

Rush-Henrietta Central School District

Strategic Plan for Use of Reserves

2015 - 2016

September 2015

Overview

The establishment and funding of reserves is an important consideration in the maintenance of a sound financial plan for any school district. While strict adherence to state law is required to ensure reserves are both legal and appropriate, adequately funded reserves are vital to the long-term health and stability of the school district. This concept is recognized by the New York State Comptroller:

Saving for future projects, acquisitions, and other allowable purposes is an important planning consideration for local governments and school districts. Reserve funds provide a mechanism for legally saving money to finance all or part of future infrastructure, equipment, and other requirements. Reserve funds can also provide a degree of financial stability by reducing reliance on indebtedness to finance capital projects and acquisitions. In uncertain economic times, reserve funds can also provide officials with a welcomed budgetary option that can help mitigate the need to cut services or to raise taxes. In good times, money not needed for current purposes can often be set aside in reserves for future use. (*Office of the New York State Comptroller – Local Government Management Guide – Reserve Funds, Pg. 1*)

The Rush-Henrietta Central School District believes that the judicious use of reserves greatly reduces long term borrowing costs, smoothes large fluctuations in tax rates and minimizes the effect of mid-year budget cuts which would have a direct impact on students. It believes it is in the best interest of both the students and taxpayers to prudently establish and use reserves to weather the financial storms and uncertainties that will occur. Again, the Comptroller notes:

The practice of planning ahead and systematically saving for capital acquisitions and other contingencies is considered prudent management. Saving for future capital needs can reduce or eliminate interest and other costs associated with debt issuances. Similarly, certain reserve funds can be utilized to help protect the budget against known risks (a potential lawsuit) or unknown risks (a major ice storm). (*Office of the New York State Comptroller – Local Government Management Guide – Reserve Funds, Pg. 2*)

This quote reflects the two purposes for the establishment of reserves:

1. Saving money for a large, one time future expenditure. A capital reserve for the replacement of a roof is an example.
2. Reserves which are intended to protect the district against a large, currently unknown risk. An insurance liability reserve is an example of this type.

Since New York State law mandates that expenditures can be no greater than the budget approved by the voters in May, the Rush-Henrietta Central School District budgets conservatively to ensure that unanticipated expenditures do not result in mid-year budget cuts which would have an immediate impact on students. This practice has allowed the district to weather mid year sales tax reductions, state aid holdbacks and significant fuel cost fluctuations without impacting instructional programs. However, conservative budgeting can also result in budget surpluses at year-end. The Board of Education reviews any budget surpluses and determines the best use of these surpluses including transfers to voter or board of education approved reserves or to a reduction in the ensuing year's tax levy. This budgeting practice has been endorsed by the Moody's Rating Agency, which has rated Rush-Henrietta's bonds as Aa2 and commented on the district budgeting practices:

“We expect the district to maintain a sound financial position over the medium term due to ongoing expenditure controls and conservative budgeting practices.”

Moody's also listed the district's strengths as:

- Strong reserve levels
- Tax base stability
- Manageable debt profile with rapid amortization

Legally established reserves can provide many benefits to the school district and to its taxpayers. However, these reserves can also cause confusion when their purpose is not clearly understood by the community. The purpose of this document is to detail Rush-Henrietta's plan for use and maintenance of reserves.

In addition to reserves the District's General Fund, Unassigned Fund Balance will be maintained at or close to the 4% allowed by law to provide the District with financial stability and a margin of safety to fund unanticipated contingent expenditures that may occur unexpectedly during the fiscal year. The Unassigned Fund Balance also provides the cash flow necessary to fund school activities from July 1st through mid September when property taxes start to be received.

The following page shows the General Fund Balance Sheet from the annual Basic Financial Statements which include the reserve balances as of June 30, 2015 and June 30, 2014:

Rush-Henrietta Central School District

General Fund - Summarized Balance Sheet

June 30, 2015 and June 30, 2014

	<u>2015</u>	<u>2014</u>	<u>Variance</u>
<u>Fund Balance and Reserves</u>			
Workers' Compensation Reserve	\$1,987,428	\$1,986,201	\$1,227
Unemployment Insurance Reserve	2,002,411	2,001,175	\$1,236
Retirement Contribution Reserve	2,017,683	15,307,210	(\$13,289,527)
Tax Certiorari Reserve	1,524,925	1,523,984	\$941
Employee Benefits & Accrued Liability Res.	1,301,087	1,008,493	\$292,594
Capital Reserves	6,231,586	9,710,653	(\$3,479,067)
Encumbrances	1,818,858	2,966,622	(\$1,147,764)
Designated Fund Balance - Ensuing Year	2,950,000	2,200,000	\$750,000
Undesignated Fund Balance	4,501,332	4,410,147	\$91,185
Total Fund Balance and Reserves	\$24,335,310	\$41,114,485	(\$16,779,175)

WORKERS' COMPENSATION RESERVE

Authority: The purpose of this reserve fund is to pay for compensation benefits and other expenses authorized by the Workers' Compensation Law, and for payment of expenses for administering this self-insurance program. The reserve may be established by board action and is funded by budgetary appropriations and such other funds as may be legally appropriated (General Municipal Law, §6j).

