are consistent with the trends we reported on in our last audit, issued in January 2010,[4] which reported that the District's budgeting practices circumvented statutory controls[5] and resulted in higher tax levies than necessary to fund District operations.

Budgeting and Fund Balance

In preparing the general fund budget, the Board is responsible for estimating what the District will spend and what it will receive in revenue (e.g., State aid), estimating how much fund balance will be available at the fiscal year end for use to help fund the budget and balancing the budget by determining the expected tax levy. Accurate estimates help ensure that the tax levy is not greater than necessary. RPTL allows the District to retain a limited amount of unrestricted fund balance (up to 4 percent of the ensuing year's budget) for unexpected events and to provide for cash flow. Fund balance in excess of that amount must be used to fund a portion of the next year's appropriations – thereby reducing the tax levy – or used to fund legally established and necessary reserves.

The Board adopted budgets that underestimated revenues and overestimated expenditures from fiscal years 2012-13 through 2014-15, which generated budget variances totaling more than $35 million. In the last three years, the Board and District officials underestimated non-property tax revenues by 16 to 23 percent, or more than $21.4 million. They also overestimated expenditures by 3 to 7 percent, totaling more than $13.7 million. These budget variances result in operating surpluses that increased available surplus fund balance.

The District reported an operating surplus in 2012-13 and operating deficits in 2013-14 and 2014-15. However, these operating deficits resulted from unbudgeted interfund transfers[6] totaling $38 million from the capital reserves to the capital projects fund (see Figure 1). Because these were unbudgeted transfers from the capital reserve and not actual general fund operating expenditures, we analyzed the operating results excluding these transfers to determine the reasonableness of the budget estimates and found that the District generated operating surpluses totaling $20 million (an average of $6.8 million a year, 6 percent of the average budget). The Board should include any planned transfers for known capital projects in its adopted budgets to provide a more clear and comprehensive illustration of all planned uses of District resources.

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[4] *Rush-Henrietta Central School District – Financial Condition and Internal Controls Over Payroll and Purchasing* (2009M-212), January 2010.

[5] Which limit year-end unrestricted unappropriated fund balance to 4 percent of the ensuing year's budget

[6] These transfers were not budgeted but were Board-approved and for voter approved projects through propositions.

Figure 1: Underestimated Revenues and Overestimated Appropriations				
	2012-13	2013-14	2014-15	Total
Estimated Revenue [a]	$32,370,972	$34,732,342	$38,009,266	$105,112,580
Actual Revenues	$39,713,091	$42,748,689	$44,055,636	$126,517,416
Variance	$7,342,119	$8,016,347	$6,046,370	$21,404,836
% Variance	23%	23%	16%	20%
Appropriations	$103,900,495	$107,549,087	$110,253,694	$321,703,276
Actual Expenditures [b]	$96,586,561	$103,870,288	$107,486,245	$307,943,094
Variance	$7,313,934	$3,678,799	$2,767,449	$13,760,182
% Variance	7%	3%	3%	4%
Total Budget Variance	**$14,656,053**	**$11,695,146**	**$8,813,819**	**$35,165,018**
Operating Surplus [b]	$8,811,503	$6,890,395	$4,685,663	$20,387,561
Capital Reserve Unbudgeted Transfers to Capital Projects Fund	$2,236,730	$14,693,388	$21,756,831	$38,686,949
District Reported Operating Surplus/(Deficit)	$6,574,773	($7,802,993)	($17,071,168)	($18,299,388)

[a] We did not include real property taxes (RPT) in our analysis of budgeted versus actual revenues because, generally, all taxes levied are received. For perspective, the tax levy in the 2012-13 through 2014-15 budgets averaged approximately $67.2 million.
[b] Does not include interfund transfers made from the capital reserve to the capital projects fund because these were not budgeted and are not actual general fund operating expenditures.

Expenditure variances were generally spread throughout budget items with the largest consistent variance for Program for Students with Disabilities – Med Eligible, which was overestimated a total of $3.9 million (12 percent). District officials told us that these expenditures are subject to change throughout the year based on enrollment of special needs students, and they plan for potential additional costs. The most significant revenue variance was the underestimation of State aid by at least 10 percent in each of the last three years for a total of $10.7 million. District officials told us that they intentionally do not budget for building and transportation aid because they transfer it to the capital reserves based on voter approval of propositions establishing the reserves, which include State aid as a potential funding source. The Assistant Superintendent for Finance transferred more than $8.8 million in aid to reserves, which accounts for 82 percent of the underestimated State aid revenue.[7] Excluding known revenues from the adopted budget is not a sound or transparent budget practice and causes unnecessary budget variances. Furthermore, the Board did not formally authorize the transfer of specific types and amounts of State aid to specific reserves.

