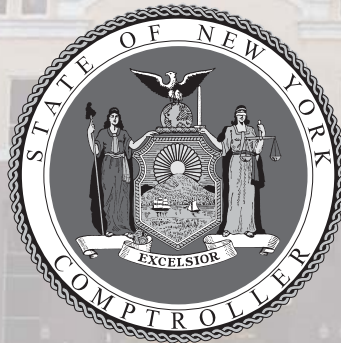




Boards of Cooperative Educational Services

Transparency and Appropriateness of Reserve Funds

2010-MS-4



Thomas P. DiNapoli

Table of Contents

	Page
AUTHORITY LETTER	2
EXECUTIVE SUMMARY	3
INTRODUCTION	5
Background	5
Objective	6
Scope and Methodology	6
Comments of BOCES Officials	6
TRANSPARENCY AND APPROPRIATENESS OF BOCES RESERVES	7
Transparency to School Districts and Taxpayers	8
Documented Plans for Reserve Funds	9
Statutory Authority	11
Recommendations	13
APPENDIX A BOCES' Reserve Balances on June 30, 2009	15
APPENDIX B BOCES' Reserve Balances, by Category, on June 30, 2009	16
APPENDIX C Responses From BOCES Officials	17
APPENDIX D Audit Methodology and Standards	22
APPENDIX E How to Obtain Additional Copies of the Report	23
APPENDIX F Local Regional Office Listing	24

State of New York Office of the State Comptroller

Division of Local Government and School Accountability

July 2010

Dear Board of Cooperative Educational Services (BOCES) Officials:

A top priority of the Office of the State Comptroller is to help BOCES officials manage BOCES resources efficiently and effectively and, by so doing, provide accountability for tax dollars spent to support BOCES operations. The Comptroller oversees the fiscal affairs of BOCES statewide, as well as BOCES' 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 operations and Board of Education governance. Audits also can identify strategies to reduce BOCES costs and to strengthen controls intended to safeguard BOCES assets.

Following is a report of our audit of Boards of Cooperative Educational Services titled Transparency and Appropriateness of Reserve Funds. 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 General Municipal Law.

This audit's results and recommendations are resources for BOCES 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

A Board of Cooperative Educational Services (BOCES) is a public organization whose primary function is to provide cooperative educational programs and services to its component and participating school districts. New York State has 37 BOCES, each of which comprises component school districts that elect the members of their respective BOCES' Board of Education (Board). The Board is responsible for establishing policies and procedures, including documented plans for the funding and use of reserves. BOCES' costs are funded primarily by charges to component and participating school districts for BOCES services, and also by Federal and State grants or aid.

It is common practice for BOCES to reserve monies for specific purposes. Education Law and General Municipal Law define the types of reserves that BOCES can maintain. All reserves must be established by Board resolution. The 37 BOCES in New York State reported to the State Education Department (SED) that their general fund reserves¹ were \$128 million as of June 30, 2008 and \$149 million as of June 30, 2009. Although the six BOCES included in this audit (Capital Region, Madison-Oneida, Erie 1, Nassau, Rockland, and Western Suffolk) reported reserves to SED totaling \$88.5 million at June 30, 2009, our examination determined that these BOCES actually had \$110 million² in 30 general fund reserves at June 30, 2009.

Scope and Objective

The objective of our audit was to determine if BOCES reserved excessive fund balance without informing their component and participating school districts for the period July 1, 2007 to June 30, 2009. For historical activity, we reviewed reserve fund data from July 1, 2005 through June 30, 2007. Our audit addressed the following related question:

- Do BOCES officials notify component and participating school districts of the moneys being reserved, establish policy guidance for funding and using reserves, and ensure that all reserves are legally authorized, properly established and adequately supported?

¹ Excludes reserves for encumbrances

² We excluded reserves for encumbrances. The Erie 1 BOCES erroneously reported three reserves in its reserve for encumbrances. It had reported them correctly in the audited annual financial statements. In addition, the Rockland BOCES inappropriately reported a long-term liability totaling more than \$14 million for future retiree health insurance expenses in its general fund statements, effectively understating fund balance. Since there is no authority to fund other post employment benefits (OPEB) such as these currently, we treated these moneys as an unauthorized reserve balance in certain calculations.

Audit Results

We found that BOCES are reserving funds without clearly reporting to their component and participating districts, and to the taxpayers who ultimately fund BOCES operations. Further, BOCES are reserving millions of dollars in excessive balances, some of which are used inappropriately or maintained in reserves that are not allowed by law.

