

QUESTAR III
BOARD OF COOPERATIVE EDUCATIONAL SERVICE
RENSSELAER-COLUMBIA-GREENE COUNTIES

FINANCIAL REPORT

JUNE 30, 2004

QUESTAR III
BOARD OF COOPERATIVE EDUCATIONAL SERVICE
RENSSELAER-COLUMBIA-GREENE COUNTIES
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JUNE 30, 2004

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QUESTAR III
BOARD OF COOPERATIVE EDUCATIONAL SERVICE
RENSSELAER-COLUMBIA-GREENE COUNTIES
MANAGEMENT'S DISCUSSION
AND ANALYSIS (UNAUDITED)
JUNE 30, 2004

The following is a discussion and analysis of the Board of Cooperative Educational Services (hereinafter referred to as "Questar III") financial performance for the fiscal year ended June 30, 2004. The section is a summary of Questar III's financial activities based on currently known facts, decisions, or conditions. It is also based on both the government-wide and fund-based financial statements. The results of the current year are discussed in comparison with the prior year, with an emphasis placed on the current year. This section is only an introduction and should be read in conjunction with Questar III's financial statements, which immediately follow this section.

FINANCIAL HIGHLIGHTS

- Net assets on an entity wide basis increased by 4.9% due to the effect of changes in encumbrances;
- Governmental revenues increased by 4.2% primarily due to increased demand for services;
- Questar III offers over 270 educational and district support services, while operating on a fiscally sound basis. Demand for Questar III educational programs is strong and we expect the trend to continue.

OVERVIEW OF THE FINANCIAL STATEMENTS

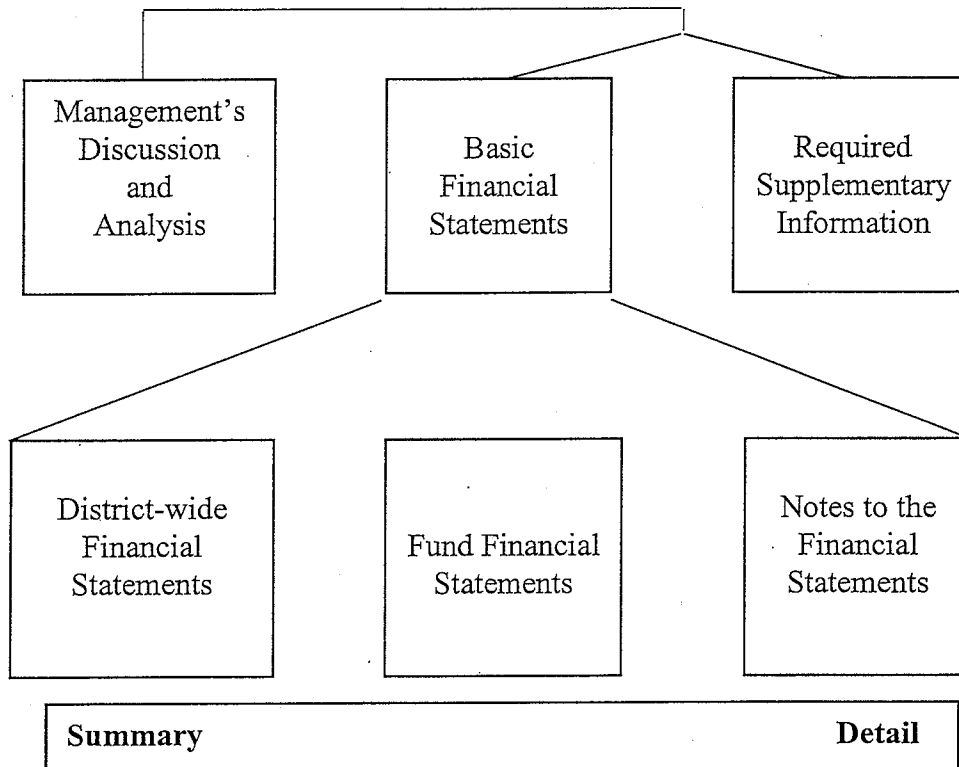
This annual report consists of three parts: MD&A (this section), the basic financial statements, and required supplementary information. The basic financial statements include two kinds of statements that present different views of Questar III:

- The first two statements are *government-wide financial statements* that provide both *short-term* and *long-term* information about Questar III's *overall* financial status.
- The remaining statements are *fund financial statements* that focus on *individual parts* of Questar III, reporting the operations in *more detail* than the entity-wide statements.
- The *governmental fund statements* tell how basic services such as instruction and support functions were financed in the *short-term* as well as what remains for future spending.
- The *Fiduciary funds statements* provide information about the financial relationships in which Questar III acts solely as a *trustee* or *agent* for the benefit of others.

The financial statements also include notes that provide additional information about the financial statements and the balances reported. The statements are followed by a section of required supplementary information that further explains and supports the financial statements with a comparison of Questar III's budget for the year and details as to amounts due from school districts and other BOCES. Table A-1 shows how the various parts of this annual report are arranged and related to one another.

QUESTAR III
BOARD OF COOPERATIVE EDUCATIONAL SERVICES
RENSSELAER-COLUMBIA-GREENE COUNTIES
MANAGEMENT'S DISCUSSION
AND ANALYSIS (UNAUDITED) (CONTINUED)
JUNE 30, 2004

Table A-1: Organization of Questar III's Annual Financial Report



QUESTAR III
BOARD OF COOPERATIVE EDUCATIONAL SERVICE
RENSSELAER-COLUMBIA-GREENE COUNTIES
MANAGEMENT'S DISCUSSION
AND ANALYSIS (UNAUDITED) (CONTINUED)
JUNE 30, 2004

Table A-2 Summarizes the major features of Questar III's financial statements, including the portion of Questar III's activities that they cover and the types of information that they contain. The remainder of this overview section of management's discussion and analysis highlights the structure and contents of each of the statements.

Table A-2: Major Features of the Entity-wide and Fund Financial Statements

	Entity-wide Statements	Fund Financial Statements	
		<u>Governmental</u>	<u>Fiduciary</u>
1. Scope	Entire governmental entity (except fiduciary funds)	The day-to-day operating activities of Questar III, such as education and district support services	Instances in which Questar III administers resources on behalf of others, such as scholarships
2. Required financial statements	<ul style="list-style-type: none"> • Statement of Net Assets • Statement of Activities and Changes in Net Assets 	<ul style="list-style-type: none"> • Balance Sheet • Statement of Revenues, Expenditures and Changes in Fund Balances 	<ul style="list-style-type: none"> • Statement of Fiduciary Net Assets • Statement of Changes in Fiduciary Net Assets
3. Accounting basis and measurement focus	Accrual accounting and economic resources focus	Modified accrual and current financial resources measurement focus	Accrual accounting and economic resources focus
4. Type of asset and liability information	All assets and liabilities, both financial and capital, short-term and long-term	Current assets and liabilities that come due during the year or soon thereafter; no capital assets or long-term liabilities included	All assets and liabilities, both financial and capital, short-term and long-term
5. Type of inflow and outflow information	All revenues and expenses during year; regardless of when cash is received or paid	Revenues for which cash is received during the year or soon thereafter; expenditures when goods or services have been received and the related liability is due and payable	All additions and deductions during the year, regardless of when cash is received or paid

QUESTAR III
BOARD OF COOPERATIVE EDUCATIONAL SERVICE
MANAGEMENT'S DISCUSSION
AND ANALYSIS (UNAUDITED) (CONTINUED)
JUNE 30, 2004

GOVERNMENT-WIDE STATEMENTS

The government-wide statements report information about Questar III as a whole using accounting methods similar to those used by private-sector companies. The Statement of Net Assets includes all of Questar III's assets and liabilities. All of the current year's revenues and expenses are accounted for in the Statement of Activities and Changes in Net Assets regardless of when cash is received or paid.