The Board also appropriated fund balance and reserves totaling approximately $14.9 million[8] during this time, which should have resulted in operating deficits and reductions in fund balance and

[7] At our April 20, 2016 exit conference, the Assistant Superintendent for Finance told us that the remaining $1.9 million aid variance was attributable to the School District Performance Improvement and Management Efficiency Grant programs, for which District officials felt the amount and timing of award and receipt of grant funds was too uncertain to include in the budget.

[8] $7.2 million in fund balance and $7.7 million from reserves

reserves. However, the District did not need to use any of the fund balance appropriated for operations due to the operating surpluses, as indicated in Figure 2. While the general fund's total fund balance has declined over the last three years, the District's budgets did not provide transparent information to District residents. The District should include in its annual budgets any planned uses of fund balance to fund reserves or capital projects, to more accurately communicate how it will use resources each year and give residents the opportunity to make informed decisions when voting on the budget.

Figure 2: Unrestricted Fund Balance at Year-End

	2012-13	2013-14	2014-15
Beginning Fund Balance	$42,300,168	$48,874,949	$41,114,473
Prior Period Adjustments	$8	$42,517	$291,980
Add: Operating Surplus/(Deficit) [a]	$6,574,773	($7,802,993)	($17,071,168)
Ending Fund Balance	$48,874,949	$41,114,473	$24,335,285
Less: Restricted Funds	$39,933,134	$31,537,716	$15,065,120
Less: Encumbrances	$2,639,852	$2,966,622	$1,818,858
Less: Appropriated Fund Balance for the Ensuing Year	$2,000,000	$2,200,000	$2,950,000
Unrestricted Fund Balance at Year-End	$4,301,963	$4,410,135	$4,501,307
Ensuing Year's Budgeted Appropriations	$107,549,087	$110,253,694	$112,533,282
Unrestricted Funds as a Percentage of Ensuing Year's Budget	4%	4%	4%

[a] Operating surplus/(deficit) calculation (revenues less expenditures) includes interfund transfers.

Because District officials made unbudgeted transfers to the capital projects fund, appropriated fund balance to fund operations and funded reserves at year-end, the District reported year-end unrestricted fund balance that complied with the 4 percent statutory restriction for fiscal years 2012-13 through 2014-15. However, when adding back unused appropriated fund balance, the District actually exceeded the limit in each year as indicated in Figure 3.

Figure 3: Unused Fund Balance

	2012-13	2013-14	2014-15
Unrestricted Funds at Year-End	$4,301,963	$4,410,135	$4,501,307
Add: Appropriated Fund Balance Not Used to Fund Ensuing Year's Budget	$2,000,000	$2,200,000	$2,950,000
Recalculated Unrestricted Funds	$6,301,963	$6,610,135	$7,451,307
Recalculated Unrestricted Funds as a Percentage of Ensuing Year's Budget	5.9%	6.0%	6.6%

During 2014-15, the District appropriated $2,950,000 for the 2015-16 budget; however, we project that it will not be needed and the District's unrestricted fund balance will likely continue to exceed the statutory limit. The District's practice of appropriating fund balance that is not needed to finance operations is misleading and, in effect, a reservation of fund balance that is not provided for by statute.

Reserves

School districts may establish reserves, in compliance with law, to restrict a reasonable portion of fund balance for a specific purpose to address long-term obligations or planned future expenditures. District officials should adopt a detailed policy or plan governing the establishment, use and funding levels or goals of reserve funds. While school districts are generally not limited as to how much money can be held in reserves, reserve balances must be reasonable. Funding reserves at greater than reasonable levels contributes to real property tax levies that are higher than necessary because the excessive reserve balances are not being used to fund operations.

