

CITY OF ALBANY

Office of Audit and Control

Performance Audit of the City's Cash and Investments

**Audit Report
July 2014**

Leif Engstrom
Chief City Auditor



Audit Team

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Please call (518) 434-5023

PREFACE

The Office of Audit and Control exists to provide oversight, transparency and public accountability as a means to improve city services. This performance audit is a part of that function.

When the Office of Audit and Control takes on an audit client and, absent evidence of misconduct, that client addresses the audit's findings; it is our commitment to support and encourage their use of the audit process to improve their operations.

This audit was conducted with the cooperation of the all of the Treasurer's Office staff and the Treasurer has committed to addressing its findings.

The proper use of the audit findings in these circumstances is to provide for oversight of the resulting changes and as the basis for informed public policy discussions.

Given that the Treasurer's office has cooperated with this audit, it would be unfair and damaging to the audit process for this audit's findings to be used for political gain. As such, the Office of Audit and Control will view the political use of this audit's findings as detrimental to our mission.

We thank the Treasurer's Office for their cooperation and commitment.

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The City's investments are generally well managed; with the best available rates, proper collateralization, and policies that follow City and State requirements.

Executive Summary

This is the second audit of the City's investments since the Office of Audit and Control was founded in 2010. The first was completed in 2011. This audit was initiated in response to a City Charter requirement and was not initiated as a result of OAC's citywide risk assessment process. As a result of the determinations made in this audit, OAC will conduct a follow-up review in 2014. The results of that review will determine the timeframe for the next audit.

The audit team found that the City's investments are generally well managed. We based this determination on the following conclusions:

- The investment policy is in compliance with the City Charter and the procedures are in compliance with that policy.
- Funds meet the New York State collateralization requirements.
- The City's interest-bearing accounts yield the best available interest rates.

Prior Audit Findings

As mentioned above, an identical audit was completed in 2011. That audit had two findings. The results of OAC's follow-up on those findings are as follows:

2011 Finding 1

Treasurer's staff was unable to readily determine whether the Security and Collateral Agreements (SCA) on file were the current version. Three of the City's SCAs are authorized by persons who no longer represent the City.

OAC Recommendation: The Treasurer's Office should maintain SCAs on file and update them when the Authorized Person ceases to be an Authorized Person.

2013 Audit Status: The Key Bank SCA was not executed by the Treasurer. However, two other SCAs identified in the 2011 audit were executed and were on file.

2011 Finding 2:

There were errors in the 2011 Bank Statement reconciliations for the General Fund and Payroll Fund.

OAC Recommendation 2: All bank reconciliations should be reviewed regularly by a supervisor. Additionally, the Treasurer should approve all adjusting entries greater than \$10,000.

2013 Audit Status: The reconciliations were accurately completed, but because of the significant delay in providing the reconciliations for review, OAC concludes that regular supervisory review did not occur until we began the audit.

Current Audit Findings

In conducting this audit, the audit team identified four findings that resulted in four recommendations. The primary causes for the findings were a lack of personnel, staff turnover, inattention to policy, and recent reassignments of duties.

The findings are as follows:

Finding 1: The Key Bank Security Collateral Agreement is a 2003 agreement and the Authorized Person is no longer with the City.

Recommendation 1: The Treasurer's Office should maintain SCAs on file and review them annually.

Finding 2: *The bank reconciliation documents were not provided for review when OAC requested them at the start of the audit in September 2013. The General fund reconciliation documents were provided January 15, 2014 and the Payroll fund reconciliation documents were provided February 20, 2014.*

Recommendation 2: All bank reconciliation documents should be reviewed regularly by a supervisor. Review should be documented. Additionally, the Treasurer should be notified of all adjusting entries greater than \$10,000.

Finding 3: The annual investment report was not prepared.

Recommendation 3. Prepare the investment report annually.

Finding 4: Key Bank funds were over the maximum of \$50 million allowed in the Funds Management and Investment Policy for the months of January through April 2013.

Recommendation 4: The investment policy specifies maximum deposits per depository in order to reduce risk by allocating funds among various authorized banks and trust companies. The policy should be complied with.

The audit team thanks the personnel who assisted and cooperated with us during this audit.