Of the almost \$110 million reserved by the six BOCES as of June 30, 2009, we found that the allocation of \$30.5 million to reserves during the audit period was not clearly reported to districts. If these BOCES reported allocations to reserves in prior years in the same manner they currently do, then they did not clearly inform districts how and why they reserved the entire \$110 million in reserves, as well as another \$19.5 million that they already spent from the reserves during the audit period. BOCES' failure to clearly report the existence of reserves, why they are needed, and how they are being funded reduces transparency to component and participating school districts and taxpayers. Transparency requires that BOCES officials disclose all the aspects of their finances, including the moneys BOCES allocate to reserves.

These BOCES maintained \$79 million (72 percent) in 27 reserves that were not authorized, not adequately supported, or not properly used. We determined that \$26.3 million was in eight reserves that BOCES are not legally authorized to establish, and \$52.7 million was in 19 reserves that BOCES could not document a need for by means of liability calculations or use plans; \$29.9 million in two of these unsupported reserves was not used as allowed by law. Each of the six BOCES had one or more unsupported reserves. By not establishing specific plans for how reserves will be used, and not maintaining schedules to support and set reasonable funding levels, BOCES are reserving excessive funds that would otherwise be returned to school districts, and potentially to taxpayers to reduce their tax levies. There is no statutory limit on the amount BOCES can maintain in most reserves, but reserves should not be a "parking lot" for excess cash or fund balance. Further, when BOCES establish unauthorized reserves, or use reserves for improper purposes, they are using school district monies in an inappropriate manner.

Comments of BOCES Officials

The results of our audit and recommendations have been discussed with BOCES officials and their comments, which are included in Appendix C, have been considered in preparing this report.

Introduction

Background

A Board of Cooperative Educational Services (BOCES) is a public organization whose primary function is to provide cooperative educational programs and services to its component and participating school districts.³ New York State has 37 BOCES, each of which comprises component school districts that elect the members of their respective BOCES' Board of Education (Board). The Board is responsible for establishing policies and procedures, including documented plans for the funding and use of reserves. BOCES' costs are funded primarily by charges to component and participating school districts for BOCES services, and by Federal and State grants or aid.

The use of reserve funds is common among BOCES. Reserves are typically funded from amounts raised through the annual budget process, transfers from unexpended balances of existing appropriations, and surplus monies. Education Law and General Municipal Law (GML) define the types of reserves that BOCES can maintain, and require that such reserves be established by Board resolution; some reserves must also be approved by a majority of the component school districts' boards of education.⁴

The 37 BOCES in New York State reported to the State Education Department (SED) that their general fund reserves⁵ were \$128 million as of June 30, 2008 and \$149 million as of June 30, 2009. The six BOCES included in this audit (Capital Region, Madison-Oneida, Erie 1, Nassau, Rockland, and Western Suffolk) reported that their reserves totaled \$88.5 million at June 30, 2009. However, our review of these BOCES' financial statements determined that these BOCES actually maintained approximately \$110 million in 30 general fund reserves⁶ at June 30, 2009.

³ Component school districts (BOCES members) provide most of the funding for BOCES facilities and services. BOCES also serves "participating" school districts, which elect to participate in one or more selected BOCES programs, and are billed accordingly.

⁴ For example, a career and technical equipment reserve

⁵ Excludes reserves for encumbrances

⁶ We excluded reserves for encumbrances. The Erie 1 BOCES erroneously reported three reserves in its reserve for encumbrances. It had reported them correctly in the audited annual financial statements. In addition, the Rockland BOCES inappropriately reported a long-term liability totaling more than \$14 million for future retiree health insurance expenses in its general fund statements, effectively understating fund balance. Since there is no authority to fund other post employment benefits (OPEB) such as these currently, we treated these moneys as an unauthorized reserve balance in certain calculations.

The following chart shows the June 30, 2008 and June 30, 2009 reserve balances for the six BOCES we audited:

BOCES	June 30, 2008 Reserve Balance	June 30, 2009 Reserve Balance
Madison-Oneida	\$8,326,605	\$8,397,482
Capital Region	\$6,589,122	\$8,298,410
Erie 1	\$6,868,719	\$8,487,370
Rockland ⁷	\$21,283,128	\$21,194,991
Nassau	\$38,964,955	\$44,733,863
Western Suffolk	\$19,216,597	\$18,878,759
Totals	\$101,249,126	\$109,990,875

Objective

The objective of our audit was to determine if BOCES reserved excessive fund balance without informing their component and participating school districts for the period July 1, 2007 to June 30, 2009. For historical activity, we reviewed reserve fund data from July 1, 2005 through June 30, 2007. Our audit addressed the following related question:

- Do BOCES officials notify component and participating school districts of the moneys being reserved, establish policy guidance for funding and using reserves, and ensure that all reserves are legally authorized, properly established and adequately supported?