The District's reserve funds represent a significant portion of total fund balance (82 percent in 2012-13 and 62 percent as of June 30, 2015). The Board does not budget to fund reserves and typically funds the reserves with year-end surpluses and unbudgeted transfers of State aid. This method of funding reduces transparency and does not provide District residents with an opportunity to vote on how funds are used. In addition to the $8.8 million in State aid transferred to reserves and $965,023 of unrestricted fund balance transferred by the Board in February 2014 to start the employee benefit accrued liability reserve (EBALR), the Assistant Superintendent for Finance transferred an additional $7.9 million of unrestricted fund balance to reserves after year-end with Board approval.[9] In addition, the Board-approved budgets included projected uses of almost $7.7 million of reserve money to finance operations from fiscal years 2012-13 through 2014-15. However, these appropriated reserve funds were not needed or used because of operating surpluses generated by inaccurate budget estimates.

The District had six reserves with balances totaling more than $15 million as of June 30, 2015.[10] We evaluated the reserve funds for reasonableness and adherence to statutory requirements. Four of these reserves had reasonable balances: workers' compensation ($2 million), tax certiorari ($1.5 million), EBALR ($1.3 million) and capital reserves[11] ($6.2 million).

We also found that the Board took appropriate corrective action after our last audit and eliminated two previous reserves. The Board

[9] This includes a total of $334,499 that the Assistant Superintendent for Finance transferred to the EBALR without documented Board approval. The Assistant Superintendent for Finance told us that when the District updated its calculation for total sick leave liability at the end of the year, he transferred the necessary funds to the reserve based on the Board's intent for the reserve balance to equal the total liability.

[10] Reduced from more than $31.5 million as of June 30, 2015

[11] This includes the 2009 and 2016 bus reserves and the 2015 capital reserve. We reviewed the 2011, 2012 and 2014 capital reserves during testing, but these reserves were closed out by the end of the 2014-15 year.

appropriately moved $8.3 million from the unauthorized other post-employment benefit reserve and dissolved the unnecessary insurance reserve by transferring its $7.9 million balance to the capital reserve to be used for upcoming capital projects. Finally, we found that the unemployment insurance and retirement contribution reserves had excessive and unnecessary balances. Specifically:

- Unemployment Insurance Reserve – This reserve is used to fund payments made when a school district elects to reimburse the New York State Unemployment Insurance Fund for actual claims filed.[12] As of June 30, 2015, the reserve had a balance of $2 million. Although the funding of this reserve is within the Board's established funding level,[13] District officials did not have documented support for the need for this funding level.

  The Assistant Superintendent for Finance told us that there are no anticipated future expenditures. Additionally, the reserve has not been used in at least the last three years, and the Board overestimated these expenditures in the budget. Therefore, the funding for this reserve is excessive.

- Retirement Contribution Reserve – This reserve is authorized to make contributions for employees covered by the New York State and Local Retirement System. This reserve was significantly overfunded at the end of 2013-14 at $15.3 million, but the Board took action to reduce the balance. In March 2015, the Board adopted a resolution to reduce the reserve by $13.3 million. As of June 30, 2015, the reserve had a balance of more than $2 million. Other than the transfer, this reserve has not been used in at least the last three years. We question the necessity for this reserve when the Board budgets for these expenditures and has not needed to use the reserve.

Because the District does not include the funding of reserves in the annual budgets, but instead funds reserves with year-end surpluses, District officials have not provided District residents with accurate and transparent budget information. In addition, retaining unsubstantiated and potentially excessive reserve balances effectively increases the

[12] A Board resolution is required to establish an unemployment insurance reserve. District officials were unable to provide us with a Board resolution establishing this reserve because the reserve was created more than 30 years ago, and the Board did not adopt a new resolution after our last audit.

[13] The Board's reserve plan states that the targeted funding level is approximately 4 percent of payroll or $2.2 million, which would support up to 100 employees' unemployment claims if extended benefit periods are enacted as they were in the prior recession.

amount by which the District has exceeded statutory fund balance limits. For example, the addition of the two unsupported reserve balances to the unrestricted fund balance and unused appropriated fund balance as of June 30, 2015 (see Figure 3), equates to 10 percent of the 2015-16 budget.

By maintaining excessive fund balance, both restricted and unrestricted, and not using the fund balance and reserves appropriated in adopted budgets, District officials are levying more taxes than necessary to sustain District operations. In addition, some current budgeting practices circumvented statutory controls and resulted in excessive fund balance that exceeded the statutory limitation of 4 percent of the ensuing year's budget.