The two district-wide statements report Questar III's *net assets* and how they are changed. Net assets, the difference between the assets and liabilities, is one way to measure the financial health or position of Questar III.

- Over time, increases and decreases in net assets is an indicator of whether the financial position is improving or deteriorating, respectively.
- For assessment of the overall health of Questar III, additional non-financial factors such as changes in Questar III's component and non-component district's health and the condition of buildings and other facilities should be considered.

In the government-wide financial statements, Questar III's activities are shown as *Governmental activities*: Most of Questar's basic services are included here, such as special education administration and substantially all these activities are financed through user charges.

FUND FINANCIAL STATEMENTS

The fund financial statements provide more detailed information about Questar III's funds. Funds are accounting devices that Questar III uses to account for specific revenue sources and spending on particular programs. The funds have been established by the laws of the State of New York.

Questar III has two kinds of funds:

- ***Governmental funds***: Most of the basic services are included in governmental funds, which generally focus on (1) how cash and other financial assets that can readily be converted to cash flow and (2) the balances left at year-end that are available for spending. Consequently, the governmental fund statements provide a detailed short-term view that helps determine whether there are more or fewer financial resources that can be spent in the near future to finance the programs of Questar III. Because this information does not encompass the additional long-term focus of the government-wide statements, additional information at the bottom of the governmental funds statements explains the relationship (or differences) between them. In summary, the governmental fund statements focus primarily on the sources, uses, and balances of current financial resources and often has a budgetary orientation. Included are the general fund, special revenue funds and capital project funds. Required statements are the Balance Sheet and the Statement of Revenues, Expenditures and Changes in Fund Balances.

QUESTAR III
BOARD OF COOPERATIVE EDUCATIONAL SERVICE
RENSSELAER-COLUMBIA-GREENE COUNTIES
MANAGEMENT'S DISCUSSION
AND ANALYSIS (UNAUDITED) (CONTINUED)
JUNE 30, 2004

FUND FINANCIAL STATEMENTS (CONTINUED)

- **Fiduciary funds:** Questar III is the trustee or *fiduciary* for assets that belong to others, such as scholarship funds, student activities funds, and post-retirement health insurance funds. Questar III is responsible for ensuring that the assets reported in these funds are used only for their intended purposes and by those to whom the assets belong. Questar III excludes these activities from the entity-wide financial statements because it cannot use these assets to finance its operations. Fiduciary fund reporting focuses on net assets and changes in net assets.

FINANCIAL ANALYSIS OF QUESTAR III AS A WHOLE

Questar III's net assets increased 4.9 percent to \$7.8 million as detailed in Tables A-3 and A-4. (3.3 million related to post-retirement benefits were reclassified from cash and long-term liabilities at June 30, 2003 for comparative reporting to June 30, 2004).

Table A-3: Condensed Statement of Net Assets
(in millions)

	Fiscal Year 2004	Fiscal Year 2003
Current and other assets	\$ 6.6	\$ 10.5
Capital assets, net of depreciation	<u>5.2</u>	<u>4.7</u>
Total Assets	<u>11.8</u>	<u>15.2</u>
 Current liabilities	 <u>4.0</u>	 <u>7.8</u>
 Net assets		
Investment in capital assets, net of related debt	5.2	4.7
Unrestricted	<u>2.6</u>	<u>2.7</u>
Total Net Assets	<u>\$ 7.8</u>	<u>\$ 7.4</u>

CHANGES IN NET ASSETS

Questar III's total fiscal year 2004 revenues totaled \$39.8 million. (See Table A-4) Charges to components and non-components accounted for 83% (81% in 2003) of Questar III's revenue. Operating grants accounted for 16% (18% in 2003).

Questar III's total fiscal year 2004 expenses totaled \$38.5 million. (See Table A-4) Of these expenses 90.2% related to instruction and instructional support (89.5% in 2003) and 9.8% related to administrative and business activities (10.4% in 2003).

QUESTAR III
BOARD OF COOPERATIVE EDUCATIONAL SERVICE
RENSSELAER-COLUMBIA-GREENE COUNTIES
MANAGEMENT'S DISCUSSION
AND ANALYSIS (UNAUDITED) (CONTINUED)
JUNE 30, 2004

Table A-4: Changes in Net Assets from Operating Results
(in millions)

	Fiscal Year 2004	Fiscal Year 2003
Revenues		
Program Revenues		
Charges for Services	\$ 33.0	\$ 30.4
Operating Grants	6.2	7.1
Other Revenues	<u>.6</u>	<u>.4</u>
Total Revenues	<u>39.8</u>	<u>37.9</u>
Expenses		
Administration	3.8	3.8
Occupational Instruction	6.2	5.0
Instruction of Handicapped	14.2	12.7
Itinerant Services	.9	.9
General Instruction	3.7	3.9
Instructional Support	4.9	5.6
Other Services	4.5	4.4
Depreciation	<u>.3</u>	<u>.3</u>
	<u>38.5</u>	<u>36.6</u>
Revenues in Excess of Expenses before Return of Surplus	1.3	1.3
Return of Surplus	<u>1.3</u>	<u>1.4</u>
Change in Net Assets	<u>\$ -</u>	<u>\$ (.1)</u>

QUESTAR III
BOARD OF COOPERATIVE EDUCATIONAL SERVICE
RENSSELAER-COLUMBIA-GREENE COUNTIES
MANAGEMENT'S DISCUSSION
AND ANALYSIS (UNAUDITED) (CONTINUED)
JUNE 30, 2004

FINANCIAL ANALYSIS OF QUESTAR III'S FUNDS

Variances between years for the governmental fund financial statements are not the same as variances between years for the District-wide financial statements. Questar III's governmental funds are presented on the **current financial resources measurement focus** and the **modified accrual basis of accounting**. Based on this presentation, governmental funds do not include long-term debt liabilities for the funds' projects and capital assets purchased by the funds. Governmental funds will include the current payments for capital assets, and the current payments for capital leases.

BUDGETARY HIGHLIGHTS

Over the course of the year, Questar III revised its budget several times. These budget amendments fall into two categories:

- Amendments and supplemental appropriations approved shortly after the beginning of the year to reflect the actual beginning account balances and encumbrances carried-over from the prior year.
- Changes made to account for significant increases or decreases in purchased services from component, noncomponent and other BOCES.

Questar III had a number of significant budget amendments during the year ended June 30, 2004 primarily to provide additional services as requested by components and others. The larger increases related to instruction for handicapped students as well as general instruction.

QUESTAR III
BOARD OF COOPERATIVE EDUCATIONAL SERVICE
RENSSELAER-COLUMBIA-GREENE COUNTIES
MANAGEMENT'S DISCUSSION
AND ANALYSIS (UNAUDITED) (CONTINUED)
JUNE 30, 2004

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

The following table reflects the total cumulative cost of various building renovations and additions, technology and equipment expenditures through the end of fiscal year 2004:

Table A-5: Capital Assets

Category	<u>2004</u>	<u>2003</u>
Land	\$ 280,430	\$ 280,430
Buildings	6,630,600	5,975,362
Machinery and Equipment	1,376,175	1,332,885
Vehicles	1,234,192	1,373,059
Construction in Progress	-	122,799
Total	<u>\$ 9,521,397</u>	<u>\$ 9,084,535</u>

Long-Term Debt

At year-end Questar III had \$53,747 in installment purchase debt outstanding. More detailed information about Questar III's long-term liabilities is presented in Note 6 to the Financial Statement.

