

OFFICE OF THE NEW YORK STATE COMPTROLLER



DIVISION OF LOCAL GOVERNMENT
& SCHOOL ACCOUNTABILITY

City of New Rochelle

Financial Condition

Report of Examination

Period Covered:

January 1, 2013 — March 18, 2014

2014M-158



Thomas P. DiNapoli

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State of New York

Office of the State Comptroller

Division of Local Government and School Accountability

August 2014

Dear City Officials:

A top priority of the Office of the State Comptroller is to help local government officials manage government resources efficiently and effectively and, by so doing, provide accountability for tax dollars spent to support government operations. The Comptroller oversees the fiscal affairs of local governments statewide, as well as compliance with relevant statutes and observance of good business practices. This fiscal oversight is accomplished, in part, through our audits, which identify opportunities for improving operations and City Council governance. Audits also can identify strategies to reduce costs and to strengthen controls intended to safeguard local government assets.

Following is a report of our audit of the City of New Rochelle, entitled Financial Condition. This audit was conducted pursuant to Article V, Section 1 of the State Constitution and the State Comptroller's authority as set forth in Article 3 of the General Municipal Law.

This audit's results and recommendations are resources for local government officials to use in effectively managing operations and in meeting the expectations of their constituents. If you have questions about this report, please feel free to contact the local regional office for your county, as listed at the end of this report.

Respectfully submitted,

*Office of the State Comptroller
Division of Local Government
and School Accountability*



**State of New York
Office of the State Comptroller**
EXECUTIVE SUMMARY

The City of New Rochelle (City) is located in Westchester County and has approximately 77,000 residents. The City Council is the legislative body responsible for establishing policies and the City Manager is responsible for administering the City's daily operations. The Commissioner of Finance is the City's chief fiscal officer and is responsible for establishing internal controls over financial operations and monitoring the budget. The Deputy Commissioner of Finance/Treasurer has custody of City funds and is responsible for maintaining the City's accounting records.

As of January 2014, the City had 586 employees. The City's budgeted appropriations for the 2014 fiscal year are approximately \$118 million, which are funded primarily with real property taxes, sales taxes, State aid and fees. In addition to the general fund, the City has several enterprise and internal service funds, a debt service and a capital projects fund.

Scope and Objective

The objective of our audit was to review the City's financial condition for the period January 1, 2013 through March 18, 2014. We extended our scope back to 2011 for analytical purposes. Our audit addressed the following related questions:

- Do City officials adequately monitor the City's financial operations to ensure fiscal stability?
- Does the cash concentration account accurately account for the cash position of City funds?

Audit Results

The City currently has a stable financial condition. The City's general fund unassigned fund balance has increased from \$1.6 million to \$6.1 million from fiscal years 2011 through 2013. However, two funds – the capital projects fund and the internal service fund-workers' compensation – reported deficits in 2013. Although the workers' compensation fund deficit decreased from \$1.3 million in 2012 to \$597,743 as of December 31, 2013, the capital projects fund's deficit increased from \$1.9 million in 2012 to \$5 million in 2013.

City officials do not report cash assets earned in each fund's cash account. All cash is deposited in a concentration account and recorded as an asset in the general fund. Instead of cash assets, the City's other funds include amounts "due from other funds" while the general fund includes a significant "due to other funds."¹ As of December 31, 2013, the general fund financial statements showed cash assets of approximately \$22 million and "due to other funds" of \$14.8 million, while other City funds,

¹ "Due to other funds" is a liability account used to record financial activities that result in one fund owing money to another, while "due from other funds" is the asset equivalent.

which received significant amounts of cash from operations, showed minor petty cash balances and significant “due from other funds” balances. As a result, the City’s financial statements are not as transparent as they could be. While all funds have direct access to cash from the concentration account for payments of payroll and vendor invoices, City officials did not maintain separate cash accounts in the individual funds.

Comments of Local Officials

The results of our audit and recommendations have been discussed with City officials and their comments, which appear in Appendix B, have been considered in preparing this report. City officials generally agreed with our recommendations and indicated that they planned to take corrective action.

Introduction

Background

The City of New Rochelle (City) is located in Westchester County and has approximately 77,000 residents. The City Council is the legislative body responsible for establishing policies and the City Manager is responsible for administering the City's daily operations. The Commissioner of Finance is the City's chief fiscal officer and is responsible for establishing internal controls over financial operations and monitoring the budget. The Deputy Commissioner of Finance/Treasurer has custody of City funds and is responsible for maintaining the City's accounting records.