District officials have tried to be transparent in their actions related to budgeting and finances, including presenting some details in public forums and on the District website and by creating a budget advisory council composed of administrators, staff, students, parents and other residents.[14] However, they are not being fully transparent and have taken minimal action to remedy the inaccurate budget estimates. In the 2015-16 budget, the Board did not appropriate any money from reserves to align with prior years' non-use of reserves and appropriated $750,000 more in unrestricted fund balance, thereby reducing the amount of appropriated fund balance and reserves by $1.3 million from the 2014-15 budget. The Board increased expenditure estimates by $2.27 million (even though prior year expenditures were less than estimates) and increased revenue estimates by $3.58 million (due, in part, to the reduction of appropriated fund balance and reserves). Consequently, the general fund will again likely recognize significant budget variances and an operating surplus, which will again increase fund balance in 2015-16.

Recommendations

The Board should:

1. Develop and adopt budgets that reflect the District's actual needs and plans and include realistic estimates for revenues, expenditures and fund balance use based on historical trends and other identified analysis.

2. Include planned funding of reserves in its adopted budget each year to provide increased knowledge and transparency to the District's voters.

3. Approve all transfers to reserves before they are made.

[14] The council was formed in 1995 to allow greater community involvement in the development of the proposed budget.

4. Review the reserves to determine if the amounts reserved are necessary and document support to justify the targeted funding levels. If deemed necessary, the Board should research the origin of the existing unemployment reserve and if unable to determine the origin of the reserve, reestablish the reserve in conformance with General Municipal Law. To the extent that they are not necessary, transfers should be made to other reserves established and maintained in compliance with statutory directives or used to benefit the District.

Separation Payments

In addition to established wages and salaries, school districts often provide separation payments to employees for all or a portion of their earned but unused leave time when the employee retires or otherwise leaves district service. These payments are an employment benefit generally granted in negotiated collective bargaining agreements (CBAs) or individual employment contracts and can represent significant expenditures. As such, District officials must ensure that employees are paid only the amounts to which they are entitled by ensuring each payment is accurate and authorized by a Board-approved employment contract. As a rule, changes to provisions of a CBA should be negotiated and agreed to by the parties to the agreement.

The District has four CBAs that stipulate terms and benefits for its employees. The District also has management confidential (MC) employees that are not part of a union. District officials told us that these employees follow the administrator CBA unless there is specific Board authorization for other benefits.[15] All of the CBAs include provisions for eligible employees to receive a payment upon separation from the District.

After an employee notifies the HR department of intent to retire or resign, the HR department provides the information to the Board for approval.[16] The personnel clerk reviews the applicable CBA to determine what separation payments the employee may be entitled to and will calculate the separation payment on a personnel directive form. Depending on the employee's CBA, the form is provided to either the Assistant Superintendent of HR or Assistant Director of HR for review and approval.[17] There is no supporting documentation provided with the form for review. Instead, the reviewer must access the financial software to look up information used in the calculation, such as the number of leave days available for payment. Separation payments (number of unused leave days and total dollar amount) are provided to the Board for approval. District officials have not developed written policies or procedures to formalize this process.

There were 269 employees who retired, resigned or otherwise separated from the District during our audit period, of which 101 received separation payments totaling $576,837. We judgmentally selected 19

15 For purposes of this audit, we have assumed the propriety of the District applying the CBA provisions to these MC employees (see, generally, Office of the State Comptroller Opinion No. 87-54 [revised]).

16 The HR department generally provides a list of separations that would include any terminations that originated in the HR department.

17 The Superintendent reviewed and approved the calculations for former Assistant Superintendents of HR.

employees[18] with separation payments totaling $195,925 (34 percent) to review the terms of separation and determine if the payments were properly calculated per Board-approved contract terms.

While these payments generally conformed to the terms of the CBAs, we found that the District paid three retirees $31,603 (5 percent) for payments approved for benefits over what was authorized in the CBAs. This includes $25,270 to two employees who were ineligible for separation payments based on their applicable CBAs and an overpayment of $6,333 to one employee for more leave time carried over from the previous year than provided for by the CBA. We also question payments to six administrators totaling $18,012 (3 percent) for vacation days carried over from the previous year without Superintendent approval, as required by the CBA.