FACTORS BEARING ON QUESTAR III'S FUTURE

At the time these financial statements were prepared and audited, Questar III was aware of the following existing circumstances that could significantly affect its financial health in the future:

- The state has been mandated by the New York State Court of Appeals to revamp the system of state aid formulas in order to provide (or divert) additional funds for children in New York City. This is the result of court action initiated by the Campaign for Fiscal Equity (CFE). It is conceivable that the required new state formulas could be changed such that the formulas which currently drive BOCES aid to school districts are altered in order to decrease the amount of BOCES aid.

QUESTAR III
BOARD OF COOPERATIVE EDUCATIONAL SERVICE
RENSSELAER-COLUMBIA-GREENE COUNTIES
MANAGEMENT'S DISCUSSION
AND ANALYSIS (UNAUDITED) (CONTINUED)
JUNE 30, 2004

FACTORS BEARING ON QUESTAR III'S FUTURE (CONTINUED)

- Questar III is currently negotiating two union contracts which comprise the majority of instructional staff. The results of the negotiations will be reflected in the cost of Questar III services.
- Based on an analysis of the most recent trends it appears that demand for Questar III educational services is strengthening. During the 2003/04 Fiscal year enrollment for Special Education, Career Technical Education, and General Education services increased by 5.4%, 14.4% and 15.5% respectively. In addition demand for certain district support services such as State Aid Planning is increasing. The following section explains some of the trends that the Questar III programs and services are currently experiencing:

Career and Technical Education - CTE: The steady increase of Career and Technical Education revenue is due to increased enrollment which in turn is due to the successful integration of academics and vocational educational programs. We anticipate demand for our Career and Technical Education services to increase even though the number of students that our current facilities can support limits us. Currently Questar III is developing new vocational programs for general as well as special education students.

Instruction for students with disabilities: The increase in revenue for our Special Education programs can be attributed to a number of different factors. Development and modification of existing programs helped us increase our enrollments. However, the number of students our current facilities can support also limits this program. We are currently negotiating with component school districts for additional classroom space.

Itinerant: This service has been declining steadily. A number of vendors compete with us in providing therapy services. Also, district needs have changed due to the expanding special education population.

General Instruction: The Alternative Educational program revenue has been increasing over the last couple of years. This is due to increased enrollment to the alternative high school program. We expect this program to continue growing since the State Education Department will implement a unique student identification number system that will encourage districts to provide alternative education opportunities to students rather than face the consequences of a high school drop out rate.

QUESTAR III
BOARD OF COOPERATIVE EDUCATIONAL SERVICE
RENSSELAER-COLUMBIA-GREENE COUNTIES
MANAGEMENT'S DISCUSSION
AND ANALYSIS (UNAUDITED) (CONTINUED)
JUNE 30, 2004

FACTORS BEARING ON QUESTAR III'S FUTURE (CONTINUED)

School District Support Services: Statewide demand for the Questar III State Aid Planing service is strong and we expect it will become even stronger as Questar III introduces new business office type services. We also believe that demand for our Risk Management service will become stronger as we implement a recently awarded federal grant that is designed to increase capacity and build collaborations within the Questar III region. However it is important to recognize that overall demand for School District Support Services is declining as districts build there own capacity or choose to purchase the service from our competition.

CONTACTING QUESTAR III'S FINANCIAL MANAGEMENT

This financial report is designed to provide citizens, taxpayers, customers, investors and creditors with a general overview of the finances of Questar III and to demonstrate our accountability with the money we receive. If you have any questions about this report or need additional financial information, contact:

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INDEPENDENT AUDITOR'S REPORT

Questar III
Board of Cooperative Educational Services
Rensselaer-Columbia-Greene Counties

We have audited the accompanying financial statements of the Questar III -Board of Cooperative Educational Services of Rensselaer-Columbia-Greene Counties ("Questar III"), as of and for the year ended June 30, 2004, as listed in the table of contents. These general purpose financial statements are the responsibility of Questar III's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Questar III at June 30, 2004, and the results of its operations for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Management's Discussion and Analysis listed in the foregoing table of contents is not a required part of the basic financial statements but is supplementary information required by the Government Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information an express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued a report dated September 17, 2004 on our consideration of Questar III's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

Our audit was made for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplementary information presented on pages 29 and 30, is presented for purposes of additional analysis and is not a required part of the general purpose financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly presented in all material respects in relation to the basic financial statements taken as a whole.

Cusack & Company, CPA's LLC

CUSACK & COMPANY, CPA'S LLC

Latham, New York
September 17, 2004

QUESTAR III
BOARD OF COOPERATIVE EDUCATIONAL SERVICE
RENSSELAER-COLUMBIA-GREENE COUNTIES
STATEMENT OF NET ASSETS
JUNE 30, 2004

ASSETS

Cash	\$ 3,110,903
State and Federal Aid Receivable	361,877
Due from School Districts	2,441,347
Other Receivables	262,102
Due from Other Funds	446,489
Prepaid Expenses	14,000
Capital Assets, Net	<u>5,180,635</u>

Total Assets	<u><u>\$ 11,817,353</u></u>
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LIABILITIES

Accounts Payable	1,631,375
Accrued Expenses	675,561
Deferred Revenues	572,071
Capital Leases Payable	53,747
Due to Retirement Systems	<u>1,057,101</u>
Total Liabilities	<u>3,989,855</u>

NET ASSETS

Invested in Capital Assets	5,180,635
Unrestricted Reserve for Encumbrances	643,137
Unrestricted Reserve for Prepaids	14,000
Unrestricted Reserve for Employee Benefits	1,926,237
Unrestricted - Capital Projects	<u>63,489</u>
Total Net Assets	<u>7,827,498</u>

Total Liabilities and Net Assets	<u><u>\$ 11,817,353</u></u>
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QUESTAR III
BOARD OF COOPERATIVE EDUCATIONAL SERVICE
RENSSELAER-COLUMBIA-GREENE COUNTIES
STATEMENT OF ACTIVITIES AND CHANGES IN NET ASSETS
FOR THE YEAR ENDED JUNE 30, 2004

	<u>Program Revenues</u>			Net (Expense)
	<u>Expenses</u>	<u>Charges for Services</u>	<u>Operating Grants and Contributions</u>	<u>Revenues and Changes in Net Assets</u>
<u>Functions/Programs:</u>				
Administration	\$ 3,823,138	\$ 4,115,000	\$ 73,794	\$ 365,656
Occupational Instruction	6,179,931	5,056,762	1,383,348	260,179
Instruction of Handicapped	14,222,396	13,861,334	964,578	603,516
Itinerant Services	930,040	942,660	-	12,620
General Instruction	3,731,317	3,109,939	558,934	(62,444)
Instructional Support	4,904,473	1,768,129	3,210,257	73,913
Other Services	4,519,767	4,812,921	-	293,154
Depreciation	<u>262,055</u>	<u>-</u>	<u>-</u>	<u>(262,055)</u>
Total Functions/Programs	<u>\$ 38,573,117</u>	<u>\$ 33,666,745</u>	<u>\$ 6,190,911</u>	1,284,539
Return of Surplus				<u>1,273,889</u>
Change in Net Assets				10,650
Encumbrances, Beginning of Year				(247,661)
Encumbrances, End of Year				643,137
Reduction in Reserve for Employee Benefits				(43,008)
Net Assets, Beginning of Year				<u>7,464,380</u>
Net Assets, End of Year				<u>\$ 7,827,498</u>

QUESTAR III
BOARD OF COOPERATIVE EDUCATIONAL SERVICE
RENSSELAER-COLUMBIA-GREENE COUNTIES
 COMBINED BALANCE SHEET
 GOVERNMENTAL FUNDS
 JUNE 30, 2004