Definitions

In order to make this report more accessible to the lay reader, we have included a definitions page for financial terms that may not be widely understood. The definitions are in the context of the City's finances.

Adjusting Entry – entries in the General Ledger made during bank statement reconciliation to allocate receipts and disbursements to the period in which they actually occurred or the account to which they correctly belong.

Bank Statement reconciliation – the process of comparing the Bank Statement balance against the General Ledger account balance and indentifying differences.

Cash funds – the money kept on hand to meet short-term and emergency funding needs.

Cash and cash items – cash and any check given immediate credit to a customer's account before a bank has received payment from the paying bank.

Cash equivalent (investment) accounts –Cash and cash equivalents are the most liquid assets found within the asset portion of an entity's balance sheet.

Collateral – items pledged as security for deposited or invested funds that are not covered by FDIC deposit insurance.

Collateralized – an account is collateralized when securities are pledged as collateral for deposited or invested funds. All City accounts that exceed FDIC insurance limits are collateralized to protect the City in the event of a bank failure.

Collateral reports – monthly reports detailing the descriptions and market value of securities pledged as collateral for deposited or invested funds.

Deferred revenue – money received for services which have not yet been delivered.

Escheat Funds – the reverting of funds to the state or some agency of the state.

General Fund – bank accounts for all financial resources except those required to be accounted for in another fund.

General ledger – the City's internal accounting records.

Investments –deposits into interest bearing accounts or obligations.

Outstanding checks – checks issued by the City, but not cashed.

Payroll Fund – bank account for funds held purely in a custodial capacity for payroll.

Reconciling adjustments – adjustments needed to balance the bank accounts to the general ledger.

Security and Collateral Agreements (SCA) -a contract that governs the relationship between the parties to a kind of financial transaction known as a secured transaction. The Security Agreement addresses issues such as acceptable types of securities held as collateral for deposited funds.

Stale dated –outstanding checks that are 90 days old or older.

Temporary investments – an investment designed to be held for a short period of time, typically a year or less.

Introduction

“A sound program for protecting public funds requires prudent strategies, including procedures to ensure the safety of investments and deposits while maximizing earnings on any money that is not required for operations.”

-Investing and Protecting Public Funds; Office of the New York State Comptroller

As the City’s chief fiscal officer, the City Treasurer is responsible for the collection, receipt, care and custody of all taxes and other monies due the City, except as otherwise provided by law¹. Under these duties, the Treasurer is responsible for the deposit of all monies received by the City and those deposits must be made in accordance with City and State law. The Treasurer is also responsible for making all investments of City funds in accordance with the rules set by the New York State General Municipal Law. ²

In New York State, local governments have a limited number of investment options available to them. Local governments are authorized to invest money temporarily in:

- Time deposit accounts in a “bank” or “trust company” located and authorized to do business in New York State. Time deposit accounts are interest bearing, for example, interest bearing checking accounts and money market deposit accounts.
- Certificates of deposit (CDs) issued by a “bank” or “trust company” located and authorized to do business in New York State. CDs are purchased for specific periods of time that may be as short as seven days or as long as a year or more.
- Certain types of obligations such as bonds, notes or other such forms of indebtedness issued by specific entities such as the United States Government and the State of New York.

All investments with a bank or trust company must have adequate collateral to secure the City’s investments that are not insured by the FDIC, and thus at risk in a bank failure or other event of default.

The City of Albany currently invests its money in interest bearing checking accounts, money market accounts, and CDs. At this time, the City has no money invested in bonds or notes. The purpose of this audit is to review the compliance of cash and investment activity in accordance with the Treasurer’s investment policy, the City of Albany Charter, and the laws and regulations of New York State.

¹ One notable exception is the Police seized assets account, which is managed by the Police Chief.

² The Treasurer is also responsible, once authorized by the Office of Audit and Control, for the payment of all vouchers, claims, payroll and other disbursements.

Background

The principal duties of the Office of Audit and Control (OAC) are to conduct performance audits of all City departments and offices; to audit all investments made by the City Treasurer on behalf of the City; and to warrant as valid all accounts payable claims prior to payment by the City Treasurer.