Scope and Methodology

We examined the minutes of Board proceedings, accounting records, financial statements, BOCES policies and procedures, and other relevant documentation of six BOCES for the period July 1, 2007 to June 30, 2009. For historical reserve fund activity, we reviewed reserve fund data for the period July 1, 2005 through June 30, 2007.

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 D of this report.

Comments of BOCES Officials

The results of our audit and recommendations have been discussed with BOCES officials and their comments, which appear in Appendix C, have been considered in preparing this report.

⁷ Includes a liability accrual that Rockland BOCES is using to fund future post-employment health insurance costs; this is discussed in detail in the individual report for the Rockland BOCES.

Transparency and Appropriateness of BOCES Reserves

BOCES can legally reserve funds for specific future uses to help reduce their reliance on operating funds or borrowed moneys. However, because BOCES funds are derived primarily from component and participating school districts, it is essential that BOCES officials clearly inform districts, and their taxpayers, why any reserves are needed, how moneys will be allocated to reserves, and how those moneys will be used. Such disclosure provides for transparency in BOCES finances and accountability for school district and taxpayer dollars. Further, while there is no statutory limit on the amount BOCES can maintain in most reserves, reserves should not be a “parking lot” for excess cash or fund balance. Rather, each reserve should be maintained at a level that is reasonable and appropriate to fund the future expenditures or liabilities it was established to pay for, as indicated in a clearly documented plan for the reserve. BOCES officials are allowed to create only those reserves allowed by statute, and may use reserved funds only for the specific purpose defined by statute.

Generally, we found that BOCES are reserving funds without clearly reporting to their component and participating districts, and to the taxpayers who ultimately fund BOCES operations. The six BOCES we audited had 30 reserve funds, totaling almost \$110 million, as of June 30, 2009.⁸ We found that \$30.5 million allocated to reserves during the audit period were not clearly reported to districts. If these BOCES reported allocations to reserves in prior years in the same manner they do currently, the entire balance of \$110 million, as well as amounts already spent⁹ from the reserves, was also not reported clearly.

Furthermore, we found that \$79 million in 27 reserves, or 72 percent of these BOCES’ total reserves, were not supported with liability calculations or documented use plans, were not used in accordance with statute, or were not authorized by statute. (See Appendix B for details of these reserves, by BOCES.) More specifically:

- \$52.7 million in 19 reserves was not supported with liability calculations or specific funding and use plans;

⁸ See Appendix A. Some June 30, 2009 data was unaudited and prior to year-end adjustments.

⁹ During our audit period, \$19.5 million was spent from the reserves.

\$29.9 million in two of these unsupported reserves was not used in accordance with statute.

- \$26.3 million was in eight reserves that were not specifically authorized by statute.

We found that each of the six BOCES had one or more unsupported reserves. BOCES' failure to clearly report the existence of reserves, why they are needed, and how they are being funded, reduces transparency to component and participating school districts and taxpayers. Transparency requires that BOCES officials disclose all the aspects of their finances, including the moneys BOCES allocate to reserves. Also, by not establishing specific plans for how reserves will be used and setting reasonable funding levels for them, BOCES are reserving excessive funds that would otherwise be returned to school districts, and potentially to taxpayers to reduce their tax levies. Further, when BOCES establish unauthorized reserves, or use reserves for improper purposes, they are using school district monies in an inappropriate manner.

Transparency to School Districts and Taxpayers

Ideally, amounts to be put in reserve funds should be included as separate items in the annual budget. It is important that BOCES officials clearly identify allocations to reserves, and not include budgetary appropriations to fund reserves with other budgeted operating expenditures in a manner that obscures their purpose. When a BOCES' proposed budget explicitly indicates the board's intent to raise resources for one or more reserve funds, the board gives its school districts and those districts' voters and residents the opportunity to know about and react to the board's plan for funding its reserves.

However, during our two-year audit period, we found that the six BOCES we audited used \$25.3 million¹⁰ in budgetary appropriations and \$5.3 million in operating surplus to fund reserves without informing districts that they were reserving these funds. At all six BOCES, budgetary appropriations used to fund reserves were included as operating expenditures for fringe benefits in the individual Cooperative Service Agreement (CoSer)¹¹ budgets. This practice does not clearly indicate that these moneys are allocated to reserves; rather, they appear as budgeted operating expenditures.

¹⁰ This amount does not include funding from transfers from other reserves.

¹¹ A CoSer is the structure a BOCES uses to manage the services it provides to its school districts. Each BOCES submits an annual CoSer application to SED for approval of the programs and services it offers to districts.