	General	Special Aid	Capital Projects	Total Governmental Funds
ASSETS				
Assets:				
Cash	\$ 1,964,846	\$ 946,813	\$ 199,244	\$ 3,110,903
State and Federal Aid Receivable	-	361,877	-	361,877
Due from School Districts	2,387,600	-	-	2,387,600
Other Receivables, Net	56,036	206,066	-	262,102
Due from Other Funds	1,100,894	-	-	1,100,894
Prepaid Expenses	14,000	-	-	14,000
Total Assets	<u>\$ 5,523,376</u>	<u>\$ 1,514,756</u>	<u>\$ 199,244</u>	<u>\$ 7,237,376</u>
LIABILITIES				
Liabilities:				
Accounts Payable	\$ 1,238,995	\$ 353,242	\$ 39,138	\$ 1,631,375
Accrued Expenses	642,068	33,493	-	675,561
Due to Other Funds	-	557,788	96,617	654,405
Deferred Revenues	1,838	570,233	-	572,071
Due to Retirement System	1,057,101	-	-	1,057,101
Total Liabilities	<u>2,940,002</u>	<u>1,514,756</u>	<u>135,755</u>	<u>4,590,513</u>
FUND BALANCES				
Fund Balance:				
Unrestricted Reserve for Encumbrances	643,137	-	-	643,137
Unrestricted Reserve for Prepaid Expenses	14,000	-	-	14,000
Unrestricted Reserve for Employee Benefits	1,926,237	-	-	1,926,237
Unrestricted	-	-	63,489	63,489
Total Fund Balance	<u>2,583,374</u>	<u>-</u>	<u>63,489</u>	<u>2,646,863</u>
Total Liabilities and Fund Balance	<u>\$ 5,523,376</u>	<u>\$ 1,514,756</u>	<u>\$ 199,244</u>	<u>\$ 7,237,376</u>
Reconciliation of Total Fund Balance to Total Net Assets:				
Total Fund Balance				\$ 2,646,863
Capital Assets				5,180,635
Installment Debt Receivables				53,747
Installment Debt Payable				(53,747)
Total Net Assets				<u>\$ 7,827,498</u>

QUESTAR III
BOARD OF COOPERATIVE EDUCATIONAL SERVICE
RENSSELAER-COLUMBIA-GREENE COUNTIES
COMBINED STATEMENT OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCES - GOVERNMENTAL FUNDS
FOR THE YEAR ENDED JUNE 30, 2004

	General	Special Aid	Capital Projects	Total Governmental Funds
REVENUES:				
Charges to Components	\$ 30,974,832	\$ -	\$ -	\$ 30,974,832
Charges to Non-Components	2,097,109	-	-	2,097,109
Charges for Services	58,534	1,557,771	-	1,616,305
Interest and Earnings	55,665	-	3,786	59,451
Miscellaneous	502,995	-	-	502,995
Sales	183,445	-	-	183,445
State and Local Sources	-	3,409,055	-	3,409,055
Federal Sources	-	1,224,085	-	1,224,085
Total Revenues	<u>33,872,580</u>	<u>6,190,911</u>	<u>3,786</u>	<u>40,067,277</u>
EXPENDITURES:				
Administration	3,715,754	73,794	-	3,789,548
Occupational Instruction	4,911,245	1,383,348	-	6,294,593
Instruction for Handicapped	13,279,694	964,578	677,516	14,921,788
Itinerant Services	930,040	-	-	930,040
General Instruction	3,188,728	558,934	-	3,747,662
Instructional Support	1,753,876	3,210,257	-	4,964,133
Other Services	4,637,754	-	-	4,637,754
Total Expenditures	<u>32,417,091</u>	<u>6,190,911</u>	<u>677,516</u>	<u>39,285,518</u>
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES:	<u>1,455,489</u>	<u>-</u>	<u>(673,730)</u>	<u>781,759</u>
OTHER SOURCES AND (USES):				
Return of Surplus	(1,273,889)	-	-	(1,273,889)
Transfer to Capital Projects	(181,600)	-	-	(181,600)
Transfer from General Fund	-	-	181,600	181,600
	<u>(1,455,489)</u>	<u>-</u>	<u>181,600</u>	<u>(1,273,889)</u>
Change in Fund Equity	-	-	(492,130)	(492,130)
Encumbrances, Beginning of Year	(247,661)	-	-	(247,661)
Encumbrances, End of Year	643,137	-	-	643,137
Reduction in Reserve for Employee Benefits	(43,008)	-	-	(43,008)
Fund Equity, Beginning of Year	<u>2,230,906</u>	<u>-</u>	<u>555,619</u>	<u>2,786,525</u>
Fund Equity, End of Year	<u>\$ 2,583,374</u>	<u>\$ -</u>	<u>\$ 63,489</u>	<u>\$ 2,646,863</u>
RECONCILIATION OF CHANGE IN FUND EQUITY TO CHANGE IN NET ASSETS:				
Change in Fund Equity				\$ (492,130)
Capital Assets Acquired				799,654
Depreciation				(262,055)
Loss on Disposal of Assets				(34,819)
Change in Net Assets				<u>\$ 10,650</u>

See accompanying notes and independent auditor's report.

QUESTAR III
BOARD OF COOPERATIVE EDUCATIONAL SERVICE
RENSSELAER-COLUMBIA-GREENE COUNTIES
STATEMENT OF FIDUCIARY NET ASSETS AND CHANGES IN FIDUCIARY NET ASSETS
JUNE 30, 2004

Statement of Fiduciary Net Assets

	<u>Private-purpose Trusts</u>	<u>Agency Funds</u>
ASSETS		
Cash and Cash Equivalents	\$ 120,811	\$ 5,293,142
Accounts Receivables	-	10,070
Total Assets	<u>\$ 120,811</u>	<u>\$ 5,303,212</u>
LIABILITIES		
Due to Student Groups	\$ -	\$ 15,327
Due to Other Funds	-	446,489
Other Liabilities	-	17,080
Post-Retirement Benefits Payable	-	4,824,316
Total Liabilities	<u>-</u>	<u>\$ 5,303,212</u>
NET ASSETS		
Reserved for Scholarships	<u>120,811</u>	
Total Net Assets	<u>120,811</u>	
Total Liabilities and Net Assets	<u>\$ 120,811</u>	

Statement of Changes in Fiduciary Net Assets

Contributions	\$ 20,277
Investment Income	<u>579</u>
Total Income	20,856
Scholarships	<u>15,350</u>
Increase in Net Assets	5,506
Net Assets, Beginning of Year	<u>115,305</u>
Net Assets, End of Year	<u>\$ 120,811</u>

QUESTAR III
BOARD OF COOPERATIVE EDUCATIONAL SERVICES
RENSSELAER-COLUMBIA-GREENE COUNTIES

NOTES TO FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2004

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The general purpose financial statements of Questar III - Board of Cooperative Educational Services, Rensselaer-Columbia-Greene Counties ("Questar III") have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as applied to government units. The Governmental Accounting Standards Board (GASB) is the accepted standard setting body for establishing governmental accounting and financial reporting principles. The more significant of Questar III's accounting policies are described below.

Reporting Entity

Questar III is governed by the Education Law and other laws of the State of New York. The governing body is the Board of Cooperative Educational Services. The scope of activities included within the accompanying financial statements are those transactions which comprise Questar III operations, and are governed by, or significantly influenced by, this Board.

Boards of Cooperative Educational Services (BOCES) were established by New York State legislation in 1948 to enable school districts to offer more breadth in their educational programs to provide vocational and special education. BOCES is a voluntary, cooperative association for school districts in a geographic area that share planning, services and programs to provide educational and support activities more economically, efficiently and equitably than could be provided locally. Questar III provides instructional and support programs and services to the following 23 school districts in New York's Rensselaer, Columbia and Greene counties:

Averill Park	Hoosick Valley
Berkshire Union Free	Hoosick Falls
Berlin	Hudson
Brittenkill	Ichabod Crane
Cairo-Durham	Lansingburgh
Catskill	New Lebanon
Chatham	North Greenbush
Copake-Taconic Hills	Rensselaer
Coxsackie-Athens	Schodack
East Greenbush	Troy
Germantown	Wynantskill
Greenville	

Questar III's programs and services include special education, vocational education, academic and alternative programs, summer school, staff development, computer services, informational, management and instructional, educational communication and cooperative purchasing.

