



# City of Rome

## Internal Controls Over Capital Projects

### Report of Examination

Period Covered:

January 1, 2010 — December 31, 2011

2012M-248



Thomas P. DiNapoli

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# State of New York Office of the State Comptroller

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## **Division of Local Government and School Accountability**

March 2013

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 Rome, entitled Internal Controls Over Capital Projects. 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*

# Introduction

## Background

The City of Rome (City) is located in Oneida County and has a population of approximately 33,700 residents. The eight-member Common Council (Council) is the City's legislative branch and comprises the elected Council President and seven elected members. The Mayor is the chief executive officer and is the president of the Board of Estimate and Contract (Board). The Board is charged with such things as letting contracts and setting salaries. The Mayor appoints a City Treasurer (Treasurer) who is responsible for the City's fiscal affairs. The Treasurer's office includes a Deputy Treasurer and City accountant. The City provides various services to its residents including general government support, police and fire protection, garbage collection, water and sewer service, and recreation. The City's budgeted general fund expenditures for the 2011 fiscal year were \$40.7 million.

Capital project funds are used to account for all of the financial activity related to the acquisition or construction of major capital assets. The City finances its capital projects through borrowings, grants, and other sources of revenue such as State aid. During our audit period, the City has undertaken 10 capital projects totaling \$6.9 million. Capital project expenditures for the last three fiscal years totaled \$8.5 million.

## Objective

The objective of our audit was to determine whether City officials provided effective oversight for capital projects. Our audit addressed the following related question:

- Did the City have adequate controls in place to properly authorize, account for and monitor capital projects?

## Scope and Methodology

We examined the City's capital projects for the period January 1, 2010 to December 31, 2011. We extended our review through August 2012 to include the closeout of 56 capital projects.

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 they planned to initiate corrective action.

The 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 to make this plan available for public review in the Clerk's office.

## Capital Projects

City officials are responsible for properly authorizing capital projects, ensuring they receive adequate funding, monitoring their financial activity, and for closing completed projects in a timely manner. Unexpended funds from bonds must be applied to the related debt<sup>1</sup> and unexpended funds from interfund transfers must be returned to the funds that originally supplied the resources.

While City officials had procedures to properly authorize capital projects, they did not adequately monitor financial activity or close completed projects in a timely manner. As a result, the City had 87 open capital projects, only nine of which were active – leaving 78 projects that had been completed, but still open in the records. Forty-eight of the completed projects had surplus balances totaling \$3.4 million, \$2.4 million of which must be transferred to the debt service fund or reserve for debt. The remaining 30 completed projects had deficits totaling \$3 million because they either did not receive the expected financing or were over-expended. The failure to properly manage capital projects has limited the transparency of the financial position of the City’s general fund.

City officials use the capital projects fund to account for the financial activity relating to acquisition or construction of major capital assets.<sup>2</sup> The Council is responsible for establishing procedures to properly authorize, finance, and monitor the status of individual capital projects. The Council and City officials should monitor the status of each project by reviewing financial reports from the Treasurer that compare actual revenues and expenditures to the approved budget.

Once a project is complete, the Treasurer should prepare a final accounting of the project and determine if any interfund loans that may have been necessary were paid back to the appropriate funds. The Council should adopt a resolution to close the project and dispose of any unexpended balance based on the project’s funding source(s). Unexpended funds originating from bonds must be applied to the related debt (transferred to the debt service fund or reserve for debt) and unexpended funds originating from interfund transfers must be returned to the fund that originally supplied the resources.

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<sup>1</sup> Transferred to the debt service fund or reserve for debt

<sup>2</sup> The City’s water and sewer funds are primarily financed by user charges and are accounted for on the enterprise basis of accounting. Although the City records capital projects related to these funds within the capital projects fund accounting records, the associated financial activity is reported in the water and sewer funds in the City’s financial statements.

All projects undertaken during our audit period were properly authorized. The Council approved capital projects financed by borrowing or capital reserve fund moneys, and the Board approved capital projects that were funded by other revenue sources (e.g., grants, State aid, or interfund transfers).<sup>3</sup> However, the City had no formal process to monitor the capital projects. The Treasurer's office did not prepare budget versus actual reports for each project, so the Council did not receive financial information that would enable it to monitor the revenues and expenditures related to each project or determine if any projects had deficits and thus required additional funding. While departments in charge of certain projects maintained folders with documentation<sup>4</sup> about those projects, they did not keep a record showing the financial results, such as where each project stands in comparison to the project budget. Such reports would have allowed City officials to compare individual capital project expenditures to authorized amounts and ensure appropriate resources were received in a timely manner to fund related costs.