Balance June 30, 2015: \$1,987,428

Balance June 30, 2014: \$1,986,201

Targeted Balance: Three to four years worth of an average year's payment, which average over \$700K per year, plus adequate coverage for prior year claims still outstanding.

Discussion: Rush-Henrietta Central School District is self insured for workers compensation up to \$100,000 per case. Claims can remain open for years so this reserve protects against both the cumulative effect of lagging claims and an abnormally large payout for a settled claim. Our estimated future liability for current outstanding claims is about \$700,000 so the current reserve would cover these plus about 1.5 years of premiums. Additionally, recent NYS Workers Compensation law changes have increased employer costs significantly. Our annual costs have increased over 50% from a few years ago.

UNEMPLOYMENT INSURANCE RESERVE

Authority: This reserve fund is used to pay the cost of reimbursement to the State Unemployment Insurance Fund for payments made to claimants. The reserve may be established by board action and funded by budgetary appropriations or other funds as may be legally appropriated (General Municipal Law, §6-m).

Balance June 30, 2015: \$2,002,411

Balance June 30, 2014: \$2,001,175

Targeted Balance: Approximately 4% of payroll or \$2,200,000. This would support up to 100 employees' unemployment claims if extended benefit periods are enacted as they were in the prior recession.

Discussion: Because of limited state aid increases, the Property Tax Levy Cap and growing benefit costs the likelihood of job cuts are becoming more probable. Although current claims have fallen from their post-recession peak the risk of a need for significant layoffs remains real as the Property Tax Levy Cap is often lower than contractual wage and benefits increases.

RETIREMENT CONTRIBUTION RESERVE

Authority: The governing board of a school district, by resolution, may establish a reserve for the purpose of financing retirement contributions made to the NY State and Local Employees' Retirement System. Establishing or expending the reserve does not require voter approval. Expenditures may only be made pursuant to a board resolution and must be used to finance retirement contributions (General Municipal Law, §6-l).

Balance June 30, 2015: \$ 2,017,683

Balance June 30, 2014: \$15,307,210

Targeted Balance: The expected long term contribution rate for the Employees Retirement System is approximately 12% of salaries, if the retirement fund earns 7.5% on its investments. Recently the State Comptroller lowered his expected rate of return to 7.0%, which is 1% lower than the Teacher Retirement System. This, combined with an increased life expectancy assumption, will make it very unlikely that the district's contribution rate will fall to 12% in the next few years. Over the last few years our average rate has ranged between 15% and 20%. The target balance would be able to cover the difference from the long term target for up to five years.

Discussion: The purpose of this reserve is to set aside available surplus to provide a source of funds to limit the property tax impact of increases in employer contribution rates for the Employees Retirement System. This reserve was authorized by the state legislature in reaction to the significant increases in retirement contribution rates that municipalities and school districts

were facing. The district anticipates funding this reserve when retirement rates are below long term averages and utilizing it when rates exceed long term averages.

TAX CERTIORARI RESERVE

Authority: The governing board of any school district, by resolution, may establish a reserve to refund taxes of the current year in tax certiorari proceedings. Establishing or expending the reserve does not require voter approval. Amounts not necessary to refund taxes must be returned to the unreserved fund balance of the general fund by the first day of the fourth fiscal year following the year for which the reserve was created. (Education Law §3651, Sub.1a, 3a)

Balance June 30, 2015: \$1,524,925

Balance June 30, 2014: \$1,523,984

Targeted Balance: Between 50% and 100% of open cases.

Discussion: Ideally this reserve should be adequate to cover between 50% and 100% of the outstanding tax certiorari cases. It is not unusual for a lawsuit to cover multiple years of assessment for large taxpayers so potential judgments may be significant. The current reserve level is 41% of the open 2014 cases. The amounts of settlements can vary greatly from year to year so this reserve protects against large, unbudgeted settlements.

EMPLOYEE BENEFIT ACCRUED LIABILITY RESERVE

Authority: The governing board of any school district, by resolution, may establish a reserve for the purpose of funding the monetary value of accrued but unused sick leave, personal leave, vacation time, and any other forms of payment of accrued but unliquidated time earned by employees that may be due upon termination of the employee's service. Establishing or expending the reserve does not require voter approval. Expenditures may only be made for allowed cash payments earned by employees due upon their termination of employment (General Municipal Law, §6-p).