The financial reporting entity consists of the following, as defined by GASB Statement 14, "*The Financial Reporting Entity*:"

1. The primary government which is Questar III;
2. Organizations for which the primary government is financially accountable, and

QUESTAR III
BOARD OF COOPERATIVE EDUCATIONAL SERVICES
RENSSELAER-COLUMBIA-GREENE COUNTIES
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2004

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Reporting Entity (continued)

3. Other organizations for which the nature and significance of their relationship with the primary government are such that exclusion would cause the reporting entity's general purpose financial statements to be misleading or incomplete.

The decision to include a potential component unit in the reporting entity is based on the criteria set forth in GASB Statement 14, including legal standing, fiscal dependency, and financial accountability. Based on the application of these criteria, the following activity is included in the reporting entity:

The Extraclassroom Activity Funds

The extraclassroom activity funds of Questar III represents funds of the students of Questar III. The Board exercises general oversight of these funds. The extraclassroom activity funds are independent of Questar III with respect to its financial transactions, and the designation of student management and the cash balances are reported in the agency fund of Questar III. Separate audited financial statements (cash basis) of the extraclassroom activity funds are located at the Questar III business office.

The Questar III Education Foundation

The Questar III Education Foundation was formed primarily to solicit contributions and bequests to support scholarship's for students of Questar III or its component school districts. The Foundation's activities are independent of Questar III with respect to its financial transactions and separate Board of Directors and the cash balances are reported in the agency fund of Questar III.

Basis of Presentation

Questar III's financial statements are presented on a government-wide, governmental fund and fiduciary fund basis in accordance with GASB Statement 34 - Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments. As a result, these financial statements include a management discussion and analysis of Questar III's overall financial position and results of operations and financial statements prepared using full accrual accounting for all of Questar III's activities.

Government-wide Financial Statements

The government-wide financial statements present aggregated information for the overall government, excluding activities reported in fiduciary funds, on a full accrual, economic resources basis. This government-wide focus is more on the sustainability of Questar III as an entity and the change in Questar's net assets resulting from the current year's activities. Internal fund transactions, including, but not limited to, operating transfers, receivables and payables have been eliminated. Government-wide financial statements include a statement of net assets and a statement of activities.

QUESTAR III
BOARD OF COOPERATIVE EDUCATIONAL SERVICES
RENSSELAER-COLUMBIA-GREENE COUNTIES
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2004

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Government-wide Financial Statements (Continued)

The statement of net assets recognizes all current and non-current assets including capital assets as well as long-term debt and obligations. Questar III's net assets are reported in three parts-invested in capital assets, net of related debt and accumulated depreciation; restricted net assets due to legal limitations imposed on their use by legislation or external restrictions by other governments; and unrestricted net assets.

The statement of activities presents a comparison between direct expenses (including depreciation) and related program revenues for each function of Questar III's governmental activities. Direct expenses are those that are specifically associated with a service, program or department and are therefore clearly identifiable to a particular function. Indirect expenses for centralized services are allocated among the programs and functions using appropriate allocation methods such as payroll costs and square footage. Program revenues include charges paid by the recipient for the goods or services offered by the programs and grants and contributions that are restricted to meeting the operational or capital requirements of a particular program. Questar III's primary program revenues are fees charged for services.

Basic Financial Statements - Fund Financial Statements

The fund financial statements provide information about Questar III's funds. The operations of each fund are accounted for within a separate set of self-balancing accounts that comprise its assets, liabilities, fund balances, revenues, and expenditures. The focus of governmental fund financial statements is on major funds rather than reporting funds by type with each major fund presented in a separate column. The following funds are used by Questar III.

- a. General - is the general operating fund and is used to account for all financial transactions except those required to be accounted for in another fund.
- b. Special Revenue - is used to account for the proceeds of specific revenue sources such as Federal and State grants, that are legally restricted to expenditures for specified purposes and other activities whose funds are restricted as to use, other than expendable trusts or major capital projects. These legal restrictions may be imposed by either governments that provide the funds or outside parties.
- c. Other - is used to account for all non-major funds including the capital projects fund.

Fiduciary Fund Financial Statements

The fiduciary fund financial statements include a statement of fiduciary net assets and a statement of changes in fiduciary net assets. Fiduciary funds are used to report assets held in a trustee or agency capacity for others and, therefore, are not available to support Questar III's programs. Questar III has the following fiduciary funds:

Private-purpose trusts - established to account primarily for the assets of a scholarship program.

Agency - established to account for assets held in trust by Questar III.

QUESTAR III
BOARD OF COOPERATIVE EDUCATIONAL SERVICES
RENSSELAER-COLUMBIA-GREENE COUNTIES
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2004

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Basis of Accounting/Measurement Focus

1. Government-wide and Fiduciary Fund Financial Statements

The government-wide and fiduciary fund financial statements are prepared using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded at the time the liabilities are incurred regardless of when the related cash flows take place. This approach differs from the manner in which governmental fund financial statements are prepared. The governmental fund financial statements are reconciled to the government-wide financial statements on the combined balance sheet and on the combined statement of revenues, expenditures and changes in funds balances for governmental funds.

2. Governmental Fund Financial Statements

The basis of accounting determines when revenues and expenditures are recognized in the accounts and reported in the financial statements, regardless of the measurement focus applied. Measurement focus is the determination of what is measured. The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. All governmental funds are accounted for using a current financial resources measurement focus. With this measurement focus, only current assets, current liabilities and interfund balances are included in the fund types on the balance sheet. Operating statements of these fund types present increases (i.e., revenues and other financing sources) and decreases (i.e., expenditures and other financing uses) in fund equity.

Modified Accrual Basis - Generally accepted accounting principles and the New York State Uniform System of Accounts for Questar III require that Questar III use the modified accrual basis of accounting for recording transactions in its governmental fund types and expendable trust and agency funds as applicable. Under this basis of accounting, revenues are recorded when measurable and available. Available means collectible within the current period or soon enough thereafter to be used to pay liabilities of the current period. A one-year availability period is used for recognition for governmental fund revenues. Material revenues that are susceptible to accrual include charges for services, intergovernmental revenues and operating transfers. If expenditures are the prime factor for determining eligibility, revenues from Federal and State grants are accrued when the expenditure is made. Expenditures are recorded when the fund liability is incurred except that:

- a. Expenditures for prepaid items are recognized at the time of disbursement when Questar III is liable for payment.
- b. Principal and interest on long-term debt is recognized as an expenditure when due.
- c. Unfunded compensated absences for vacation leave and other compensated absences with similar characteristics and additional salary-related payments are recognized as a liability as the benefits are earned by the employees, based on the rendering of past service and the probability that the employees will be compensated for the benefits through paid time off or some other means. This includes vacation leave and other compensated absences with similar characteristics that were earned but not used during the current or prior periods and for which employees can receive compensation in a future period. Amounts do not include leave expected to lapse and include leave that new employees will eventually qualify for.

QUESTAR III
BOARD OF COOPERATIVE EDUCATIONAL SERVICES
RENSSELAER-COLUMBIA-GREENE COUNTIES
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2004

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Basis of Accounting/Measurement Focus (Continued)

2. Governmental Fund Financial Statements (Continued)

Capital Assets and Depreciation

Capital assets are reported at actual or estimated historical cost based on appraisal or deflated current replacement cost. Contributed assets are reported at estimated fair market values at the time received.

