



**Philip J. LaTessa**  
**City Auditor**

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**CASH & INVESTMENTS AUDIT**

**APRIL 1, 2006 – JUNE 30, 2006**

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**Introduction:**

As required under Article V, Section 5-503, of the Charter of the City of Syracuse, the annual audit of the City of Syracuse's cash and cash equivalents activity for the period April 1, 2006 through June 30, 2006 was conducted. The purpose of this audit is to review cash and investment activity as set forth in the City of Syracuse Investment Policy and the City of Syracuse Charter, as adopted by the Common Council. The examination was administered in accordance with the *Generally Accepted Government Auditing Standards*, issued by the Comptroller General of the United States and *Standards for the Professional Practice of Internal Auditing*, as circulated by the Institute of Internal Auditors.

These standards require that we plan and perform the examination to afford a reasonable basis for our judgments and conclusions regarding the organization, program, activity or function under examination. It was not our objective to, and we do not, express an opinion on the financial statements of the City of Syracuse, New York, or provide assurance as to either the City's internal control structure or the extent of its compliance with statutory and regulatory requirements and guidance of the Office of the State Comptroller.

The management of the City of Syracuse, New York, is responsible for the City's financial affairs and for safeguarding its resources. This responsibility includes establishing and maintaining an internal control structure to provide reasonable, but not absolute, assurance that resources are safeguarded against loss from unauthorized use or disposition; that transactions are executed in accordance with management's authorization and are properly recorded; that appropriate financial records are prepared; that applicable laws, rules and regulations are observed; and that appropriate corrective action is taken in response to audit findings.

This report is intended solely for the information of the Mayor and Common Council of the City of Syracuse, New York, yet it is understood to be a matter of public record and its distribution is not limited. Further information regarding this audit is available at the City of Syracuse's Audit Department upon request. The Audit Department would like to thank the personnel who assisted and cooperated with us during the audit.

**Scope:**

The scope of the examination entailed reviewing the bank statements, collateralized deposit data, general ledger and related records for the period April 1, 2006 through June 30, 2006.

**Objectives:**

The original objectives of the cash and investment audit were as follows:

1. Determine whether the cash balances represent all cash and cash items on hand, in transit to or in financial institutions and are properly recorded.
2. Determine whether funds are properly collateralized.
3. Assess the cash balances in non-interest bearing accounts.

**Methodology:**

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To reach the assurance that the cash balances represented all cash items on hand, in transit to or in appropriate financial institutions and properly recorded, and that all investments and cash funds are properly collateralized, the Department of Audit tested the City's cash and cash equivalents activity for each month in the audit period. For the liquid asset (cash) accounts belonging to the City departments, the Department of Audit tested the information found on the Bank Reconciliations and Schedules of Collateral to the corresponding bank and collateral statements via the financial institutions. Once the proper figures were determined, they were traced to the general ledger detail to ensure all cash items were properly represented and recorded. The collateralized funds were recalculated to ensure accuracy.

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

The Department of Audit interviewed Finance Department staff, including the Systems Accounting Manager, with the purpose of getting a fuller understanding of the influences affecting the timeliness of the reconciliations done as a part of cash management.

**Conclusion:**

With reasonable assurance, it was determined that the City's cash and cash equivalent balances were free from material misstatements for the period April 1, 2006 through June 30, 2006. For the period examined, the Audit Department was reasonably assured that all city accounts were properly collateralized.

**Auditor's Note:**

On March 15, 2007, the Audit Department issued the cash and investments audit report for the quarterly period from January 1, 2006 through March 31, 2006, covering the third quarter of the 2005/06 fiscal year. That audit included mention of a finding reported on other occasions during the auditing of the city's cash and investments for the 205/2006 fiscal period. The specific finding pertained to the large compensating balance retained at JP Morgan Chase Bank on behalf of the City of Syracuse.