All activity on the 2013 investments, deposits, collateral, and bank reconciliations were performed by the Treasurer's office staff. The Office of Audit and Control staff was not involved in any duties of the areas reviewed in this audit and had not been for more than a year before the initiation of the audit.

Scope, Objectives, and Methodology

Scope

The scope of the investment audit is the review and examination of the investment and bank accounts, all collateral reports, related general ledger accounts and related records for the period of January 2013 through September 2013.

Objectives

1. Determine whether the actual procedures are in compliance with the City Charter and the Investment Policy.
2. Examine the rates and interest earned.
3. Determine whether the funds are properly collateralized.
4. Assess the cash balances in non-interest bearing accounts.
5. Determine whether the general ledger cash balances represent all cash and cash items on hand, in transit to or in financial institutions and that cash and cash items are properly recorded.

Methodology

The audit team reviewed cash balances on the general ledger to assure that all cash items on hand or in transit are in appropriate financial institutions and properly recorded, and that all investments and cash funds are properly collateralized. We also reviewed reconciliations of the investment and bank accounts to the general ledger and reviewed the cash and cash equivalents activity for each month in the audit period. For the liquid assets (cash), we reviewed information on the bank reconciliations and the collateral reports. The general ledger detail was reviewed to ensure that all cash items were properly represented and recorded. Collateral reports and SCAs were reviewed to determine proper coverage of deposited funds and to ensure they are current and appropriately executed.

For the City's cash equivalent (investment) accounts, the figures in the City's general ledger were checked to the appropriate supporting documentation from the financial institution to ensure proper representation and recording. The institutions were reviewed to ensure compliance with the City's investment policy.

The audit team reviewed the responsibilities of the staff involved with investments.

The Chief City Auditor warrants valid all vouchers, claims, payroll and other authorized disbursements. This is a Charter-mandated, non-audit service that impairs independence in regards to all audits performed by the Office of Audit and Control.

Audit Results

1. The Funds Management and Investment Policy is in compliance with the City Charter. The procedures are in compliance with the policy except regarding the annual investment report.
 - a. The Funds Management and Investment Policy was adopted by the Treasurer in the spring of 2011.
 - b. The Investment Policy states that the Treasurer annually prepares an investment report summarizing investment results, and providing detail on the type, term, interest rates and yields of the City's investments during the prior year.
 - c. This report was not prepared for 2011 and 2012.
2. Rates and interest earned on interest-bearing accounts are the best rates available and the investments are in compliance with the investment policy and general municipal law.
3. Funds were adequately collateralized for every account.
4. The City's security and collateral agreements with the banks meet New York State requirements.
5. The City Treasurer has undertaken the important task of identifying City-issued outstanding checks that are more than two years old. The escheat funds have been turned over to NYS Unclaimed Funds managed by the NYS Comptroller. The contact information for the Office of Unclaimed Funds is:

Office of the State Comptroller
Office of Unclaimed Funds
110 State Street
Albany, New York 12236

Phone: 1-800-221-9311 (Monday through Friday, 8:00 am – 4:30 pm)

Finding 1:

The Key Bank Security and Collateral Agreement is a 2003 agreement with a past City Comptroller, who has left the City, as the authorized person.

A former Assistant Treasurer who had left the City is an Authorized Person on The First Niagara Security and Collateral Agreement.

Condition: The most recent executed collateral agreement with Key Bank is dated 2003 and was signed by a former City Comptroller who is no longer with the City. A former Assistant Treasurer is an Authorized Person on the First Niagara Security and Collateral Agreement.

Criteria: When the SCAs were executed, the City agreed to "furnish a new Certificate of Authorized Persons in the event that any present Authorized Person ceased to be an Authorized

Person or in the event that any other Authorized Persons are appointed and authorized. Until such new Certificate is received, the Bank or Agent is fully protected in acting upon Written (or Oral) instructions or signatures of the present Authorized Persons.”

Effect: The City had between \$66 Million to \$37 Million in Key Bank Accounts from January 2013 through September 2013 and \$15 Million to \$14 Million January 2013 through June 2013 at First Niagara. Risk of losing the funds is unlikely but the impact would be high.

Cause: The Assistant Treasurer left in May 2012 and responsibilities had to be rearranged. Responsibility for the maintenance of the file was not clarified during these changes.