Balance June 30, 2015: \$1,301,087

Balance June 30, 2014: \$1,008,493

Targeted Balance: fully fund entitlements due employees upon leaving employment.

Discussion: This reserve is for contractual benefit entitlements that will be paid directly upon an employee's termination. It does not include post-employment health benefits under GASB 45. New York State has not yet developed a method to fund that multi-million dollar liability. Rush-Henrietta's employee benefit accrued liability supports earned, but not used, sick and personal days.

REPAIR RESERVE

Authority: The Repair Reserve Fund is used to pay the cost of repairs to capital improvements or equipment, which repairs are of a type not recurring annually. Voter approval is required to fund this reserve. Expenditures from this reserve may be made only after a public hearing has been held, except in emergency situations. If no hearing is held, the amount expended must be repaid to the reserve fund over the next two subsequent fiscal years (General Municipal Law, §6-d).

Balance June 30, 2015: \$0

Balance June 30, 2014: \$0

Targeted Balance: Projected costs of future repairs on non-instructional buildings.

Discussion: Rush-Henrietta Central School District has not maintained this reserve because no state aid is paid for expenditures from this reserve. Since school renovations tend to generate building aid it is more advantageous to fund from capital reserves. However, projects at the West Henrietta Education Building and the Parker Administration do not qualify for state aid so at a future date the board may want to consider funding this reserve.

CAPITAL RESERVES

Authority: The Capital Reserve Fund is used to pay the cost of any object or purpose for which bonds may be issued. Voter authorization is required for both the establishment of the reserve and for payments from the reserve. The form of the required legal notice for the vote on establishing the reserve and the form of the proposition to be placed on the ballot are set forth in §3651 of the Education Law.

Balance June 30, 2015: \$4,970,089

Balance June 30, 2014: \$6,512,175

Targeted Balance – may not exceed the voter authorized limit for each reserve, plus accumulated interest earnings. Normal, routine maintenance projects which had been postponed because of Phase III were funded in the amount of \$12 million from this reserve in 2013-14. This was partially replenished with the 2013-14 building aid and excess fund balance. Funding for the \$19 Million Full Day Kindergarten and District Reconfiguration project approved by the voters in 2014-15 came from the liquidation of the GASB45/ERS Reserve along with funding from this Capital Reserve.

Discussion: The Rush-Henrietta Central School District has used capital reserves to its advantage for many years. A capital reserve allows the District to save money in anticipation of

a renovation or addition to a building. Using saved cash, rather than borrowing, for building projects offers the district two advantages:

1. The use of cash financing avoids the interest charges and debt issuance costs associated with borrowing to accomplish the same result.
2. The current building aid formula provides state aid to the District for cash expenditures as if it had borrowed. That is, state aid is provided on interest expenses, even though those expenses were avoided. This provides a future revenue stream to the budget.

In short, the use of cash financing through capital reserves is prudent financial planning, avoids the expense of bond interest and increases state aid available to the district. In order to replenish the reserve the Board of Education has authorized that state aid for projects paid for by utilizing the capital reserve is used to replenish this reserve.

BUS RESERVE

Authority: The Bus Reserve Fund is a capital reserve specified to be used to pay for bus purchases. Voter authorization is required for both the establishment of the reserve and payments from the reserve.

The form of the required legal notice for the vote on establishing the reserve and the form of the proposition to be placed on the ballot are set forth in §3651 of the Education Law.

Balance June 30, 2015: \$1,261,497

Balance June 30, 2014: \$3,198,478

Targeted Balance – may not exceed the voter authorized limit of \$12 million, plus accumulated interest earnings. Voter authorized funding totaling \$2.6 million for the 2015-16 bus purchases to include extra buses for the impact of the district reconfiguration. The bus reserve was partially replenished by the bus purchase aid received this year.

Discussion: Currently, the district's bus purchase plan replaces buses when they reach approximately 100,000 miles and ten years of age. Beyond this, bus maintenance costs begin to increase sharply as equipment ages. This plan serves to keep our fleet current, while stabilizing the tax rate as the number of buses replaced varies. Also, bus purchase costs have increased significantly over the last five years as a result of enhanced anti-pollution requirements. A combination of budget and reserve funding ensures the total cost is not too onerous to district taxpayers.