The HR department calculated and the Superintendent approved a $25,753 payment to the former Assistant Superintendent of HR/Organization Development who did not meet all of the "qualifying conditions" for eligibility for certain payments, based on the terms of the CBA followed for this employee.[19] The Board approved this amount, which included $12,150 for unused sick time, $7,000 as payment in lieu of life insurance and $6,603 for unused vacation days. Only the $6,603 for unused vacation days was properly authorized.

Although the Board stated in the minutes that it approved the payment for unused sick leave "in accordance with the" administrator CBA, this employee did not meet all of the qualifying conditions for a separation payment for unused sick leave under this CBA. In particular, this employee did not submit an irrevocable letter of intent to retire at least six months in advance of the retirement date, as required by the CBA. Board members told us that they were aware that the individual did not meet certain eligibility requirements when they approved the payment. However, the Board minutes did not document any legal rationale for making this payment. The CBA also stipulated that an employee must have a minimum of 10 years of service with the District to receive life insurance in retirement. Because the employee had only six years of service, the employee did not meet the requirement set forth in the CBA. Instead, the Board authorized a $7,000 payment in lieu of life insurance. There is no provision in the CBA for such a "cash in lieu of" payment and we are aware of no State statute that would authorize a school district to provide such a cash payment by Board resolution.

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[18] We selected 10 retirees with separation payments totaling $178,431 and nine non-retirement separations with separation payments totaling $17,494. See Appendix C, Audit Methodology and Standards, for further details on the sample selection.

[19] This is an MC employee who follows the administrator contract.

The HR department calculated and approved a $6,120 separation payment for unused sick leave to a teacher who did not meet all of the listed qualifying conditions for eligibility based on the terms of the applicable CBA. The CBA requires the employee to file an irrevocable letter of intent to retire by February 1 of the school year in which the retirement will take place and retire at the end of the school year in which the request is made to be eligible for a payment of unused sick days.

Although the teacher retired in October 2014 (well after the end of the school year), HR staff told us that they thought the employee was eligible because she provided notice of intent to retire by the February deadline. However, this is only one of the eligibility conditions. Because the teacher did not retire at the end of the school year as required, she did not meet all of the listed qualifying conditions to receive a separation payment. On November 4, 2014, the Board stated in the minutes that it approved the $6,120 payment "in accordance with the" teachers' CBA. Board members told us that they rely on the review and approval process in the HR department to determine eligibility and payment amounts.

The HR department calculated and the Superintendent approved a separation payment to the former Assistant Superintendent of HR/School Operations[20] totaling $37,333 for unused sick and vacation time. The CBA followed for this employee provides for the carryover into the subsequent year of up to two weeks of vacation leave (10 days), due to "unusual circumstances," with Superintendent approval. However, the separation payment included 20 days of vacation leave carried over, 10 more days than allowed per contract (if the proper approvals were received). The only documentation provided regarding the additional leave days carried over was the employee's retirement letter, which stated that per previous discussions with the Superintendent, he would be allowed to carryover any unused days beyond the contractual limit of 10 days.

Although the Board approved the total payment (number of vacation days and amount), the express language in the CBA limits the carryover of vacation days, with the approval of the superintendent, to two weeks. Therefore, it appears this individual was overpaid $6,333 for these additional 10 vacation days beyond the maximum set forth in the CBA followed for this employee.

We also question payments to six administrators totaling $18,012 for vacation days carried over from the previous year without approval as provided for in the CBA.[21] The CBA states that due to "unusual

[20] This is an MC employee who follows the administrator contract.

[21] This total excludes payment for the 10 days overpayment previously discussed, but includes the first 10 days carried over for this individual.

circumstances," an employee may request the Superintendent to allow a maximum of two weeks of the earned but unused vacation to be carried forward into the subsequent year. However, the payroll and HR departments have allowed administrators to carryover up to two weeks unused vacation leave without Superintendent approval. A Board member told us that the Board encourages the administrators to use leave and would not expect to see a large amount of leave time carried over. Nonetheless, the express language in the CBA does not provide for carryover absent Superintendent approval. We question the appropriateness of the carryover of vacation time and the subsequent payment of the unused days carried over.

We believe it is not appropriate to provide benefits in excess of those set forth in the CBA or to depart from qualifying conditions in a CBA, absent agreement by the parties. Providing alternative arrangements allows for the appearance of favoritism. Documenting, in writing, policies and procedures for making separation payments in accordance with the terms and conditions of CBAs would help prevent any confusion or misunderstandings regarding the benefits due.