Further, five of the six BOCES used operating surplus to fund reserves without informing school districts that they planned to use any resulting surplus to fund reserves. At the end of the fiscal year, three of these five BOCES gave surplus reports to each of their component and participating school districts. Surplus reports indicate the surplus (or refund due) that is payable to that school district by the CoSer for that year. However, the amounts the BOCES retained for funding reserves were not clearly identified as such in these reports; instead, they were factored into the total expenditure amounts for CoSer services. The other two BOCES that funded reserves with operating surplus did not provide any surplus reporting to component and participating school districts. Because the BOCES consistently classified the moneys they used to fund reserves as fringe benefit expenditures, rather than funds used to create or add to BOCES reserves, it appears likely that these allocations were made without the knowledge of component and participating school districts and district taxpayers.

BOCES officials and board members at all six BOCES indicated that reserve funding and use was discussed verbally with school district officials. However, none of the six BOCES could provide written documentation that information on the funding and use of reserve funds was provided to all component and participating school districts. Such lack of disclosure compromises the transparency of BOCES operations and denies the school districts complete knowledge of how BOCES is ultimately using money paid by districts for BOCES services.

Documented Plans for Reserve Funds

Although there is no statutory limit on the amount that can be maintained in most reserves, the balances in statutorily authorized reserves should be reasonable and based on intended future expenditures or estimated liabilities. Reserving more than necessary in a reserve is not appropriate: this practice idles funds that belong to school districts and taxpayers. It is important that BOCES officials develop a clearly documented plan for each reserve, including how the reserve is intended to be used, and how and at what level it will be funded. The plan should require that schedules or other documentation be maintained to track the amount of the liability or other specific future use the reserve was established to fund.

However, we found that the BOCES we audited had no plans or documentation to support 63 percent of the money they maintained in 22 legal reserves. The six BOCES had 22 authorized reserve funds, totaling \$83.7 million, as of June

30, 2009; BOCES officials had no plans or supporting documentation for 19 of these reserve funds,¹² with balances totaling \$52.7 million. BOCES officials did not provide any evidence to indicate how they planned to fund these reserves, how much they planned to accumulate in the reserves, and ultimately how the reserved funds would be spent. Further, \$29.9 million in two of these reserves was being used for purposes that were not allowed by law.

BOCES officials were able to support the reserve balance in the remaining three legal reserves and portions of two other reserves, totaling approximately \$31 million, with intended future expenditures or estimated liabilities. These intended future expenditures included compensated absences benefits due to employees upon separation from employment, and actual accounts payable liabilities, as follows:

- Erie 1 BOCES and Western Suffolk BOCES had compensated absences worksheets to support their employee benefit accrued liability reserves totaling \$21.7 million.
- Capital Region BOCES had documentation of a disputed outstanding liability with a telecommunication provider to support its property loss reserve of about \$1 million.
- Nassau BOCES had compensated absences worksheets to support the proper use of \$7.6 million, a portion of its employee benefit accrued liability reserve totaling \$33.5 million.¹³
- Madison Oneida BOCES had compensated absences worksheets totaling about \$1 million to support its employee benefit accrued liability reserve that had a balance of \$1.3 million.

The informal manner the BOCES used to maintain millions of dollars in 19 reserves for undisclosed purposes does not properly account for school districts' funds. BOCES boards do not require that a plan be formulated, with the reserve's purpose and

¹² Two of these reserve funds were partially supported; the supported portions of these reserves were not included in the total unsupported balance.

¹³ Nassau BOCES inappropriately used the remaining \$25.9 million in this reserve to pay for retiree health insurance. We classified these amounts as unsupported reserve balance, and discuss the improper use of this reserve in the "Statutory Authority" section of this report.

funding needs identified, before the reserve is approved. Such a plan should also identify the laws or regulations that authorize each reserve, state how each reserve will be funded (whether from budgetary appropriations or from allocation of operating surplus), specify funding limits for the reserve, and require board review on a regular basis to verify the reasonableness of the amounts reserved. BOCES should also maintain schedules, when applicable, to support reserve balances and funding levels.

We found that, of the six BOCES we audited, four had not developed any policies or specific documented funding and use plans for reserve funds. Erie 1 and Western Suffolk BOCES had taken steps toward developing such policies, as follows:

- During our fieldwork, Erie 1 BOCES officials prepared written plans for four of their five reserve funds; they had previously created written procedures for a fifth reserve, an employee benefit accrued liability reserve. However, these written plans were not approved by the board, and required more specific information on the funding and use of reserve funds to provide adequate guidance.
- At Western Suffolk BOCES, the Board resolutions that established the reserve funds included calculations for specific limits on reserve funding. While setting limits is useful, it is also important to define each reserve's statutory authority, purpose, funding methods, and documentation requirements.