As of January 2014, the City had 586 employees. The City's budgeted appropriations for the 2014 fiscal year are approximately \$118 million, which are funded primarily with real property taxes, sales taxes, State aid and fees. In addition to the general fund, the City has several enterprise and internal service funds, a debt service and a capital projects fund.

Objective

The objective of our audit was to review the City's financial condition. Our audit addressed the following related questions:

- Do City officials adequately monitor the City's financial operations to ensure fiscal stability?
- Does the cash concentration account accurately account for the cash position of City funds?

Scope and Methodology

We examined the City's financial condition for the period January 1, 2013 through March 18, 2014. We extended our scope back to 2011 for analytical purposes.

We conducted our audit in accordance with generally accepted government auditing standards (GAGAS). More information on such standards and the methodology used in performing this audit are included in Appendix B of this report.

Comments of Local Officials and Corrective Action

The results of our audit and recommendations have been discussed with City officials and their comments, which appear in Appendix A, have been considered in preparing this report. City officials generally agreed with our recommendations and indicated that they planned to take corrective action.

The City Council has the responsibility to initiate corrective action. A written corrective action plan (CAP) that addresses the findings and recommendations in this report should be prepared and forwarded

to our office within 90 days, pursuant to Section 35 of the General Municipal Law. For more information on preparing and filing your CAP, please refer to our brochure, *Responding to an OSC Audit Report*, which you received with the draft audit report. We encourage the City Council to make this plan available for public review in the City Clerk's office.

Financial Condition

Financial condition may be defined as a city's ability to balance recurring expenditure needs with recurring revenue sources, while providing desired services on a continuing basis. A city in good financial condition generally maintains adequate service levels during fiscal downturns and develops resources to meet future needs. Conversely, a city in fiscal stress may struggle to balance its budget, can suffer through disruptive service level declines, has limited resources to finance future needs, and often has minimal cash available to pay current liabilities as they become due. Positive results from operations increase fund balance and foster growth, while operational deficits deplete fund balance.

The City currently has a stable financial condition. The City's general fund unassigned fund balance has increased from \$1.6 million to \$6.1 million from fiscal years 2011 through 2013. However, two funds – the capital projects fund and the internal service fund-workers' compensation – reported deficits in 2013. Although the workers' compensation fund deficit decreased from \$1.3 million in 2012 to \$597,743 as of December 31, 2013, the capital projects fund's deficit increased from \$1.9 million in 2012 to \$5 million in 2013.

The general fund's financial condition has steadily improved since 2011. In 2013, fund balance increased considerably due mainly to a one-time sale of a City property that was not included in the budget. General fund expenditures were also \$2.3 million less than budgeted for 2013. As a result, the general fund reported an unassigned fund balance of \$6.1 million at December 31, 2013, which represents approximately 5 percent of the 2014 appropriations. This non-recurring revenue source will not be available in subsequent years to help finance recurring expenditures.

Figure 1 shows that the general fund's unassigned fund balance increased each year, from \$1.6 million in 2011 to \$3.1 million in 2012 and \$6.1 million in 2013.

Figure 1: General Fund - Fund Balance

Fiscal Year	2011	2012	2013
Nonspendable	\$3,357,522	\$3,637,072	\$4,167,398
Committed	\$300,000	\$300,000	\$300,000
Assigned	\$174,820	\$1,310,739	\$1,313,605
Unassigned	\$1,630,194	\$3,176,116	\$6,131,072
Total Fund Balance	\$5,462,536	\$8,423,927	\$11,912,075

The City's capital projects fund and internal service fund-workers' compensation (workers' compensation fund) had deficits for each of the last three years. The capital projects fund had an unassigned fund balance deficit of \$4.9 million and the workers' compensation fund had an unrestricted deficit of \$597,743 as of December 31, 2013.

The unassigned deficit in the capital projects fund increased each year from \$1.3 million in 2011, to \$1.9 million in 2012 and to \$5 million in 2013. The deficit increase from 2012 to 2013 was due to the increase in bond anticipation notes (BANS) issued to finance various capital projects. The deficit in the capital projects fund is expected to be eliminated when bonds are issued or BANS are redeemed.

Figure 2: Capital Projects Fund - Fund Balance

	FY 2011	FY 2012	FY 2013
Nonspendable	\$60,000	\$60,000	\$60,000
Unassigned	(\$1,276,399)	(\$1,939,321)	(\$5,021,613)
Total Fund Balance	(\$1,216,399)	(\$1,879,321)	(\$4,961,613)

The workers' compensation fund deficit declined from \$1.36 million in 2012 to \$597,743 as of December 31, 2013, or by 56 percent. City officials stated that this decline was due to increases in rates to user departments. They believe that the deficit will be eliminated by December 2014.