Recommendations

The Board should:

5. Review the inappropriate separation payments identified in this report with the District's legal counsel and take appropriate action within the law to recover those payments deemed inappropriate.

The Superintendent should:

6. Approve any permissible carryover of administrator vacation days as provided for in the CBA.

District officials and staff should:

7. Develop procedures to govern separation payments to ensure they are consistent with the terms and conditions of CBAs.

8. Ensure that separation payments are made according to the terms of the negotiated CBAs. Changes to these terms should be agreed to by the parties.

APPENDIX A

RESPONSE FROM DISTRICT OFFICIALS

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

Rush-Henrietta Central School District

www.rhnet.org

May 13, 2016

Edward V. Grant, Jr., Chief Examiner
Division of Local Government and School Accountability
Office of the State Comptroller
The Powers Building
16 West Main Street – Suite 522
Rochester, New York 14614

Dear Mr. Grant:

We wish to acknowledge receipt of the findings and recommendations outlined in your recent "Report of Examination" of the Rush-Henrietta Central School District for the period of July 1, 2012, through October 30, 2015. Some of your observations will assist us in improving our practices so we have already implemented changes.

While we value the opinions of the Comptroller, we would like those reading the audit report to understand that in general, the budget comments focus solely on single-year budgeting practices without regard to a long-term strategy that has served our district and taxpayers well for many years.

See Note 1 Page 22

At the most local of levels, a Board of Education must balance its responsibility to be both fiscally responsible to the community and to deliver sound educational programs to students. At the same time, the board must abide by the many constraints placed upon us by state and federal laws, regulations, and mandates. The Rush-Henrietta Board of Education, elected by the local residents, spends a great deal of time developing budgets that balance all of these priorities.

In fact, the board's strategic multi-year practice has enabled the district to deliver a 2015-16 true value tax rate that is 2 percent lower than the 2005-06 tax rate, continue to have the lowest tax rate in the county, and maintain one of the lowest debt levels in the state. With more than 75 percent of our residents approving our budgets in each of the past five years, our community members recognize the value of our stable tax rates and continued fiscal responsibility. Moody's continues to affirm our Aa2 credit rating, despite our dwindling fund balance and even Gov. Cuomo has recognized our good fiscal processes, awarding our district with a $1.9 million Management Efficiency grant.

See Note 2 Page 22

See Note 3 Page 22

While the recommendations may result in a single-year tax levy reduction, they will result in significant changes in later years. Instead, the Rush-Henrietta Board of Education believes our residents prefer a stable, consistent, and predictable tax rate.

See Note 4 Page 22

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Financial Management

A critical factor in the budget-setting process is the parameter that state law does not allow the board to exceed the budget. Using historical averages as suggested by the Comptroller, would have significant impact on students in years where expenditures trend above average. If a rainy day is not planned for – and suddenly arrives – this could result in severe mid-year program reductions for students. Therefore, similar to many fiscally healthy school districts, our Board of Education incorporates flexibility into the budget. This flexibility is funded with "appropriated fund balance" (accumulated savings) rather than increasing the tax levy. Please note, the appropriated reserves and fund balance has decreased by almost 50 percent from the 2012-13 budget to the 2015-16 budget as the district continues to tighten budgeting processes.

See Note 5 Page 22

We find the comment in the report that states, "The Board should include any planned transfers for known capital projects in its adopted budgets to provide a more clear and comprehensive illustration…" to be illogical. Residents see each proposed capital proposition, including planned reserve transfers, separately so they explicitly understand what they are approving. If we also budget the planned reserve transfers in our operating budget it would make the operating budget opaque and grant the same spending authorization twice for a single project.

See Note 6 Page 22

Budgeting and Fund Balance

For decades, the Rush-Henrietta Board of Education has endorsed - and our district voters have approved – propositions for the establishment of Capital Reserves to be funded by "any and all state aid." The district has a long history of paying cash, and avoiding millions of dollars in financing fees, for most of its capital projects. This has been accomplished, with voter approval, by directing all state aid from prior capital projects into capital reserves for future capital projects. Since the intent was not to use this money for operating expenses, they were not budgeted for in the General Fund. Although the board endorsed, and the voters approved, this process the district agrees it could be even more transparent by also including these amounts in the budget. Effective immediately, we will budget both the anticipated building aid to be received and the associated transfer to capital.