In response to these findings, BOCES officials indicated that they are not required by statute or any other regulation to have written plans for reserve funds. This is true. However, BOCES officials do have a responsibility to the school districts they serve to reserve only reasonable amounts of funds for necessary and appropriate uses. Plans for managing reserves, including specific guidance for the funding and use of reserve funds, provides for control over these moneys, and accountability for how BOCES use them. Because such controls were not in place, these six BOCES accumulated a total of \$52.7 million in reserves without providing evidence of the purpose and appropriateness of the reserves, or the reasonableness of the amounts reserved.

Statutory Authority

BOCES are allowed to create only those reserves that are specifically authorized by statute. GML and Education Law authorize BOCES to establish certain reserves for specific uses stated in the law. BOCES are not authorized to create reserves to

pay for retiree health insurance benefits, workers' compensation benefits, or retirement incentives. In addition, authorized reserves may be used only for the specific purpose of the reserve, as defined by statute. However, as of June 30, 2009, these six BOCES had \$56.1 million in 10 reserves that either lacked statutory authority or were used inappropriately.

All six BOCES we reviewed have established reserves that they lack authority to have and/or used an authorized reserve (employee benefit accrued liability reserve) for purposes not authorized by statute. These unauthorized reserve balances, totaling \$56.1 million are detailed as follows:

Unauthorized BOCES Reserve Balances at June 30, 2009						
Reserve	Madison-Oneida	Capital Region	Erie 1	Rockland	Nassau	Western Suffolk
Retiree Health Insurance	\$6,426,847	-	-	\$14,670,719 ¹⁴	-	-
Employee Benefit Accrued Liability	-	\$3,971,854	-	-	\$25,905,866	-
Workers' Compensation	-	\$1,092,321	\$331,227	\$931,281	-	\$2,475,184
Teachers' Retirement Incentive	-	-	\$302,499	-	-	-
Section 803 ¹⁵	-	-	-	\$32,976	-	-
Total by BOCES	\$6,426,847	\$5,064,175	\$633,726	\$15,634,976	\$25,905,866	\$2,475,184

Workers' Compensation – Currently, there is no statutory authority for a BOCES to create a workers' compensation reserve. However, in four of the six BOCES reviewed, BOCES had established a Workers' Compensation Reserve to pay workers' compensation claims or for the BOCES cooperative workers' compensation program, a self-insurance program. As of June 30, 2009, the four BOCES had accumulated a total of \$4.8 million in these reserves. BOCES officials generally stated that they did not realize that BOCES are not authorized to create such reserves. BOCES officials also contend that the statute regarding workers' compensation reserves is unclear.

¹⁴ Represents a liability accrual that Rockland BOCES is using to fund future post-employment health insurance costs; this is discussed in detail in the individual report for the Rockland BOCES.

¹⁵ Retirement and Social Security Law, Section 803, provides for retroactive membership in the New York State and Local Employees' Retirement System for public employees who failed to file an application for retirement system membership.

Other Post-Employment Benefits – Currently, there is no statute under GML or Education Law allowing the creation of a reserve for post-retirement health insurance premiums, otherwise known as other post-employment benefits. However, one of the six BOCES reserved \$6.4 million specifically for retiree health insurance. Another BOCES improperly accounted for post-employment health insurance costs that will be paid in future years as a current liability funded by almost \$14.7 million in excess accumulated funds, which has the same effect as a reserve. Two other BOCES improperly used an employee benefit accrued liability reserve to accumulate a total of \$29.9 million for retiree health insurance payments. Employee benefit accrued liability reserves can be used to accumulate monies to make cash payments to employees for accrued leave time due to them upon separation from employment; moneys from this reserve cannot legally be used to pay post-retirement health insurance costs.

Retirement Payments – We also found that one BOCES had established a reserve to fund teachers’ retirement incentives (\$302,499), and that another BOCES had set up a reserve to accumulate funds to pay BOCES retroactive contributions to the New York State and Local Employees’ Retirement System (NYSLRS) on behalf of BOCES employees who applied for retroactive membership in NYSLRS. Neither of these reserves is allowed by law.

BOCES officials told us they had established these reserves because they had been advised to do so by the BOCES’ certified public accountant and/or because they wanted to be fiscally prudent and create reserve funds to pay for these future liabilities. Had BOCES boards developed reserve policies and procedures to determine which reserves the law allows BOCES to establish, and how reserved funds can be used, they could have avoided reserving school districts’ funds in unauthorized reserves, and using reserved funds for inappropriate purposes. BOCES use of unauthorized reserve funds is an improper use of school districts’ and taxpayers’ resources.

Recommendations

To BOCES Officials:

1. The BOCES board should ensure that participating and component districts are properly notified of BOCES’ intent to fund reserves. Reserve funding should be budgeted and part of a board-adopted plan, and amounts budgeted for the purpose of funding reserves should be clearly identified.

