

City of Rye, New York

Communication of Internal Control Matters Identified in the
Audit to Those Charged with Governance and Management

December 31, 2013

**Communication of Internal Control Matters Identified in the Audit to
Those Charged with Governance and Management**

**The Honorable Mayor,
Members of the City Council and
City Manager
City of Rye, New York
1051 Boston Post Road
Rye, New York 10580**

Auditors' Communication on Internal Control

In planning and performing our audit of the basic financial statements of the City of Rye, New York ("City") as of and for the year ended December 31, 2013, in accordance with auditing standards generally accepted in the United States of America, we considered the City's internal control over financial reporting ("internal control") as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control. Accordingly, we do not express an opinion on the effectiveness of the City's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control was for the limited purpose described in the first paragraph and was not designed to identify all deficiencies in internal control that might be deficiencies, significant deficiencies or material weaknesses and, therefore, there can be no assurance that all such deficiencies have been identified.

We did not identify any deficiencies in internal control that we consider to be material weaknesses, as defined above.

However, as indicated in the attached Addendum A, we share for your consideration other observations about the internal control and operations. In Addendum B, we identify other accounting and auditing matters for your information.

This communication and addenda are intended solely for the information and use of management and the City Council and are not intended to be and should not be used by anyone other than these specified parties. We will be pleased to discuss these communications and comments in further detail at your convenience, or to assist you in implementing the recommendations.

O'Connor Davies, LLP

O'Connor Davies, LLP
Harrison, New York
June 27, 2014

City of Rye, New York

Addendum A

Control Deficiencies

- **Capital Projects Fund**

Inactive Projects

Our audit of the Capital Projects Fund indicated that several projects had no financial activity during the current fiscal year.

Recommendation

A lack of financial activity in a capital project over an extended period of time may be an indication of the project's completion. Upon determination that a capital project has been completed, the governing board should pass a resolution indicating this status and directing the disposition of the unexpended proceeds. If the unexpended balance of the project consists of monies provided from obligations, its use would be restricted to the payment of outstanding indebtedness. If the remaining balance consists of a return of a contribution from an operating fund, it should be returned to that fund to be used for any lawful purpose.

Project Deficits

Our audit disclosed that the following capital projects reflected deficit fund balances as of December 31, 2013:

Kirby Lane Sanitary Sewer	\$	405,555
Annual Sidewalk Replacement Program		150,838
Upper Blind Brook Study		8,740

Recommendation

These deficits arise from expenditures exceeding current financing on these projects. We suggest that the Board address these deficits and authorize the necessary funding to insure their elimination.

- **Capital Assets**

Capital Assets Inventory

The City has not performed a physical inventory of its capital assets, primarily machinery, equipment and vehicles, in many years.

Recommendation

We recommend that the City follow through with its plan for a physical inventory of its capital assets to ensure that only those assets currently in use are reported in the books and records.

City of Rye, New York

Addendum A

Control Deficiencies

- **Journal Entries**

Our audit of the City's procedures related to authorization and approval of manual journal entries disclosed that there is no formal review and approval process in place.

Recommendation

Manual journal entries in excess of a predetermined monetary threshold should be reviewed by an individual not involved in creating the entry, to ensure appropriateness and accuracy. In order to improve the City's internal control, we recommend that consideration be given to redistributing these duties among available personnel.

- **Procurement Policy**

In accordance with General Municipal Law, the City is required to bid public works contracts in excess of \$35,000. Additionally, the City's procurement policy states that written quotes will be required for purchases of \$5,000 or more. Likewise, verbal quotes will be required for any purchase of at least \$2,500 and below \$5,000. However, in one instance, we noted that the City failed to bid a contract for bus services.

Recommendation

We recommend that the City follow its procurement policy and General Municipal law as noted above.

City of Rye, New York

Addendum B

Other Matters

- **Governmental Accounting Standards Board (“GASB”) Statement No. 68 “Accounting and Financial Reporting for Pensions”**

In June 2012, GASB issued Statement No. 68. This Statement establishes new accounting and financial reporting requirements for governments that provide their employees with pensions. This pronouncement supersedes Statement No. 27, “*Accounting for Pensions by State and Local Governmental Employers*.” Under this previous standard, *cost-sharing multiple employer defined benefit plans* (such as the plans administered by the State of New York for its municipalities and school districts) which share their assets *and* their obligations to provide pension benefits to their employees – i.e. plan assets can be used to pay the pensions of the employees of any municipal or school district employer that provides pensions through the plans, have not been required to present actuarial information about pensions. Instead, information has been required to be presented in the pension plans’ own financial statements for all of the participating municipalities and school districts combined.