In addressing the finding, the Finance Department informed the City Auditor that actions had taken to ameliorate the excessively large amount of cash that the City has kept in a non-interest bearing account over the last several years. Specifically, the City had taken steps as follows: The City had taken the initiative to print the 2007 Onondaga County Property Tax bills at the City in order to use larger coupons, similar to the coupons utilized by the City for City and City School District tax bills, which avail themselves to scanning; systems were instituted to allow data to be exchanged between the lockbox processor and the City Information Systems Department via e-mail in formatted text; and, the City had advertised the soliciting of RFQ's (Requests for Qualifications) for lockbox services with quotes having been received in early 2007.

**Background:**

As noted in the objectives for the Cash And Investment Audit For The Period Of April 1, 2006 Through June 30, 2006, the consistently large balance in the city's JP Morgan Chase Bank Account-Chase General Account #99.01.301.01 has been given closer scrutiny due to the substantial size of the balance and the non-interest bearing nature of this particular account. This

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follows a consistent pattern observed in Cash and Investment audits going back to January, 2005. In the beginning of January, 2005, the JP Morgan Chase Bank Account was twelve million dollars. During that month, the account balance was reduced to ten million dollars, which has remained the consistent amount held in this non-interest bearing account until the end of calendar 2005.

The Chase Bank Account carried forward the ten million dollar balance into January, 2006; this amount was reduced by two million dollars in February and remained at the eight million dollar level through June 30, 2006. This adjustment came as the result of the Finance Department determining in conjunction with Chase Bank what a sufficient amount was to compensate for related services, taking into consideration the level of activity, the changes to interest rates, etc. that are the basis for the non-interest bearing balance required by the bank.

In previous audits, these findings raised questions as to why the City would leave such large amounts of cash in accounts with virtually no activity and not producing any interest earnings for the City. The explanation provided by the Finance Department relates to the fact that this JP Morgan Chase Bank Account is a compensating balance bank account. Compensating balances are balances held in accounts that generate no interest earnings and are used by the bank in lieu of charging for a specified set of services, predominantly in this instance, the lockbox operation.

JP Morgan Chase was selected in February 2003, based on a Request For Proposal (RFP) to provide lockbox services to the City relative to the collection of taxes, parking tickets and water billing. The responses received to the RFP, from JP Morgan Chase, M&T and Fleet Banks, were reviewed by a Request For Proposal Committee and a recommendation to select Chase Bank was made to the Mayor, approved by him and was about to be submitted to the Council for approval when the Law Department determined that the Commissioner of Finance had the authority to negotiate the contract and that Council approval was not required. The Commissioner of Finance communicated to JP Morgan Chase Bank the city's intention of retaining the bank for the lockbox services; and although they were already the financial institution providing the services at that time, their response to the RFP was, by far, the lowest. At that time, the City also negotiated the arrangements whereby the lockbox services were to be paid for by using compensating balances to off-set the cost rather than actually charging the city for the various lockbox transactions times the specific per-item fee.

For the processing of the tax payments, the City's tax stubs contain a feature permitting electronic scanning (Optical Character Recognition). The tax bills sent out by the City, as the agent for the collection of Onondaga County's taxes have not included the electronic scanning feature until the 2007 Onondaga County Property Tax bills were printed by the City, using larger payment stubs, to change the situation that had for some time prevented the lockbox processor from scanning both City and County payments. Due to the fact that almost all City and County taxes (two different coupons) are paid by one check, previously, it was not possible to process the City coupon by scanning and the County coupon manually. However, JP Morgan Chase Bank had been charging the lower scanning fee for both City and County coupons, as noted in the information provided by the Finance Department in Number 2 and Number 3, below. The nature of the City Auditor's concern centered on the fact that the situation presented by the smaller County payment stubs, which prevented scanning as an option, limited the potential competition among financial institutions in bidding on the City's business.