2. The board and BOCES officials should develop written plans for the funding and use of reserve funds.
3. The BOCES board should review BOCES' legally established reserves and determine if the balances are necessary and reasonable. To the extent that they are not, BOCES officials should reduce the reserves to reasonable levels in compliance with statutory restrictions.
4. BOCES management should discontinue the use of workers' compensation reserves, retiree health insurance reserves, retirement incentive reserves, and retroactive contribution reserves. The funds in these reserves should be returned to operating funds and properly apportioned to the component and participating school districts.
5. BOCES management should discontinue the inappropriate use of employee benefit accrued liability reserves (EBALR). Funds in excess of the amounts necessary to satisfy genuine EBALR liabilities can be transferred only to certain other reserves authorized by law.

To State Policymakers:

6. The Legislature should establish a trust fund that allows BOCES the opportunity to fund certain other post-employment benefits, such as health insurance costs for retired employees.
7. The Legislature should consider clarifying the statute regarding the ability of BOCES to establish a workers' compensation reserve fund.

APPENDIX A

BOCES' RESERVE BALANCES ON JUNE 30, 2009¹⁶

Reserve	Madison-Oneida	Capital Region	Erie 1	Rockland	Nassau	Western Suffolk	Totals
Employee Benefit Accrued Liability Reserve	\$1,296,881	\$3,971,854	\$6,782,741		\$33,478,545	\$14,587,176	\$60,117,197
Unemployment Insurance Reserve	\$673,754	\$489,914	\$1,044,030	\$562,656	\$494,107	\$253,615	\$3,518,076
Career and Technical Education Equipment Reserve		\$302,869	\$26,873				\$329,742
Retirement Contribution Reserve		\$1,421,639			\$10,455,877	\$1,162,784	\$13,040,300
Property Loss Reserve		\$1,019,813		\$942,147	\$264,493		\$2,226,453
Insurance Reserve				\$4,055,212	\$40,841	\$400,000	\$4,496,053
Retiree Health Insurance Reserve/Accrual ¹⁷	\$6,426,847			\$14,670,719			\$21,097,566
Workers' Compensation Reserve		\$1,092,321	\$331,227	\$931,281		\$2,475,184	\$4,830,013
Retirement/Teachers' Incentive Reserve			\$302,499				\$302,499
Section 803 Accrual				\$32,976			\$32,976
Totals	\$8,397,482	\$8,298,410	\$8,487,370	\$21,194,991	\$44,733,863	\$18,878,759	\$109,990,875

¹⁶ Some June 30, 2009 data was unaudited and prior to year-end adjustments.

¹⁷ Includes a liability accrual that Rockland BOCES is using to fund future post-employment health insurance costs; this is discussed in detail in the individual report for the Rockland BOCES.

APPENDIX B

BOCES' RESERVE BALANCES, BY CATEGORY, ON JUNE 30, 2009¹⁸

	Total Reserves	Reserves Not Specifically Authorized by Statute	Reserve Moneys Not Supported or Not Used in Accordance with Statute	Authorized Reserves with Support for Balance
Madison-Oneida	\$8,397,482	\$6,426,847	\$920,828	\$1,049,807
Capital Region	\$8,298,410	\$1,092,321	\$6,186,276	\$1,019,813
Erie 1	\$8,487,370	\$633,726	\$1,070,903	\$6,782,741
Rockland	\$21,194,991	\$15,634,976 ¹⁹	\$5,560,015	\$0
Nassau	\$44,733,863	\$0	\$37,161,184	\$7,572,679
Western Suffolk BOCES	\$18,878,759	\$2,475,184	\$1,816,399	\$14,587,176
Total	\$109,990,875	\$26,263,054	\$52,715,605	\$31,012,216

¹⁸ June 30, 2009 data was unaudited and may not include end-of-year additions, subtractions, or adjustments.

¹⁹ While BOCES officials have not established a reserve for this purpose, officials have improperly accounted for post-employment health insurance costs that will be paid in future years as a current liability funded by excess, accumulated funds, having the same effect.

APPENDIX C

RESPONSES FROM BOCES OFFICIALS

We provided a draft copy of this global report to each of the six BOCES we audited and requested responses. Of the five BOCES that responded, four generally disagreed with the findings in the global report; one BOCES generally agreed with our findings, but contended that there is limited guidance regarding reserve funds and that related regulations are unclear. The BOCES that responded were Erie 1, Western Suffolk, Rockland, Madison-Oneida and Nassau. Capital Region BOCES officials were provided with an opportunity to respond to this global report, but they chose not to do so.

The following comments were excerpted from the five responses we received, and an OSC note addressing the comments follows in each topic area. Our findings at each of the six BOCES, the individual BOCES' response to those findings, and OSC comments on the response are contained in individual letter reports addressed to each BOCES.