Figure 3: Internal Service Fund - Workers' Compensation Fund Balance

	FY 2011	FY 2012	FY 2013
Revenues	\$625,816	\$1,037,978	\$1,712,253
Expenditures	\$1,656,944	\$2,131,081	\$961,467
Operating Surplus/(Deficit)	(\$1,031,128)	(\$1,093,103)	\$750,786
Unrestricted Deficit Fund Balance	(\$1,772,777)	(\$1,356,512)	(\$597,743)

Recommendation

1. City officials should continue to monitor the capital projects and workers' compensation funds to ensure that the deficits in these funds are eliminated.

Cash Concentration Account

It is good business practice for a local government to minimize the number of bank accounts that it maintains. In addition, local governments should consolidate funds for investment to the extent possible with consideration for legal and accounting requirements. Local governments also should commonly group certain fund activities – such as payroll and disbursements for vendors’ activities – from several funds by using cash concentration accounts. Cash concentration is the transfer of funds from diverse accounts into a central account to improve the efficiency of cash management. The consolidation of cash into a single account allows a local government to maintain smaller cash balances overall, and to identify excess cash available for investment. Local governments should maintain separate accounting for the respective funds so that they are properly credited with interest earnings based on the amount of deposits. The City Charter is silent on the cash concentration system that the City uses.

City officials do not report cash assets in each fund’s cash account. All cash is deposited in a concentration account and recorded as an asset in the general fund. Instead of cash assets, the other City funds include amounts “due from other funds,” while the general fund includes a significant “due to other funds.”² As a result, the City’s financial statements are not as informative as they could be because the amount that the general fund owes the other funds is not generated from direct cash advances or services from these other funds to the general fund. Rather, this balance results from the City’s practice of depositing cash from all funds into the concentration account without maintaining a separate ledger account for cash in the respective funds. All accounting for cash among the City’s funds is done through the “due to/due from” accounts. Consequently, any increase of activities in these funds automatically shows an increase in “due to other funds” in the general fund. Interest income accrued from deposits in the concentration account is allocated to the various City funds.

The City has handled the trust and agency fund differently from other funds. Individual trust items totaling \$2.9 million were deposited in the concentration account and recorded as accounts receivable in the trust and agency fund. Because these funds were available for use in the concentration account instead of being properly segregated as an investment, they might not be available when needed for the purpose

² “Due to other funds” is a liability account used to record financial activities that result in one fund owing money to another, while “due from other funds” is the asset equivalent.

or obligations of the respective trust.³ In addition, proceeds of debt⁴ totaling \$4.9 million, issued to finance capital projects for the capital projects fund, were included in the concentration account. These funds did not appropriately include ledger accounts to record cash assets in their respective funds and report in their respective financial statements.

The “due to other funds” in the general fund increased by approximately \$6 million from fiscal years 2011 through 2013 as a result of concentration account activity. As of December 31, 2013, general fund financial statements showed cash assets of approximately \$22 million and “due to other funds” of \$14.8 million, while other funds, which received significant amounts of cash from operations, showed minor petty cash balances and significant “due from other funds” balances. As a result, the City’s financial statements are not as transparent as they could be. While all funds have direct access to cash from the concentration account for payments of payroll and vendor invoices, City officials did not maintain separate cash accounts in the individual funds.

Showing inflated cash and “due to other funds” balances in the general fund, inflated “due from other funds” in the enterprise and capital funds, and receivables in trust and agency funds can be misleading. This practice does not show the true financial position of each fund. Further, it does not provide the level of protection required for trust and agency funds and proceeds of debt for capital projects fund activities.

Recommendation

2. City officials should establish and use cash account codes to record revenue deposits and disbursements for each fund.

³ Trust and agency funds are required by law to be used only for their intended purposes. Trust and agency funds must be available to fulfill the requirements of the individual trust.

⁴ Proceeds of debt are required by law to be used only for their intended purposes.