The new Statement was designed to give users of the financial statements of cost-sharing employers access to better, more transparent financial information through the municipality or school district’s own financial statements. Under the new standards, cost-sharing employers will be required to report in their Statement of Net Position a net pension liability, pension expense and pension related deferred inflows and outflows of resources based on their proportionate share of the collective amounts for all of the municipalities and school districts in the plan. The net pension liability is the difference between the total pension liability (the present value of projected benefit payments to employees based on their past service) and the assets (mostly investments reported at fair value) set aside in a trust and restricted to paying benefits to current employees, retirees and their beneficiaries.

Statement No. 68 expands disclosures in the notes to financial statements and the required supplementary information (“RSI”). The note disclosures must include 1) a description of the plan(s) and the benefits provided, 2) the significant assumptions employed in the measurement of the net pension liability, 3) descriptions of benefit changes and changes in assumptions, 4) assumptions related to the discount rate and the impact on the total pension liability of a one percentage point increase or decrease in the discount rate and 5) the net pension liability and deferred inflows and outflows of resources. The RSI must provide ten year historical information (when available) regarding the entity’s proportionate share of the net pension liability and a schedule of the entity’s contributions. Notes to RSI are also now required regarding factors that significantly affect the trends in the schedules.

It is important to note that Statement No. 68 relates to *accounting and financial reporting* issues only, that is, how pension costs and obligations are measured and reported in the entity’s audited financial statements. This Statement *does not* address how the entity approaches the *funding* of the plan. The provisions of this Statement are effective for the City’s financial statements for the year ending December 31, 2015, with earlier implementation encouraged.

City of Rye, New York

Communication of Matters Identified in the Audit to Those Charged with Governance

We have audited the financial statements of the City of Rye, New York ("City") as of and for the year ended December 31, 2013, and have issued our report thereon dated June 2, 2014. Professional standards require that we provide you with information about our responsibilities under auditing standards generally accepted in the United States of America, as well as certain information related to the planned scope and timing of our audit. We have communicated such information in our engagement letter to you dated December 5, 2013. This letter provides additional required communications related to our audit.

Our responsibility under professional standards

Our responsibility is to form and express an opinion about whether the financial statements, which are the responsibility of management, are presented fairly, in all material respects, in conformity with accounting principles generally accepted in the United States of America ("US GAAP"). Those individuals charged with governance of the City are responsible for the oversight of the financial reporting process, and our audit does not relieve management and those charged with governance of their respective responsibilities.

Our responsibility for the supplementary information accompanying the financial statements is to evaluate the presentation of the supplementary information in relation to the financial statements as a whole and to report on whether the supplementary information is fairly stated, in all material respects, in relation to the financial statements as a whole.

With respect to such supplementary information, we made certain inquiries of management and evaluated the form, content and methods of preparing the information to determine that the information complies with US GAAP, the method of preparing it has not changed from the prior year, and the information is appropriate and complete in relation to our audit of the financial statements. We compared and reconciled the supplementary information to the underlying accounting records used to prepare the financial statements or to the financial statements themselves.

In connection with our audit, we performed tests of the City's compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit. Also in accordance with OMB Circular A-133, we examined, on a test basis, evidence about the City's compliance with the types of compliance requirements described in the "U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement" applicable to each of its major federal programs for the purpose of expressing an opinion on the City's compliance with those requirements. While our audit provided a reasonable basis for our opinion, it does not provide a legal determination on the City's compliance with those requirements.

Planned scope and timing of the audit

We conducted our audit consistent with the planned scope and timing we previously communicated to you.

City of Rye, New York

Communication of Matters Identified in the Audit to Those Charged with Governance

Qualitative aspects of significant accounting practices

Significant accounting policies

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by the City are described in Note 1 to the financial statements. There has been no initial selection of accounting policies and no changes in significant accounting policies or their application during the reporting period that had a significant impact on the financial statements. No matters have come to our attention that would require us to inform you about (1) the methods used to account for significant unusual transactions, and (2) the effect of significant accounting policies in controversial or emerging areas for which there is a lack of authoritative guidance or consensus.

Significant accounting estimates

Accounting estimates made by management are an integral part of the financial statements and are based on management's knowledge and experience about past and current events and assumptions about future events. Actual results could differ from those estimates.