Capital assets with a minimum depreciable base of \$5,000 are depreciated in the government-wide financial statements using the straight-line method with capital assets below this threshold being expensed in the year acquired. Estimated useful lives of the various classes of depreciable assets are as follows: buildings - 15 to 50 years, machinery and equipment - 7 to 15 years and vehicles - 8 years.

Long-Term Debt

Long-term debt includes Questar III's installment purchase debt.

Compensated Absences

Vacation leave is recorded as an expenditure when earned and the estimated liability is reported. Employees accrue vacation leave based on years of service.

Deferred Revenue

Deferred revenues are reported on the balance sheet of the governmental funds combined balance sheet. Deferred revenues arise when potential revenues do not meet both the measurable and available criteria for recognition in the current period. Deferred revenues also arise when resources are received by Questar III before it has a legal claim to them, as when grants are received prior to the incidence of qualifying expenditures. In subsequent periods, when both recognition criteria are met, or when Questar III has legal claim to the resources, the liability for deferred revenues is removed and revenues are recognized.

Post Retirement Benefits

In addition to providing pension benefits, Questar III provides health insurance coverage for retired employees and their survivors. Substantially all of Questar III's employees may become eligible for these benefits if they reach normal retirement age while working for Questar III. Health care benefits are provided through plans whose premiums are based on the benefits paid during the year. The cost of providing post-retirement benefits is entirely borne by Questar III.

QUESTAR III
BOARD OF COOPERATIVE EDUCATIONAL SERVICES
RENSSELAER-COLUMBIA-GREENE COUNTIES
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2004

1. **SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

Basis of Accounting/Measurement Focus (Continued)

2. **Governmental Fund Financial Statements (Continued)**

Fund Balance-Reservations and Designations

Reservations of fund balances are created to either satisfy legal restrictions or to plan for future expenditures. A designation of unreserved fund balances in governmental funds indicates the use of these resources in the subsequent year's budget. The following is a description of the reserves utilized by Questar III.

Encumbrance Reserve

The balance of the account represents the amount of outstanding encumbrances at the end of the fiscal year.

Reserve for Employee Benefits

The balance of the account represents funds set aside for the payment of accrued benefit liabilities for employees.

Budgetary Procedures and Budgetary Accounting

1. **Budget Policies**

The budget policies are as follows:

- a. Section 1950 §4(b) of the Education Law requires adoption of a final budget by no later than May 15, for the ensuing year.
- b. Questar III administration prepares a proposed administrative, capital and program budget, as applicable, for approval by members of Questar III board for the general fund.
- c. Appropriations for educational services are adopted at the program level and lapse at the end of each fiscal year.
- d. A tentative administrative budget is provided to the component districts for adoption by resolution. Approval of the tentative administrative budget requires the approval of a majority of the component school boards actually voting. During the current year, the administrative budget was approved by a majority of its voting component school boards.

2. **Budget Basis of Accounting**

Budgets are adopted annually on a basis consistent with accounting principles generally accepted in the United States of America. Appropriations authorized for the current year are increased by the amount of encumbrances carried forward from the prior year.

QUESTAR III
BOARD OF COOPERATIVE EDUCATIONAL SERVICES
RENSSELAER-COLUMBIA-GREENE COUNTIES
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2004

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Budgetary Procedures and Budgetary Accounting (Continued)

2. Budget Basis of Accounting (Continued)

Questar III's Board can approve budget revisions based upon a request for additional services and surplus revenues.

2. CASH AND INVESTMENTS

Questar III's investment policies are governed by state statutes. In addition, Questar III has its own written investment policy. Questar III monies must be deposited in FDIC-insured commercial banks or trust companies located within the state. The School Business Administrator is authorized to use demand accounts and certificates of deposit. Permissible investments include obligations of the U.S. Treasury and U.S. Agencies, repurchase agreements, and obligations of New York State or its localities.

Collateral is required for demand deposits and certificates of deposit not covered by Federal Deposit Insurance. Obligations that may be pledged as collateral are obligations of the United States and its agencies and obligations of New York State or its localities.

Total financial institution (bank) balances at June 30, 2004 per the bank were \$11,610,060 with a carrying value of \$8,524,856. These deposits were entirely covered by Federal Deposit Insurance or by collateral held by a bank in Questar III's name.

Questar III maintains a pooled cash account in which cash is deposited into one bank account and accounting records are maintained to show the portion of the balance attributable to each fund. At June 30, 2004 Questar III's book balances in the pooled bank accounts were \$1,964,846 in the General Fund and \$4,824,316 in the Agency Fund.

3. OTHER RECEIVABLES

Other receivables at June 30, 2004 consisted of the following, which are stated at net realizable value:

<u>Fund</u>	<u>Description</u>	<u>Amount</u>
General	Fee for Service	\$ 56,036
Special Revenue	Fee for Service Billings	\$ 206,066
Trust and Agency	Due from Terminated Employees	\$ 10,070

QUESTAR III
BOARD OF COOPERATIVE EDUCATIONAL SERVICES
RENSSELAER-COLUMBIA-GREENE COUNTIES
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2004

4. INTERFUND TRANSACTIONS

Interfund balances at June 30, 2004 are as follows:

	<u>Interfund Receivable</u>	<u>Interfund Payable</u>
General Fund	\$ 1,100,894	\$ -
Special Revenue Fund	-	557,788
Capital Projects	-	96,617
Trust and Agency	-	446,489
	<u>\$ 1,100,894</u>	<u>\$ 1,100,894</u>

5. CAPITAL ASSETS

A summary of capital assets for the year ended June 30, 2004 is as follows:

	<u>Restated Beginning Balance</u>	<u>Additions</u>	<u>Deletions</u>	<u>Ending Balance</u>
Land	\$ 280,430	\$ -	\$ -	\$ 280,430
Buildings	5,975,362	800,314	145,076	6,630,600
Machinery and Equipment	1,332,885	69,018	25,728	1,376,175
Vehicles	1,373,059	53,121	191,988	1,234,192
Construction in Progress	122,799	677,515	800,314	-
	<u>9,084,535</u>	<u>1,599,968</u>	<u>1,163,106</u>	<u>9,521,397</u>
Less Accumulated Depreciation:				
Buildings	2,329,281	128,470	110,257	2,347,494
Machinery and Equipment	907,686	69,313	25,728	951,271
Vehicles	1,169,713	64,272	191,988	1,041,997
	<u>4,406,680</u>	<u>262,055</u>	<u>327,973</u>	<u>4,340,762</u>
Capital Assets, Net	<u>\$ 4,677,855</u>	<u>\$ 1,337,913</u>	<u>\$ 835,133</u>	<u>\$ 5,180,635</u>

Depreciation expense was \$262,055 for the year ended June 30, 2004.

6. INSTALLMENT PURCHASE DEBT

Installment purchase debt consists of various leases incurred for the purchase of equipment. The contracts will all mature in the current fiscal year.

QUESTAR III
BOARD OF COOPERATIVE EDUCATIONAL SERVICES
RENSSELAER-COLUMBIA-GREENE COUNTIES
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2004

6. INSTALLMENT PURCHASE DEBT (CONTINUED)

Installment purchase debt activity for the year ended June 30, 2004 is as follows:

Installment Purchase Debt, Beginning Balance	\$ 160,942
Repayments	<u>(107,195)</u>
Installment Purchase Debt, Ending Balance	<u>\$ 53,747</u>

7. PENSION PLANS

General Information

Questar III participates in the New York State and Local Employees' Retirement System (ERS), and the New York State Teachers' Retirement System (TRS). These Systems are cost sharing multiple employer, public employee retirement systems. The Systems offer a wide range of plans and benefits which are related to years of service and final average salary, vesting of retirement benefits, death and disability.