BOCES' Use of Reserve Funds

Erie 1 BOCES: "Erie 1 BOCES strongly believes that we have a fiduciary responsibility to protect the financial stability of our organization and the money that our districts have entrusted us with to run efficient and effective programs."

Madison-Oneida BOCES: "...the Comptroller characterizes BOCES as consistently classifying the moneys they used to fund reserves as fringe benefits expenditures." "The cost of employing the staff member includes not only the salary and benefits paid in the current year, but other forms of deferred compensation which are owed because of this year's service but not paid until later." "...we believe it is prudent cost accounting for the districts that benefit from that teacher's work this year to bear the cost of the future liability."

Western Suffolk BOCES: "The creation and funding of reserves is a tool that BOCES boards have available to enable BOCES to adjust to costs that cannot be adequately anticipated or funded within the annual charges assessed to the component districts."

Rockland BOCES: "...our BOCES is in a sound financial position that will allow us to continue to provide our students with the programs and services that our component districts expect from us. In providing those program and services, we incur financial obligations and, based upon our prudent fiscal planning, we anticipate meeting all of our obligations on a timely basis."

Nassau BOCES: "We believe strongly that the reserves at Nassau BOCES are maintained at a level that is appropriate and likely insufficient given the size of the Agency."

Comptroller's Note

BOCES must operate within applicable laws, rules and regulations. While we agree that reserves are a useful financial tool for BOCES, we stress the need for accountability to the districts and taxpayers that fund BOCES operations. It is essential that BOCES justify reserve amounts with written documentation and justification that clearly indicates reserve funding and use. Without such support and straightforward reporting, districts and taxpayers could be unaware of the intended purpose and plan for such reserves. Further, unless BOCES have a plan for a reserve's use, and comply with the plan, reserved monies could be used for inappropriate purposes and the balances maintained in such reserves could become excessive.

Advice from External Auditors

Erie 1 BOCES: "The reserves that we set up were set up many years ago, with the knowledge and the approval of our independent auditors who have expressed the appropriateness of such reserves in the scope of protecting this financial stability."

Madison-Oneida BOCES: "As we, and apparently other BOCES, advised you, decisions regarding reserve fund balances are guided by the expert advice of our independent accounting advisors. For this reason, and the reasons stated in our response to the individual audit report regarding this BOCES, we disagree with the representation in the draft Report that this BOCES did not have an adequate basis, documented or otherwise, for its management of reserve fund balances."

Rockland BOCES: "All of our annual financial statements have been subject to rigorous review by our external auditor and we have not received any adverse opinion in terms of our reserves or accruals."

Nassau BOCES: "A portion of the Reserve for Employee Benefit Accrued Liability was reserved to help pay the costs of retiree health benefits. These funds were set aside in these reserves years ago on the advice of the independent auditor..."

Comptroller's Note

It is BOCES' responsibility to decide on an appropriate course of action. One source of advice comes from professionals like the external auditor. However, BOCES must ensure that advice from its external auditors complies with all applicable laws.

Unclear or Limited Guidance

Erie 1 BOCES: "Due to the unclear regulations and limited guidance from regulatory agencies, we believe that what we had set up was authorized."

Madison-Oneida BOCES: "The Office of the State Comptroller provides no formula or other useful advice that a board of cooperative educational services can access in

advance to determine whether its decision regarding fund balance meets some standard of acceptability.”

Nassau BOCES: “We appreciate the role of the audit process in ensuring public agencies follow published and adopted policies, rules and regulations. However, OSC has used this audit process to introduce (by implication) new reporting standards and new mandates for additional plans.”

Comptroller’s Note

The expectation that BOCES must comply with applicable laws, rules, and regulations, establish appropriate written plans, and clearly report reserve funding and use should not be viewed as new or unclear. We do acknowledge that one issue needs clarification: specifically, the language regarding which entities are authorized by statute to establish a workers’ compensation reserve. We have recommended that State policymakers make such clarification.

Furthermore, BOCES officials should not limit their accountability efforts to actions they are mandated to perform: fiscal transparency and accountability are good public policy, and public servants should not require a statutory mandate before they provide such transparency.

Transparency and Reporting to Districts

Erie 1 BOCES: “Erie 1 BOCES also believes that in order to build trust with our districts and the community, it is very important to be transparent in all our operations. We agree that a more formal process of notifying the districts would create more transparency.”

Madison-Oneida BOCES: “This portion of the draft Report fails to mention the “transparency” that is built into the BOCES system by the structure of each BOCES board representing the component school districts, and the requirement of Section 1950 that component school districts be directly involved in developing the cost structures for shared services.”

Western Suffolk BOCES: “We are unaware of any legal requirement that the BOCES report to the components on the specific issue of allocation of funds to reserves.”