See Note 7 Page 22

In addition, the district was awarded $3.9 million in governor's performance grants over a three-year period. During the second year of funding, the Comptroller ruled these revenues must be accounted for in the General Fund. This, combined with the uncertainty of the annual renewal and timing, made it impossible to budget these in the General Fund. If these were properly excluded from the "underestimated revenue," calculation the real difference is closer to 3 percent rather than the 16 percent to 23 percent portrayed.

See Note 8 Page 23

To put this further in perspective, the $35.2 million in budget variance noted in the report is only 5 percent of the total $643 million revenue and expenditure budgets for the three years. Furthermore, if we reduce the $35.1 million by transfers to capital reserves and supplemental performance grants, the total variance is $22.4 million, or 3 percent. We do not deem this to be unreasonable.

Figure 2 shows the proper way to calculate Unrestricted Fund Balance. This clearly demonstrates that the district is in statutory compliance. Figure 3 as presented in your report is creative, but contrary to State Education Department guidance on how to calculate this. Our auditors assure us we are in compliance with the statutory requirements as defined by SED and shown in Figure 2.

See Note 9 Page 23

Reserves

Each year, the Rush-Henrietta Board of Education reviews and adopts a "Strategic Plan for Use of Reserves." This shows each reserve, establishes a targeted reserve amount, and explains the proper legal requirements to fund the reserve. Figure 2 in the Audit Report shows "Restricted Funds" or reserves have decreased in excess of 50 percent during the audit period. Since reserves are not a

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recurring revenue stream, the district does not consider it fiscally prudent to utilize them for ongoing operational expenses. This is why Unemployment and Retirement reserve balances haven't been utilized in the past three years. They are intended for unusual, infrequent circumstances and not for recurring operational expenses.

Year-end surpluses are used to fund reserves or applied to the ensuing year's budget to reduce the need for a tax levy increase. This is criticized in the Comptroller's report. As you should know, it is impossible to precisely budget exact spending amounts so there will be variances. Incredibly, following the Comptroller's guidance would have us unnecessarily expending funds so as to not have a surplus; we consider this to be an unwise use of taxpayer funds. More prudent is to direct these surplus funds to reserves as the board is legally entitled to do for more thoughtful future use.

See
Note 10
Page 23

Separation Payments

Another area reviewed by the Comptroller was separation payments made to employees when they leave the district's employment, either through retirement or resignation. Most separation payments are in accordance with the district's Collective Bargaining Agreements that cover the vast majority of the district's employees. It is the responsibility of the Board of Education to review and approve all Collective Bargaining Agreements prior to their implementation.

More than 1,100 employees work full time for the district so it is impossible to include all possible scenarios and conditions in a single document. This is especially true in a complex environment covered by union contracts, state Civil Service law, and federal and state labor and tax laws. It is occasionally in the best interests of the district to enter into a unique type of separation agreement. These are always approved by the Board of Education, just as the board has to approve all Collective Bargaining agreements. The district's attorney assures us these types of unique agreements are under the legal purview of the Board of Education.

See
Note 11
Page 23

Finally, the report mentions the vacation carryover days allowed under the CBA as long as they are approved by the Superintendent. Traditionally, the Superintendent had delegated this responsibility to the Human Resources department but to ensure there is no confusion the Superintendent will approve these directly as recommended in the report.

The Board of Education will certainly take into consideration the Comptroller's observations and opinions as it continues to formulate the strategic financial and instructional priorities for the district.

Very truly yours,

Diane E McBride

Diane McBride
President, Board of Education

J. Kenneth Graham, Jr.

J. Kenneth Graham, Jr., Ph.D.
Superintendent of Schools

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APPENDIX B

OSC COMMENTS ON THE DISTRICT'S RESPONSE

Note 1

Our findings and recommendations focus on practices used over the last three years and are consistent with the trends reported on in our previous audit report. Planning for operating deficits by appropriating fund balance, while underestimating revenue and overestimating expenditures and, therefore, not using the appropriated fund balance, is not a transparent means of communicating financial plans and financial condition to District residents.

Note 2

Our report discusses the tax levy, not the tax rate. The tax levy has increased by more than $12 million over the last 10 years.