DEBT SERVICE RESERVE

Authority: The Mandatory Reserve for Debt Service Fund is used to hold the proceeds of a bond issuance in excess of the capital expenditures funded by the bonds. A Board of Education resolution is required for the establishment of the reserve and payments can only be made for

debt service or retirement of outstanding bond obligations. The legal basis of this reserve is set forth in §6-1 of General Municipal Law.

Balance June 30, 2015: \$284,947

Balance June 30, 2014: \$231,441

Targeted Balance – any bond proceeds not fully expended for its targeted capital expenditure must be placed in this reserve. Expenditures may only be made to pay interest and principal for these bonds or to reduce the amount of outstanding bonds.

Discussion: The Rush-Henrietta Central School District issued bonds to fund the Burger / Roth Middle School renovations. At the completion of the project \$231,143 of borrowed funds had not been expended. Therefore, these funds, plus accumulated interest, must be kept in reserve and used to fund debt service for the bonds issued for this project. When a bond refunding for outstanding TOC bonds was undertaken in 2013-14 a Debt Service Fund was established and these funds were moved to the new Debt Service Fund. Therefore, they are no longer part of the General Fund.

INSURANCE RESERVE

Authority: This reserve fund is used to pay judgments, claims, incidental costs and professional services connected with the investigation and settlement of claims. The reserve is funded by budgetary appropriations or any other permissive referendum. The amount that can be paid into the reserve during each fiscal year is limited to 5% of the annual budget. There is, however, no limit upon the amount which may be accumulated in the fund (General Municipal Law, §6-n).

Balance June 30, 2015: \$ 0

Balance June 30, 2014: \$ 0

Targeted Balance: approximately 5% of the annual budget would provide protection against large deductibles and sharp premium increases.

Discussion: Rush-Henrietta buildings are valued at over \$260 million. The district plan has a 10% deductible for any claims. This reserve would help fund these deductibles plus is an excellent tool to mitigate against sharp premium increases that occasionally happen in the insurance markets. Currently this reserve is not utilized but funding may be considered in the future.

PROPERTY LOSS RESERVE AND LIABILITY RESERVE

Authority: This reserve fund is used to pay for property loss and liability claims incurred. Separate funds for property loss and liability claims are required and these reserves may not in

total exceed 3% of the annual budget or \$15,000 whichever is greater. (Education Law, §1709, Subdivision 8-c).

Balance June 30, 2015: \$0

Balance June 30, 2014: \$0

Targeted Balance: 3% of the annual budget.

Discussion: This reserve is not intended for use on an ongoing basis; rather, it protects the District in the case of a catastrophic event. Rush-Henrietta carries \$10 million of liability insurance but would be responsible for any judgments in excess of this amount. Currently this reserve is not utilized but funding may be considered in the future.

RESERVE FOR ENCUMBRANCES

Authority: Governmental Accounting Standards Board (GASB) requires the district to recognize purchase commitments that will be expended in a future period. The Reserve for Encumbrances is the amount of purchase commitments made at year-end where the goods won't be received until the following fiscal year.

Balance June 30, 2015: \$1,818,858

Balance June 30, 2014: \$2,966,622

Targeted Balance: This reserve must equal the value of outstanding purchase obligations to be satisfied.

Discussion: This required reserve recognizes that purchase commitments were made from a current budget but the goods won't be received until a future period. This ensures that funds used to pay for purchases are aligned with their intended funding sources (budget year or identified capital project). The reserve sets aside the funds for these commitments. Under GASB54 there is no longer a reserve for encumbrances but rather these commitments are identified in "Assigned" fund balance.

In addition to reserves the district also has an Assigned Appropriated and Unassigned fund balance. These fund balances are used for the following purposes:

ASSIGNED APPROPRIATED FUND BALANCE

Purpose: Planned reduction in fund balance to reduce the property tax levy necessary to support the current budget.

Balance June 30, 2015: \$2,950,000

Balance June 30, 2014: \$2,200,000

Targeted Balance: An appropriation of fund balance represents a non-recurring revenue that cannot be anticipated to be available in the ensuing year's budget. Overuse can cause the depletion of available fund balance, ultimately leading to spikes in the property tax rate. Therefore there should be a consistent use rather than large variation in application. As the Property Tax Cap continues there will be ongoing budget reductions so it is believed that the amounts available for appropriated fund balance will be constrained over the next few years.

UNASSIGNED FUND BALANCE

Purpose: Used to fund expenditures from July through September of the ensuing year prior to the inflow of property tax receipts. Also provides a source of funds for unanticipated increases in expenditures, decreases in revenue and interruptions in cash flow.

Balance June 30, 2015: \$4,501,332

Balance June 30, 2014: \$4,410,147

Targeted Balance: by law, the unassigned fund balance is limited to 4% of the ensuing year's budget. This is generally considered to be the ideal balance.