The water bill stubs are OCR coded and the City is charged the lower rate for the water payments processed through the lockbox. The parking ticket stubs received at the lockbox are manually processed due to the fact that the nature of the instrument ( the tickets that are sent in with the

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associated payments) prohibits electronic scanning, frequently being exposed to elements such as rain, snow, etc, therefore limiting the use of the more advanced technology.

The fees being charged by the bank is \$0.345 for tax coupons and water stubs, and \$0.74 for parking ticket stubs. The Finance Department personnel interviewed while researching this topic stressed several points regarding the current relationship with JP Morgan Chase and the unusually large amounts retained in the Chase General Account:

1. The large amount that was held in the Chase General Account was a reflection of extremely low interest rates in the market during 2005 compounded by the extremely long time that rates were at these all-time lows. Indeed, at the end of the calendar year 2005, these large balances were still insufficient, per the analysis, to provide adequate coverage of the services. However, JP Morgan Chase waived the difference.
2. Chase Bank had operated in a way that was beneficial to the City by using compensating balances as the basis for recovering its cost as opposed to paying interest on the balances and charging the fee provided for by means of the RFP. Since banks are driven by balances rather than a profit/loss statement, it is more in their interest to have the moneys sitting in the account; this benefit translates to a better pricing being made available back to the City.
3. Recognizing the benefits noted in Number 2, Chase Bank was willing to offer the City the benefit of the scanning price for County coupons and waive the insufficient account balances at year-end.

The Finance Commissioner has responded to questions regarding the arrangement which had continued between the City and Chase Bank in his management responses to the last several Cash and Investments audits. The Commissioner has regularly noted that before issuing another Request For Quotes, technological considerations and advancements need to be implemented to provide an environment where true competitive submittals are turned into the City for evaluation. Such prerequisite modifications have recently occurred and the Finance Department has moved to address the situation that had existed from 2003 until the beginning of 2007. In January 2007, the lockbox services were bid out via Request For Qualifications. Three quotes have been received and are currently in the evaluation process.

Additionally, in the Fall of 2005, the City of Syracuse administration, through the efforts of the Commissioner of Finance, began working with the Common Council in order to obtain legislative approval to introduce options for paying property taxes by means of credit card or e-Check via the internet. The Finance Commissioner took the lead role for the City in heading up a consortium of City and Onondaga County personnel in researching the requirements of New York State General Municipal Law, Section 5(b) and in the interviewing of prospective service providers as required by regulations adhered to by the City of Syracuse. The service provider selected, Municipal-Payments.com, an internet site owned and operated by Systems East, Inc. was determined to have the most user-friendly website and was capable of handling the complicated four-payment cycle of the City and County (for City residents) tax bills.

On December 19, 2005, the Common Council approved two ordinances that authorized the electronic payment option. The first ordinance, # 601-2005, authorized the Commissioner of Finance to accept payment of property tax bills, including all applicable fees, interest and penalties by Credit Card or e-Check via the internet in accordance with General Municipal Law (GML) Section 5(b). The proposed payment option was seen as a convenient method of payment

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should taxpayers chose to use the internet and as an enhancement that could reduce the administrative time for processing the over-the-counter and mail-in payments.

The second ordinance, #602-2005, provided for the waiving of the competitive bidding process for the selection of vendor to be contracted with to be the internet site for the acceptance of real property tax payments by credit card or e-Check for the City of Syracuse. A waiver of the competitive process was requested due to the fact that this undertaking was a collaborative project with Onondaga County and Systems East, Inc. had been able to meet the requirements of the joint property tax collection system. The term of the agreement was established to be for one year, with two one year renewal options exercisable by the City. Ordinance #602 further specifies that any charges associated with the individual transaction are to be paid by the internet user, not the City.

On May 8, 2006, the Common Council took action to extend internet payment capability to include payments for billing originating with the City of Syracuse Water Fund. Ordinances # 195 and # 196 of 2006 amended the two ordinances previously approved in 2005 to authorize internet payments specifically for water billing with incidental fees being charged back to the water fund. Future extensions of the internet payment capability are expected to be implemented over time, beginning with parking ticket payments.