Note 3

Bond rating services analyze the risk to investors of an entity's indebtedness. They are not concerned if excess funds of the District's residents are accumulated. Our audit analyzed the District's finances on behalf of the residents. We would not characterize the general fund balance as "dwindling" because the money has been transferred to the capital projects fund and is still on hand for future use.

Note 4

A budget based on accurate estimates helps ensure the tax levy is not greater than necessary and can produce a stable, consistent and predictable tax rate.

Note 5

Appropriated fund balance is intended to finance anticipated expenditures in lieu of additional taxes and reduce surplus fund balance. Flexibility to meet unanticipated expenditures and revenue shortfalls is provided by unexpended fund balance and reserves.

Note 6

Including planned transfers to the capital projects fund in the budget would present all planned expenditures and offsetting revenues in a comprehensive and transparent format. Voters approved using reserve money for projects, but did not approve the timing and amounts of the transfers, which is the purpose of the annual budgets. Including planned transfers in the budget would not constitute approval to spend or transfer the same funds twice.

Note 7

The propositions state that the source of the reserve funding shall be determined by the Board and may be transferred from, among other sources, any and all State aid. This allows Board discretion and does not provide for all aid to be automatically transferred to reserves. Regardless, the State aid is general fund operating revenue and should be included in the operating budget.

Note 8

The District's calculation in the response is incorrect. If the $3.9 million was excluded from the underestimated non-property tax revenue, the variance for the three year period would be 17 percent.

Note 9

Our report does not say the District was not in compliance with the statutory requirement. We say that when unused appropriated fund balance is added back, the District actually exceeded the limit in each year. The practice of appropriating fund balance that is not needed to finance operations is misleading, and, in effect, a reservation of fund balance that is not provided for by statute.

Note 10

Our report does not suggest making unnecessary expenditures. The report recommends adopting accurate budgets to help ensure that the tax levy is not greater than necessary rather than the current practice of annually generating surpluses.

Note 11

The District did not provide any Board-approved separation agreements for the three retirees who received benefits that exceeded those authorized in the CBAs.

APPENDIX C

AUDIT METHODOLOGY AND STANDARDS

The objectives of our audit were to examine the District's financial management and calculation of separation payments for the period July 1, 2012 through October 30, 2015. To achieve our audit objectives and obtain valid evidence, we performed the following procedures:

- We interviewed District officials and staff to gain an understanding of the District's budgeting process and processing and approval of separation payments.

- We reviewed the results of operations and analyzed changes in fund balance for the period July 1, 2012 through June 30, 2015. To gain additional background information and for perspective, we also reviewed financial data for reserves prior to the audit scope period.

- We compared the adopted budgets to actual operating results (in total and for individual line items) to determine if budget estimates were reasonable.

- We reviewed the appropriation of the District's reserves and fund balance and compared the appropriation to actual use. We calculated the adjusted unrestricted fund balance to include consistent unused portions of appropriated fund balance and compared it to ensuing year budget appropriations.

- We reviewed Board minutes, resolutions and other documentation to determine if reserve funds were created, funded and expended properly, and if transfers were appropriate.

- We reviewed the Board-adopted reserve plan, supporting documentation and reserve balances to determine if balances were reasonable.

- We reviewed the negotiated CBAs to identify terms authorizing separation payments.

- The District provided data directly from its computerized financial software and we analyzed it electronically using computer-assisted techniques.

- We reviewed Board minutes, inquired with District officials and reviewed the results of the analysis of the electronic data to identify all separation payments made during our scope period.

- We reviewed records for all 269 employees who left District service to determine if they were eligible for a separation payment.

- We selected a judgmental sample of 19 previous employees with separation payments totaling $195,926 (34 percent) to determine if payments were made according to CBAs or other Board authorizations.

- o There were 71 retirees who received separation payments totaling $530,908. We selected a judgmental sample of 10 retirees with separation payments totaling $178,431 (34 percent). We selected all four administrators/MC employees and two individuals from each of the other three CBAs.

- o There were 30 non-retirees who received separation payments totaling $45,297. We selected a judgmental sample of nine non-retirement separations with separation payments totaling $17,494 (39 percent). We selected all five administrators and two individuals from each of the other two CBAs (the remaining contract provided for separation payments only at retirement). During testing we found that one individual we had classified as an administrator was not an administrator but part of a different CBA. We still included this individual in our sample for testing.

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 objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

APPENDIX D

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