Plan Descriptions

Teachers' Retirement System. The TRS is administered by the New York State Teachers' Retirement Board. The System provides benefits to plan members and beneficiaries as authorized by the Education Law and the Retirement and Social Security Law of the State of New York. The New York State TRS issues a publicly available financial report that contains financial statements and required supplementary information for the System. The report may be obtained by writing the New York State Teachers' Retirement System, 10 Corporate Woods Drive, Albany, NY 12211-2395.

Employees' Retirement System. The New York State and Local Employees' Retirement System provides retirement benefits as well as death and disability benefits. Obligations of employers and employees to contribute and benefits to employees are governed by the New York State Retirement and Social Security Law (NYSRSSL). As set forth in the NYSRSSL, the Comptroller of the State of New York (Comptroller) serves as sole trustee and administrative head of the System. The Comptroller shall adopt and may amend rules and regulations for the administration and transaction of the business of the System and for the custody and control of its funds. The System issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to the New York State and Local Retirement System, 110 State Street, Albany, NY 12244.

Funding Policies

The Systems are noncontributory except for the employees who joined the Systems after July 27, 1979 who contribute 3% of their salary, for first ten years of membership. For the New York State and Local Employees' Retirement System, the Comptroller shall certify annually the rates expressed as proportions of payroll of members, which shall be used in computing the contributions required to be made by employers to the pension accumulation fund. Pursuant to Article 11 of the Education Law, rates are established annually for TRS by the New York State Teachers' Retirement Board.

QUESTAR III
BOARD OF COOPERATIVE EDUCATIONAL SERVICES
RENSSELAER-COLUMBIA-GREENE COUNTIES
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2004

7. PENSION PLANS (CONTINUED)

Questar III is required to contribute at an actuarially determined rate. The required contributions and applicable rates for the current year and two preceding years were:

	ERS		TRS	
	Amount	Rate	Amount	Rate
2004	\$ 619,038	12.08%	\$ 438,063	2.52%
2003	\$ 301,784	4.50%	\$ 151,833	0.36%
2002	\$ 87,296	0.91%	\$ 234,633	0.43%

The Questar III's contributions made to the Systems were equal to 100 percent of the contributions required for each year.

8. POST-RETIREMENT BENEFITS

Questar III provides post retirement health insurance coverage to its retired employees and their survivors. Substantially all of Questar III's employees may become eligible for these benefits if they reach normal retirement age while working for Questar III. Currently, 188 retirees meet those eligibility requirements. Questar III pays 100% of the costs of premiums to an insurance company which provided health care insurance. During 2001, Questar III engaged an actuary who estimated that the future cost of providing post retirement health insurance for current retirees and active employees approximated 9.7 million and 29 million, respectively, assuming a 5% rate of return on invested funds and a 7.5% inflation rate for the cost of health insurance premiums. In accordance with an informal plan to recognize the liability for post retirement health insurance over a period of years, Questar III has recognized a portion of the estimated cost of providing future post retirement health benefits to its retirees at \$4,824,316 which has been recorded as a cash asset and liability in the agency fund. (In prior years this had been recorded in the general fund.) In addition, \$1,969,245 has been recorded as an employee benefit accrued liability reserve fund. The actual cost of health insurance premiums paid for during the year ended June 30, 2004 for Questar III's 226 retirees and spouses was \$590,380.

9. CONTINGENCIES AND COMMITMENTS

Other Contingencies

Questar III has received grants which are subject to audit by agencies of the state and federal governments. Such audits may result in disallowances and a request for a return of funds to the federal and state governments. Questar III believes disallowances, if any, will be immaterial.

Leases

Questar III was committed to various operating lease arrangements at June 30, 2004.

QUESTAR III
BOARD OF COOPERATIVE EDUCATIONAL SERVICES
RENSSELAER-COLUMBIA-GREENE COUNTIES
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2004

9. CONTINGENCIES AND COMMITMENTS (CONTINUED)

Leases (Continued)

The following table summarizes Questar III future payment requirements as of June 30, 2004 under noncancellable operating leases:

Year Ending	
2005	\$ 727,298
2006	741,627
2007	381,111
2008	351,295
2009	280,725
Thereafter	<u>460,629</u>
	<u>\$ 2,942,685</u>

Worker's Compensation Self-Insurance

Questar III participates in a self-insurance plan for worker's compensation called The Rensselaer Columbia-Greene (RCG) Counties Worker's Compensation Consortium ("Consortium"). The Plan is a claims-servicing public entity risk pool which began operations in July, 1985. The Consortium was formed by participating school districts and the Questar III. The purpose of the Consortium is to operate a plan to provide the employees of the participants with worker's compensation benefits and the participants with centralized administration and insurance covering job-connected disabilities and including the cost of medical treatment. The Consortium was accepted as a self-insurer by the State of New York Worker's Compensation Board effective July 1, 1985. The Consortium is governed by a Plan Agreement administered by a Board of Directors, consisting of one Director for each member. As of June 30, 2004 there were 11 participating members from Rensselaer, Columbia and Greene Counties in New York State. An estimated actuarial calculated liability to the Consortium of \$357,534 has been recorded in the accrued expenses in the general fund. Payments made to the Consortium during the year ended June 30, 2004 were \$191,040.

Dental Self-Insurance

Questar III is self-insured for dental insurance. Dental claims expense for the year ended June 30, 2004 was \$107,545.

QUESTAR III
BOARD OF COOPERATIVE EDUCATIONAL SERVICES
RENSSELAER-COLUMBIA-GREENE COUNTIES
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2004

9. CONTINGENCIES AND COMMITMENTS (CONTINUED)

Union Contracts

Questar III employees are represented by collective bargaining agents. Those agents which represent them and the dates of expiration of their agreements are as follows:

<u>Bargaining Unit</u>	<u>Contract Expiration Date</u>
Teachers' Association	June 30, 2004
Assistant Unit	June 30, 2004
Support Services	June 30, 2005

SUPPLEMENTARY INFORMATION

QUESTAR III
BOARD OF COOPERATIVE EDUCATIONAL SERVICE
RENSSELAER-COLUMBIA-GREENE COUNTIES
ANALYSIS OF ACCOUNT A431-SCHOOL DISTRICTS AND OTHER BOCES
FOR THE YEAR ENDED JUNE 30, 2004

SUPPLEMENTAL SCHEDULE #1

July 1 - Debit Balance	<u>\$ 2,165,332</u>
Debits:	
Billings to School Districts and Other BOCES	33,071,941
Surplus Refund to School Districts	1,265,053
Encumbrances - End of Year	<u>643,137</u>
Total Debits	<u>34,980,131</u>
Total	<u>37,145,463</u>
Credits:	
Collections from School Districts and Other BOCES	33,236,313
Adjustments - Credits to School BOCES - Revenues in Excess of Expenditures	1,273,889
Encumbrances - Beginning of Year	<u>247,661</u>
Total Credits	<u>34,757,863</u>
June 30 - Debit Balance	<u><u>\$ 2,387,600</u></u>

QUESTAR III
BOARD OF COOPERATIVE EDUCATIONAL SERVICE
RENSSELAER-COLUMBIA-GREENE COUNTIES
SCHEDULE OF GENERAL FUND REVENUES AND EXPENDITURES - BUDGET AND ACTUAL
FOR THE YEAR ENDED JUNE 30, 2004