In addition, the City did not have procedures to routinely close out capital projects when they were completed. Although the Deputy Treasurer closed 12 water and sewer capital projects that had surplus fund balances in 2011, this was the first time any capital projects had been closed in many years. During the course of our audit fieldwork, City officials made considerable progress in evaluating capital projects and identifying those projects that were complete and should be closed out. The City identified 78 completed projects that were still open in the records as of 2011. Many of these projects dated back to the 1990s – some with surplus balances and some with deficits. For example, the City's open projects included a 1993 project for the purchase of a wheel loader with a deficit balance of \$63,732, a 1997 project for parking garage improvements with a surplus fund balance of \$174,909, and a 1998 project for bus terminal renovations with a deficit fund balance of \$249,019. Without a proper closeout of projects, the Council cannot determine the final cost of each project and may be unaware of project overruns, cash balances remaining or outstanding loans that must be repaid to other funds.

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<sup>3</sup> Of the 10 projects undertaken during our audit period, six were funded by borrowing or a capital reserve and all six were authorized by the Common Council. The other four were approved by the Board, which consists of the Mayor, the Corporation Counsel, the Commissioner of Public Works, the Treasurer and the President of the Common Council.

<sup>4</sup> The folders contained documentation such as the Board resolution to accept a contract, the contract, other legal paperwork (e.g., the insurance and workers compensation forms), and resolutions regarding change orders or financing. We did not find any budget versus actual financial results in the capital project folders.

In total, the City had 78 open completed capital projects. Over a third of the projects (30 projects) had deficit fund balances – meaning the project expenditures exceeded the project revenues, totaling about \$3 million combined. According to the Treasurer, the reasons for these deficits varied but, essentially, the projects were either over-expended, did not receive expected financing, or a combination of the two. In either case, the related operating fund would be responsible for providing the funds to close these projects. In addition, 48 projects had funds remaining after the projects were completed, many of which were funded by debt. According to Local Finance Law,<sup>5</sup> any bond proceeds remaining after a project is completed must be used only to pay debt service on the associated debt. Because many of these projects were funded by debt, the residual balances must be restricted and used to pay debt service on the related obligations.

Table 1 shows a breakdown of the 60 completed projects in the general fund and the net effect on the general city and inside district if all projects were closed out as of December 31, 2011.<sup>6</sup> Table 2 shows the results of the 18 completed projects in the water and sewer funds. Because the water and sewer funds are accounted for as enterprise funds, capital project activity is already reported within these funds in the financial statements.

<b>Table 1: Net Effect of Closing Completed Capital Projects in the General Fund</b>			
<b>Fund</b>	<b>Description</b>	<b>Surplus Moneys to be Restricted for Debt Service</b>	<b>Net Deficits that Require Funding</b>
General Fund - General City (56 Projects)	Surplus that must be restricted to pay off the related debt	\$2,085,897	
	Surplus available for transfer to the general fund		\$660,637
	Deficits that require funding		(\$1,531,758)
	<b>Net deficit that requires funding</b>		<b>(\$871,121)</b>
General Fund - Inside District (4 Projects)	Deficits that require funding		(\$292,719)
	<b>Totals</b>	<b>\$2,085,897</b>	<b>(\$1,163,840)</b>

<sup>5</sup> Section 165

<sup>6</sup> The general fund is made up of the general city and inside district. The inside district portion is related to police expenditures.

<b>Table 2: Summary of Open Completed Projects in Water and Sewer Funds</b>			
Water (8 Projects)	Surplus that must be restricted to pay off the related debt	\$216,687	
	Deficits		(\$177,029)
Sewer (10 Projects)	Surplus that must be restricted to pay off the related debt	\$119,227	
	Surplus available for unrestricted use in the sewer fund		\$347,921
	Deficits		(\$1,004,189)
	<b>Net deficits</b>		<b>(\$656,268)</b>
<b>Totals</b>		<b>\$335,914</b>	<b>(\$833,297)</b>

As shown in Table 1, if all the completed projects were closed in the general fund, \$2.1 million would have to be restricted for debt service and net deficits totaling \$1.2 million would have to be recorded to reduce the unassigned portion of fund balance in the general city and inside district funds. In August 2012, the Council passed a resolution that authorized the Treasurer to retroactively close the 56 completed projects in the general city fund, as of December 31, 2011. In aggregate, the projects with surpluses and associated outstanding debt were closed by transferring \$2,085,897 to the reserve for debt in the general city fund.<sup>7</sup> The remaining surplus from those projects combined with the projects that had deficits amounted to a combined deficit of \$871,121. When these projects were closed, it resulted in a decrease of \$871,121 in unassigned fund balance in the general city fund. As a result, that fund ended the 2011 fiscal year with a reported unassigned fund balance deficit of \$566,341.<sup>8</sup>