Certain accounting estimates are particularly sensitive because of their significance to financial statements and their susceptibility to change, such as:

- Actuarial assumptions related to the Other Post Employment Benefit Obligations ("OPEB")
- Asset lives for depreciable capital assets
- Estimates of certain receivable balances and allowances for uncollectible amounts
- Estimates for certain operating and long-term liabilities

Management believes that the estimates used and assumptions made are adequate based on the information currently available. We evaluated the key factors and assumptions used to develop the estimates in determining that they are reasonable in relation to the financial statements as a whole.

Financial statement disclosures

Certain financial statement disclosures involve significant judgment and are particularly sensitive because of their significance to financial statement users. The most sensitive disclosures affecting the financial statements relate to:

- Pension plan information
- Other post employment benefit obligations payable
- Outstanding bonded indebtedness
- Fund balances

The financial statement disclosures are consistent and clear.

Significant difficulties encountered during the audit

We encountered no significant difficulties in dealing with management relating to the performance of the audit.

City of Rye, New York

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Uncorrected and corrected misstatements

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that we believe are trivial, and communicate them to the appropriate level of management.

We are required to communicate to you misstatements that remain uncorrected, including any related to prior periods, and the effect, if any, that they may have on the opinion in our report, and request their correction.

There are no such financial statement misstatements that remain uncorrected.

In addition, we are required to communicate to you all material, corrected misstatements that were brought to the attention of management as a result of our audit procedures. The adjusting journal entries following this communications letter summarize the material misstatements that were corrected by management.

Disagreements with management

For purposes of this letter, a disagreement with management is a matter, whether or not resolved to our satisfaction, concerning financial accounting, reporting, or auditing, which could be significant to the financial statements or the auditors' report. No such disagreements arose during the course of the audit.

Representations requested from management

We have requested certain written representations from management in a separate letter dated June 2, 2014.

Management's consultations with other accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters. Management informed us that, and to our knowledge, there were no consultations with other accountants regarding auditing and accounting matters.

Other matters discussed with management

We generally discuss with management a variety of matters, including the application of accounting principles and auditing standards, business conditions affecting the City, and plans and strategies that may affect the risks of material misstatement. None of the matters discussed and our responses thereto were a condition to our retention as auditors.

The former Rye Golf Club Manager resigned in February 2013 and was later arrested in November 2013 for alleged misuse/misappropriation of public funds. The City has filed an insurance claim for approximately \$2 million. The City is currently unable to determine the recoverability of the insurance claim, if any, and as such, no provision has been made for this amount in the financial statements.

We have provided our comments regarding deficiencies and other matters noted during our audit in the attached addenda.

City of Rye, New York

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Auditor independence

We affirm that O'Connor Davies, LLP is independent with respect to the City in accordance with professional standards.

This communication is intended solely for the information and use of the City Council and management of the City and is not intended to be and should not be used by anyone other than these specified parties.

Client: **City of Rye**
 Engagement: **Audit**
 Period Ending: **12/31/2013**
 Trial Balance:
 Workpaper:

Account	Description	W/P Ref	Debit	Credit
Account	Description	W/P Ref	Debit	Credit

General Fund

Adjusting Journal Entries JE # 7

To accrue the balance of hurricane Sandy debris removal project

41002	DUE FROM STATE GOVERNMENT		203,643.00	
4960	FEDERAL AID EMER DISASTER			203,643.00
Total			203,643.00	203,643.00

Capital Projects Fund

Adjusting Journal Entries JE # 2

To accrue federal aid and Con Ed reimbursements based on expenditures for the Central Avenue Bridge project

380	accounts receivable		30,387.00	
41001	DUE FROM FEDERAL GOVT		506,917.00	
2770	UNCLASSIFIED REVENUE			30,391.00
4597	FEDERAL AID TRANSPRTATION			506,913.00
Total			537,304.00	537,304.00

Adjusting Journal Entries JE # 5

To accrue revenue for Sluice gate project - County will reimburse 50%

44001	DUE FROM COUNTY GOVT		186,538.00	
277050	Westchester County Aid			186,538.00
Total			186,538.00	186,538.00

Debt Service Fund

Adjusting Journal Entries JE # 1

To record refunding debt activity - 2013 refunding

54903	FINANCIAL/AUDITING SVCS		6,655.00	
56011	PMT TO REFUNDED BOND AGENT		385,828.00	
2710	PREMIUM ON OBLIGATIONS			13,598.00
5711	REFUNDING BONDS ISSUED			378,885.00
Total			392,483.00	392,483.00

Risk Retention Fund

Adjusting Journal Entries JE # 5

To accrue - based on additional receivable in excess of retention amounts (Caspi Case)

380	ACCOUNTS RECEIVABLE		111,483.00	
268000	GENERAL INS RECOVERIES			111,483.00
Total			111,483.00	111,483.00