APPENDIX A

RESPONSE FROM LOCAL OFFICIALS

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

Department of Finance
515 North Avenue
New Rochelle, NY 10801



Tel (914) 654-2063
Fax (914) 654-2344

Howard Rattner
Commissioner

City of New Rochelle New York

August 19, 2014

Ms. Tenneh Blamah
Chief Examiner of Local Government and School Accountability
Office of the State Comptroller
33 Airport Center Drive, Suite 103
New Windsor, N. Y. 12553

RE: City of New Rochelle Financial Condition
Draft Audit Report Dated July 2014
2014M-158

Dear Ms. Blamah:

We have reviewed the above referenced audit report and offer the following comments in accordance with your letter dated July 23, 2014.

Recommendation #1 – Continue to monitor Capital and Workers’ Compensation Funds

The report notes a deficit balance in the Capital Projects Fund as of December 31, 2013. The report also acknowledges that the deficit is expected to be eliminated when bonds are issued or BANS are redeemed. We agree with both of these findings. It has been the practice of the City of New Rochelle to take advantage of historically low short-term interest rates by issuing Bond Anticipation Notes (BANS) for a one-year period and renewing those notes annually for a five year period or, for longer-term construction projects, converting the notes to bonds. Under generally accepted accounting principles for government entities, BAN proceeds are recognized as a liability when issued and as revenue when redeemed; consequently, until the BANS are fully redeemed, or bonds issued, a deficit occurs.

In March 2014, the City issued bonds which eliminated approximately \$3.5 million of the \$5 million fund balance deficit as of December 31, 2013. The balance of the deficit will be eliminated over the next few years as the BANS are redeemed.

The report also notes that the deficit position in the Workers’ Compensation Fund was reduced from \$1.36 million in 2012 to \$597,743 as of December 31, 2013. The Workers’ Compensation Fund is an internal service fund which is funded by user charges to operating departments. For several years, workers’ compensation costs exceeded budgetary estimates due to State-mandated increased

compensation rates coupled with the deleterious effects of an older and leaner workforce. To address this condition, user charges were increased in both the 2013 and 2014 adopted budgets which will totally eliminate the deficit position by December 31, 2014.

Recommendation #2-Establish and use cash account codes to record revenue deposits and disbursements for each fund

For many years, the City has maximized investment income by employing a pooled cash investment practice where funds are deposited in demand deposit accounts, time deposit accounts and certificates of deposit with original maturities of less than three months. The City's treatment of these funds is in accordance with General Municipal Law Section 10 and Chapter 42 of the Municipal Code and is fully collateralized and/or insured.

We concur with the auditor's finding that cash from all operating funds is deposited in this concentration account without maintaining separate general ledger cash accounts in each fund. The City's governmental fund financial reporting uses the current financial resources measurement focus and the modified accrual basis of accounting where revenues, by fund, are recognized when measurable and available and expenditures are recorded when a liability is incurred. While the cash is deposited in the concentration account, each fund records its respective assets as "due from other funds" and its respective liabilities as "due to other funds". Therefore, the net assets, liabilities and fund balances of each fund would be unchanged if the City recorded its cash in the manner recommended in the audit report.

With respect to the treatment of the cash deposited in the trust and agency fund, we concur that approximately \$2.9 million of that fund's assets is shown as a receivable rather than an investment. We will reclassify this treatment although again it should be noted that this would have no bottom line impact on our financial statements.

Finally, it should be noted that the City received an unqualified opinion on our FY 2013 financial report from our independent audit firm in accordance with generally accepted accounting principles and has been awarded the Government Finance Officers Association's Certificate of Achievement for Excellence in Financial Reporting for the past twenty-two years. That award recognizes that the City's financial statements conforms with "...the highest standards of preparation of state and local government financial reports".

We appreciate the opportunity to present these comments in response to your report.

Very Truly Yours,

HOWARD RATTNER
Finance Commissioner

APPENDIX B

AUDIT METHODOLOGY AND STANDARDS

Our overall goal was to assess the City's financial condition and identify areas where the City could realize efficiencies and protect assets from loss or misuse. To accomplish this, our initial assessment included a comprehensive review of the City's financial condition.

To achieve our financial condition objective and obtain valid audit evidence, we performed the following audit procedures:

- We reviewed the City's policies and procedures for developing and reporting information relevant to financial and budgeting activities. This included gaining information on City officials' fiscal responsibilities.
- We interviewed City officials to determine what processes were in place and gain an understanding of the City's financial condition and budget.
- We reviewed and analyzed the City's financial records and reports for all funds, including balance sheets, budget reports, and statements of revenues and expenditures.
- We reviewed the City's multiyear financial plan to determine if it was up-to-date.

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

APPENDIX C

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APPENDIX D

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AND SCHOOL ACCOUNTABILITY

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