SUPPLEMENTAL SCHEDULE #2

	<u>Original Budget</u>	<u>Amended Budget</u>	<u>Actual</u>	<u>Over (Under) Amended Budget</u>	
REVENUES					
Administration (001-002)	\$ 4,299,192	\$ 4,305,092	\$ 4,112,443	\$ (192,649)	
Occupational Instruction (100-199)	5,223,600	5,079,603	5,079,603	-	
Instruction for Handicapped (200-299)	12,498,722	13,877,312	13,877,312	-	
Itinerant (300-399)	817,645	942,660	942,660	-	
General Instruction (400-499)	2,822,500	3,119,157	3,119,157	-	
Instructional Support (500-599)	1,519,331	1,821,289	1,821,289	-	
Other (600-699)	<u>5,316,075</u>	<u>4,920,116</u>	<u>4,920,116</u>	<u>-</u>	
Total	<u>\$ 32,497,065</u>	<u>\$ 34,065,229</u>	<u>\$ 33,872,580</u>	<u>\$ (192,649)</u>	
	<u>Original Budget</u>	<u>Amended Budget</u>	<u>Actual</u>	<u>Encumbrances</u>	<u>Unencumbered Balance</u>
EXPENDITURES					
Administration (001-002)	\$ 4,299,192	\$ 4,305,092	\$ 3,897,354	\$ 17,020	\$ 390,718
Occupational Instruction (100-199)	5,223,600	5,079,603	4,911,245	181,975	(13,617)
Instruction for Handicapped (200-299)	12,498,722	13,877,312	13,279,694	313,142	284,476
Itinerant (300-399)	817,645	942,660	930,040	17,497	(4,877)
General Instruction (400-499)	2,822,500	3,119,157	3,188,728	52,079	(121,650)
Instructional Support (500-599)	1,519,331	1,821,289	1,753,876	30,671	36,742
Other (600-699)	<u>5,316,075</u>	<u>4,920,116</u>	<u>4,637,754</u>	<u>30,753</u>	<u>251,609</u>
Total	<u>\$ 32,497,065</u>	<u>\$ 34,065,229</u>	<u>\$ 32,598,691</u>	<u>\$ 643,137</u>	<u>\$ 823,401</u>

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Members of the Board
Questar III
Board of Cooperative Educational Services
Rensselaer-Columbia-Greene Counties

In planning and performing our audit of the financial statements of Questar III, Board of Cooperative Educational Services Rensselaer-Columbia-Greene Counties for the year ended June 30, 2004, we considered the Organization's internal control in order to determine our auditing procedures for the purpose of expressing an opinion on the financial statements and not to provide assurance on internal control.

However, during our audit we became aware of matters that are opportunities for strengthening internal controls and operating efficiency. The memorandum that accompanies this letter summarizes our comments and suggestions regarding those matters. This letter does not affect our report dated September 17, 2004, on the financial statements of Questar III.

We will discuss the status of these comments during our next audit engagement. We have already discussed these comments and suggestions with various Organization personnel, and we will be pleased to discuss them in further detail at your convenience, to perform any additional study of these matters, or to assist you in implementing the recommendations.



CUSACK & COMPANY, CPA'S LLC

(1) **Establishment of an Audit Committee**

The auditor of Questar III's financial statements must be independent, both in fact and in appearance. A properly constituted audit committee helps to enhance the financial statement auditor's real and perceived independence by providing a direct link between the auditor and the governing board.

One important advantage of an audit committee is that it helps to facilitate communication between management, the auditors, and the governing board. An audit committee also limits the reliance governing bodies must place on the technical expertise of the independent auditor. An audit committee is useful, too, in helping to focus and document the government's process for managing the financial statement audit.

In recent years, the importance of audit committees has come to be recognized increasingly in both the public and private sectors. This importance is reflected in the requirement set by generally accepted auditing standards that auditors determine that the audit committee (or its equivalent) is informed of various matters of importance related to the financial statement audit.

The audit committee should play an advisory role to the governing body. Management and the governing board remain ultimately responsible for the fair presentation of the financial statements and for obtaining and monitoring the financial statement audit.

Recommendation: We make the following recommendations regarding the establishment of an audit committee:

- Questar III should consider establishment of an audit committee or its equivalent. Reliable audits are essential to the credibility of financial reporting by local governments. The audit committee is a practical tool that a government can use to enhance the independence of the external auditor, and hence the reliability of the financial statement audit.
- The audit committee should be formally established by charter, enabling resolution, or other appropriate legal means.
- The members of the audit committee collectively should possess the expertise and experience in accounting, auditing, and financial reporting needed to understand and resolve issues raised by the independent audit of the financial statements.
- A majority of the members of the audit committee should be selected from outside of management.
- An audit committee should be sufficiently large to ensure that its members possess all of the skills needed to realize the committee's objectives. At the same time, the audit committee should be small enough to operate efficiently.

- The primary responsibility of the audit committee should be to oversee the independent audit of Questar's financial statements, from the selection of the independent auditor to the resolution of audit findings.
- The audit committee should have access to the reports of any internal auditors, as well as access to any annual internal audit work plans.
- The audit committee should present annually to the governing board and management a written report of how it has discharged its duties and met its responsibilities. It is further recommended that this report be made public.

(2) Establishment of an Internal Audit Function

The term "internal auditor" is commonly used in a variety of ways in the public sector. For example, some individuals with the title "internal auditor" are actually elected officials who, for all practical purposes, function as external auditors. Conversely, many individuals in the public sector perform one or more of the duties of an internal auditor, although they may use some other job title. For purposes of this recommended practice, an "internal auditor" will be considered to be any audit professional who works directly for management, at some level, and whose primary responsibility is helping management to fulfill its duties as effectively and efficiently as possible.

Internal auditors can be of great value to state and local governments in a variety of ways. In particular, they commonly assist management in monitoring the design and proper functioning of internal control policies and procedures. In this capacity, internal auditors themselves function as an additional level of control and so help to improve the government's overall control environment. Internal auditors also can play a valuable role conducting performance audits, as well as special investigations and studies.

Recommendation: We make the following recommendations regarding the establishment of an internal audit function:

- Questar III should consider the feasibility of establishing a formal internal audit function because such a function can play an important role in helping management to maintain a comprehensive framework of internal controls. As a rule, a formal internal audit function is particularly valuable for those activities involving a high degree of risk (*e.g.*, complex accounting systems, contracts with outside parties, a rapidly changing environment).
- The internal audit function should be established formally by charter, enabling resolution, or other appropriate legal means.
- It is recommended that internal auditors of state and local governments conduct their work in accordance with the professional standards relevant to internal auditing

contained in the U.S. Generally Accounting Office's publication *Government Auditing Standards* (e.g., generally accepted government auditing standards). These standards direct, for example, that internal auditors "report the results of their audits and be accountable to the head or deputy head of the government entity and should be organizationally located outside the staff or line management function of the unit under audit." (Section 3.19)

- At a minimum, the head of the internal audit function should possess a college degree and appropriate relevant experience. It also is highly desirable that the head of the internal audit function hold some appropriate form of professional certification (e.g., certified internal auditor, certified public accountant, certified information systems auditor).
- All reports of internal auditors, as well as the annual internal audit work plan, should be made available to the government's audit committee or its equivalent.

(3) **Governmental Accounting Standards Board ("GASB") Statement No.45 "Accounting and Financial Reporting by Employers for Post-retirement Benefits Other Than Pension"**

Prior to 2004, and the issuance of GASB 45, there was little or no formal guidance on the accounting for post-retirement health insurance. In 2001, management took a proactive position and estimated its liability for post-retirement health insurance at approximately \$40 million and began a plan to recognize the liability for post-retirement health insurance over a number of years. As of June 30, 2004, \$4.8 million has been recognized as a liability in the agency fund and \$1.9 million has been recognized as an employee benefit accrued liability reserve fund for post-retirement health insurance. GASB 45 would be effective for Questar III for the fiscal year ending June 30, 2008, although earlier implementation is encouraged. Essentially, GASB 45 would replace management's current policy of recognition, which is based on ability to charge users, to an actuarially computed amount.

Recommendation: As the recent guidance provided by GASB 45 requires the establishment of a liability and eliminates the provision for an employee benefit accrued liability reserve, we recommend that the reserve be eliminated and that management consider the early implementation of GASB 45.