The addition of internet receipts accounts meant that new reconciliations, with the same requirements as all other bank accounts, would need to become part of the monthly bank reconciliation process. Anticipating that the new payment options would create the need for additional levels of coordination, the City's Finance Department put together for internal use a preliminary document that was intended to outline the differences in the operation of these accounts, in contrast to other accounts, and initial solutions to problems that might be, in the early stages of the implementation of electronic payment processes, potential problems that could arise with the expansion of electronic transmissions as a desirable payment option.

Detailed in the preliminary "Internet Account Reconciliation" outline is the following information:

*The structure of the 412 account was set up so that it would collect data on taxpayer-initiated payments made through the Municipal-Payments.com website. This website is operated by the firm awarded the City contract and allows each department that is folded into the internet payment option (Treasury, Water, Parking Tickets, etc.) to run a daily report from the website, prepare a cash report and apply payments to taxpayer accounts. Each department may prepare two separate cash reports: one for credit card and another for e-Check payments. Deposits made to the bank will start at two per day-one for all credit card payments and another for all e-Checks. Note that Systems East does not receive or disburse cash; it only provides the interface through its Municipal-Payments.com website. This website collects payment data and passes the information to the City and to the companies processing credit card and e-Check transactions.*

*Based upon the selection of payment method, the transactions are relayed to the bank by Global Payments (for credit cards) or ACH Direct (for e-Check). Each of these entities makes available an audit trail report which ties to the deposit into the 412 account. The websites are Authorize.net for credit cards and PaymentsGateway.net for e-Checks. Generally, the four cash reports will tie into the two deposits in the bank. The reconciliation should assure that all deposits reported by Systems East/Municipal-Payments.com have indeed been credited to the City's bank account.*

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The Audit Department's initial review of bank reconciliations in the April-June, 2006 period, which was the first quarter where internet activity appeared, indicated some discrepancies existed between bank statements and what was appearing in the General Ledger for the 412 account. Subsequent interviews with Finance Department staff suggested some timing issues had been associated with the implementation of the new payment options, and the Audit staff was provided with the assurance that later bank reconciliations were becoming smoother and easier to complete with further attention having been devoted to reconciliation development for internet activity.

**Findings and Recommendations:**

**Recommendation 1: City's Reconciliation Of Internet Account Needs Continued Attention And Development**

The preliminary reconciliation document previously quoted quite accurately reflects the complex nature of the internet bank account. Accordingly, the review undertaken of the initial bank reconciliations for May and June, 2006, which were the first months to have internet activity hit the General Ledger and the City's bank account, indicated that there was significant additional work required on the part of the Finance Department to produce an adequate reconciliation report based on the inconsistent timing element combined with the rolling of multiple payments into single deposits, as associated with bank deposit reporting. This lack of clarity has created an environment wherein further development and refinement of methods for reconciliation were critical for maintaining internal monitoring of the payments made through the internet and for any meaningful reconciliation/confirmation work to be performed by either the City Audit Department or any other external auditing entity looking into the handling of these particular revenues.

**Recommendation:** It is the conclusion of the Department of Audit that the Finance Department of the City of Syracuse needs to include on a monthly basis, in the information conveyed to the Audit Department for the reconciliation of the 412 account, the audit trail reports that have been generated by Global Payments and ACH Direct for the credit card and e-Check payments and which have been conveyed to the City. These reports should be attached to the bank reconciliation as an integral part of the documentation forwarded to Audit to provide explanatory and sufficient back-up information. This additional detail will allow third party reviewers to fully understand the reconciliation work done in Finance and be able to confirm its accuracy.

**Management Response:**

"Future reconciliations for the internet account will include the requested information as part of the reconciliation package on a monthly basis. Additionally, management will strive to devise a less cumbersome reconciliation strategy."

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