Rockland BOCES: “As far as the issue of transparency is concerned as it pertains to our fiscal practices, we continue to make full disclosure on a regular basis to all of our component school districts at monthly meetings with superintendents of schools and with business officials, in budget publications and at our annual meeting.”

Nassau BOCES: “Accordingly, we have felt that our extensive efforts were sufficient, but we will undoubtedly incorporate the new OSC guidance issued in December 2009 with whatever additional costs ensue.”

Comptroller's Note

Complete transparency is essential for BOCES, school districts and local governments to maintain the trust and support of taxpayers. The school districts and taxpayers that fund and benefit from BOCES services should be provided with complete information that clearly indicates BOCES' financial activities, including the funding and use of reserve funds. This information should appear in BOCES' written plans for reserve funds, budget documents, and financial reports and should occur in the normal course of business. It is highly unlikely that simply reporting such plans and activity would create any additional cost for BOCES.

No Statutory Requirement for Written Plans for Reserves

Erie 1 BOCES: "However, while there is no existing statute or regulation to this degree, we do agree that a more formal approach to identifying these needs would be beneficial to the process that we currently have."

Western Suffolk BOCES: "If additional statutory or regulatory requirements are desired by the Comptroller's office, they should be proposed and adopted, and take effect in the future."

Madison-Oneida BOCES: "We appreciate the acknowledgement by the Comptroller (P.11) that there is no statutory or regulatory requirement that a board of cooperative educational services adopt a documented use and funding plan for reserve funds."

Rockland BOCES: "As far as the comment made on page 4 of the Global Report about the need to establish plans for how reserves will be used, we would point out that there is no statutory requirement to have such plans..."

Nassau BOCES: "OSC concedes that it is true that BOCES are not required by statute or any other regulation to have written plans for reserve funds (page 11); Nevertheless, OSC's criticism of BOCES' lack of documented plans appears 12 times."

Comptroller's Note

Having written funding and use plans for reserves helps ensure that reserve funds are being properly established for an authorized and needed purpose and that the balances in existing reserve funds are not excessive or unnecessary. Developing and following such plans is simply sound management practice, regardless of whether doing so is legally required.

Clarifying Statutory Language – Workers' Compensation Reserve

Erie 1 BOCES: "E1B would like further clarification on whether a workers' compensation reserve is authorized to operate by a BOCES."

Western Suffolk BOCES: “We support recommendation 7 in the report which recommends that the legislature clarify the statute as it relates to BOCES.”

Rockland BOCES: “As such, pursuant to General Municipal Law §6-j, we are legally authorized to have a workers compensation reserve.”

Nassau BOCES: “We agree with the Comptroller’s recommendation.”

Support for Other Post-Employment Benefits (OPEB) Trust

Madison-Oneida BOCES: “We agree with the Comptroller that the proper solution to the problem of unfunded retiree health insurance obligations is the passage of enabling legislation.”

Nassau BOCES: “OSC has since concluded that OPEB trusts can only be created through legislation and we do not dispute this conclusion. Accordingly, we add our voice to the Comptroller’s (Recommendation 6 below) in calling for this legislation.”

APPENDIX D

AUDIT METHODOLOGY AND STANDARDS

During this audit, we examined the BOCES records and reports for reserves for the period July 1, 2007 to June 30, 2009, and for historical information we reviewed reserve history back to the 2005-06 fiscal year. Our overall goal was to assess the transparency and use of BOCES' reserve funds. To accomplish this, we interviewed BOCES' officials, reviewed documentation on reserves, and performed tests to determine if the reserve balances were adequately supported.

To determine if reserve balances were reasonable we reviewed the BOCES' documentation, if available, to support the reserve balances and conducted tests, as necessary to ensure this documentation was supported and accurate.

To determine if the BOCES have adequate policies and procedures for reserves, we reviewed the BOCES' policies and procedures, if available, and determined if they included specific information on funding and use of reserves and reporting to component school districts. In addition, we reviewed Board resolutions to determine if they included information that could be construed as Board policy.

To determine if BOCES are reporting reserve activity to component school districts, we interviewed BOCES officials to determine what type of reporting is provided to component school districts, and reviewed this reporting, if any, to determine if it included information specifically on reserves.

To determine if BOCES had the authority to maintain certain reserves, we reviewed General Municipal Law, Education Law and the opinions of the Office of the State Comptroller to determine what types of reserves can be maintained by BOCES.

Performance criteria for this audit were based upon certain statutory requirements of Education Law, General Municipal Law, and other guidance and rules prescribed by the Office of the State Comptroller. General Municipal Law and the Accounting and Reporting Manual (ARM) published by the Office of the State Comptroller provided guidance and standards on the system of accounts required for municipalities in New York State.

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

APPENDIX E

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