As of the end of our fieldwork, City officials had taken no action to close the remaining 22 completed projects in the other funds. Our review of the 2011 financial statements indicates that the inside district fund has sufficient resources to address the respective deficit in the capital projects that were associated with that fund (\$292,719). The water and sewer projects' net deficits are already included within the water and sewer enterprise funds unrestricted net assets.<sup>9</sup> However, the City has not yet restricted the \$355,914 surpluses in these funds that must be used to pay off the related debt.

The failure of the Council to oversee capital projects has resulted in projects being overspent and not receiving appropriate funding. In addition, without a proper closeout of each project, the City's

<sup>7</sup> For projects with multiple sources of financing (e.g., bonds, State/Federal aid, interfund transfers), the entire residual balance was considered bond proceeds and credited to the reserve for debt.

<sup>8</sup> The City had not yet closed its 2011 books when the Council passed this resolution. Therefore, the Treasurer recorded these entries retroactively and the adjustments are reflected in the City's December 31, 2011 reported balances.

<sup>9</sup> An unrestricted net asset is an asset with no external restriction as to use or purpose. The restricted net assets in the City's enterprise funds include those invested in capital assets, net of debt.

final financial position is not transparent. The Treasurer told us that he has now assigned his Deputy Treasurer to work directly with the department heads to make sure funding is in place for each capital project and that project spending does not exceed authorized amounts.

## **Recommendations**

1. The Council should monitor each project by requiring the Treasurer to submit periodic reports that show actual revenues and expenditures over the life of the project compared to the approved budget.
2. The Council should close out the remaining capital projects that are complete and develop procedures to ensure that current and future capital projects are closed in a timely manner and any cash or deficit remaining is accounted for properly.

**APPENDIX A**  
**RESPONSE FROM LOCAL OFFICIALS**

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

JOSEPH R. FUSCO, JR.  
Mayor



JOHN MAZZAFERRO  
Common Council President  
(315) 838-1731

**OFFICE OF THE PRESIDENT OF THE COMMON COUNCIL**

ROME CITY HALL, 198 N. WASHINGTON STREET

ROME, NEW YORK 13440-5815

Fax: (315) 838-1165

[www.romenewyork.com](http://www.romenewyork.com)

February 13, 2013

Office of the State Comptroller  
Division of Local Government & School Accountability  
PSU – CAP Submission  
110 State Street, 12 th Floor  
Albany, NY 12236

Re: Response to Report of Examination of City of Rome's Internal Controls Over Capital Projects  
Audit Report Number 2012M-248

Dear Sir:

The City of Rome Common Council members are in receipt of the above referenced report. We agree with the findings outlined and will present a formal Corrective Plan of Action within the 90 day time frame specified within the report.

Very truly yours,

John Mazzaferro  
President of the Common Council

Cc. Members of the Common Council

## APPENDIX B

### AUDIT METHODOLOGY AND STANDARDS

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

- Interviewed City officials and employees to determine how capital projects are authorized, monitored and closed out.
- Reviewed the City charter to determine how projects should be authorized.
- Reviewed Council and Board minutes to determine whether projects were authorized.
- Traced project authorizations to accounting system reports to verify they agreed.
- Reviewed departmental records to determine how departments monitor capital projects.
- Reviewed accounting system reports and City spreadsheets to determine whether completed capital projects are closed out.
- Analyzed the impact on the operating funds' financial condition if/when completed projects are finally closed out.
- Reviewed accounting system reports and City spreadsheets to determine whether the City maintains separate accounting records for each project.
- Traced project revenues between bank statements and the accounting system reports to determine whether funds are properly segregated and accounted for.
- Reviewed the external auditor's reclassifying entry as of December 31, 2009 to gain an understanding of the establishment of the many due to and from accounts in the capital projects fund.
- Compared accounting system reports and City spreadsheets for consistency.
- Compared City-reported financial results (Annual Update Document) to externally audited financial statements for consistency.

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

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Andrew A. SanFilippo, Executive Deputy Comptroller  
Steven J. Hancox, Deputy Comptroller  
Nathaalie N. Carey, Assistant Comptroller

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