Recommendation: Maintain Security and Collateral agreements on file in the office responsible for ensuring the appropriateness of the securities and adequate collateral for deposited funds. Update all Security and Collateral agreements annually.

Finding 2:

The bank statement reconciliation documents were not provided for review when OAC requested them at the start of the audit in September 2013.

Condition: The bank statement reconciliation documents for General Fund and Payroll Fund were not ready for review in September when this audit started. The bank statement reconciliation documents for the General Fund and Payroll Fund were not provided until December 24th and December 30th. OAC requested the documents in September 2013. The reconciliation documents for the General Fund bank statements were made available for review January 15, 2014. The reconciliation documents for the Payroll Fund bank statements were available for review February 20, 2014. The Key Bank outstanding check list was not updated for obsolete checks until December 2013. The General Fund outstanding check list was not updated until the October 31, 2013 Bank Statement.

Criteria: The bank reconciliation documents should be reviewed by a supervisor regularly to ensure that all bank transaction errors and/or accounting errors are identified and corrected in a timely manner. The Key Bank outstanding check list should be reviewed regularly as a part of the monthly reconciliation process and any checks that are not outstanding should be removed. The review and actions taken should be documented.

Effect: Bank account transaction errors and/or General Ledger accounting errors may not be correctly identified in a timely manner.

Cause: The Assistant Treasurer left in May 2012 and responsibilities had to be rearranged.

Recommendation: A supervisor should review the bank reconciliations regularly to ensure that all bank transaction errors and/or accounting errors are identified and corrected in a timely manner. Additionally, the Treasurer should be notified of all adjusting entries \$10,000 or greater.

Finding 3:

Investment reports for 2011 and 2012 were not prepared.

Condition: When OAC requested the investment reports for 2011 and 2012, the Deputy Treasurer told us that the investment reports had not been prepared.

Criteria: The Funds Management and Investment Policy states that “The Treasurer annually prepares an investment report, summarizing investment results, and providing detail on the type, term, interest rates and yields of the City’s investments during the prior year.”

Effect: Information regarding investment activity has not been reported, and is not readily available for review.

Cause: The Deputy Treasurer did not know why the report had not been prepared.

Recommendation: The Investment report, which does not have to be extensive, should be prepared annually in compliance with the Investment Policy.

Finding 4:

Key Bank funds were over the maximum of \$50 million allowed in the Funds Management and Investment Policy for the months of January through April 2013.

Condition: The amount of funds deposited in one Depository was approximately \$10 Million over the maximum amount authorized in the Funds Management and Investment Policy for the months of January through April 2013.

Criteria: The Funds Management and Investment Policy under Designation of Depositories states that “The banks and trust companies authorized for the deposit of monies up to the following maximum amounts are:”

Depository Name	Maximum Amount
Key Bank	\$50,000,000
M&T Bank	\$50,000,000
JP Morgan/Chase	\$50,000,000
Citizen’s Bank	\$50,000,000
Bank of America	\$50,000,000
HSBC	\$50,000,000
TD Bank	\$50,000,000
First Niagara Bank	\$50,000,000

Effect: In the unlikely event of a bank failure, any funds exceeding the maximum amount would be unnecessarily put at risk. The risk of loss is extremely low because the funds were adequately collateralized.

Cause: The policy was not complied with.

Recommendation: The current investment policy specifies maximum deposits per depository in order to reduce risk by allocating funds among various authorized banks and trust companies. The policy should be complied with.

Note: This finding existed during the scope of the 2011 Investment Audit by OAC but was not identified in that audit.

Prior Audit Findings

2011 Finding 1:

Treasurer's staff was unable to readily determine whether the Security and Collateral Agreements (SCA) on file were the current version. The First Niagara agreement which was dated May 2011 was the only one identifiable as current. Three of the agreements are with Authorizing Persons who no longer represent the City.

Condition: SCAs have not been updated for Authorized Persons and agreements were not identifiable as current.

Criteria: SCAs should be on file in the office responsible for ensuring adequate collateral for deposited funds and the agreements should be updated when there is a change of Officers for the City.

Effect: If the agreements are not readily used for reference and review, then a change of personnel could result in inadequate review of the collateral reports for legal securities and adequate collateral coverage of deposited funds. The agreements could be compromised if they are not updated for Authorized Persons.

Cause: The restructuring of the City Treasurer's office and the City Comptroller's office into the City Treasurer's office and the Office of Audit and Control (OAC) involved changeover in both staff and responsibilities. In addition, two of the supervisory personnel left and responsibilities had to be rearranged. Responsibility for the maintenance of the file was not clarified during these changes.

Recommendation: Maintain Security and Collateral agreements on file in the office responsible for ensuring the appropriateness of the securities and adequate collateral for deposited funds. Update all Security and Collateral agreements when the Authorized Person ceases to be an Authorized Person or in the event that any other Authorized Persons are appointed and authorized.

2013 Status: All but one SCA was updated after the 2011 audit. OAC found that the SCAs need to be reviewed annually.

2011 Finding 2:

There were errors in the 2011 Bank Statement reconciliations for the General Fund and Payroll Fund.

Condition: Although most of the general ledger or bank account errors were found and corrected, the reconciliations contained reconciling items that were not accurate, or were not supported with documentation or explanations of the reconciling adjustment. The reconciliations were not reviewed by a supervisor or a qualified staff person. Additionally, the Property Tax bank account statements (for internet payments) were not included with the General fund bank reconciliation.

Criteria: Work done by staff should be reviewed by a supervisor or other qualified staff person for completeness and correctness.

Effect: Some items may not have been properly identified for correction on the City's general ledger accounts or bank accounts, with the potential to damage cash flow management. There is

also the potential that Treasurer's Office management would not be aware of material adjustments.

Cause: The restructuring of the City Treasurer's office and the City Comptroller's office into the City Treasurer's office and the OAC involved changeover in both staff and responsibilities. The change added a significant new responsibility (performance auditing) without additional personnel. These events and realities may have contributed to lower prioritization in the monitoring of certain activities.

Recommendation: All bank reconciliations should be reviewed and signed regularly by a supervisor, and the Treasurer should be notified of any adjusting entry of \$10,000 or greater. Adjustments should have supporting documentation and explanation. Additionally, the Property Tax bank account statements should be included with the General Fund bank reconciliation.

2013 Status: OAC did not find errors in the bank reconciliations. We found that the reconciliations were not reviewed and signed regularly by a supervisor although we are aware that they were reviewed before they were provided to OAC for review for this audit.

APPENDIX



CITY OF ALBANY
OFFICE OF THE TREASURER
ROOM 109
24 EAGLE STREET
ALBANY, NEW YORK 12207
TELEPHONE (518) 434-5035

DARIUS SHAHINFAR
CITY TREASURER

Memorandum

To: Leif Engstrom, City Auditor
From: Darius Shainfar, City Treasurer
Re: Response to Performance Audit
Date: July 24, 2014

In accordance with the Albany City Charter, the Office of Audit and Control conducted an audit of the City's cash and investments. The audit contained 4 Findings and Recommendations. Below, please find our office's response to the OAC findings.

Our office agrees with Finding 1 and Recommendation 1. With the change in Administration, our office, with the assistance of the Law Department, is currently engaged in a review of all contracts and agreements to ensure that all contracts are properly tracked and updated as necessary.

Our office agrees with Finding 2 and Recommendation 2. The delay in response was due to miscommunication and misunderstanding between the two offices over the required documents for the scope of the audit and the necessity of the provision of certain documents.

Our office agrees with Finding 3 and Recommendation 3. OAC correctly notes that municipal investments are strictly limited by State law to investments that bear almost no risk. Responsibility for completion of the report, a relatively new requirement for the Treasurer's office, has been allocated going forward.

Our office agrees with Finding 4 and Recommendation 4. OAC correctly concludes that city funds were not exposed to additional risk, and have been at extremely low risk because of adequate collateralization. Market and banking conditions had led to the request from banks of higher average levels of funds in city

accounts, which led the Treasurer's office to consider amending this policy. However recent regulatory changes have led banks to request lower levels of funds. The account limits at issue are set by policy, not by statute, and therefore policy changes should be made, in conjunction with the Common Council, to provide flexibility to reflect market and banking conditions.

We extend our thanks to the OAC for the thoroughness of their work, and look forward to providing any additional information that they might need or request.