

**AUDIT COMMITTEE OF THE CITY OF NEW YORK**

**MINUTES OF THE AUDIT COMMITTEE MEETING**

**HELD ON WEDNESDAY, FEBRUARY 26, 2014**

**OFFICES OF SKADDEN, ARPS, SLATE, MEAGHER & FLOM LAW FIRM**

**ATTENDANCE**

|                             |  |
|-----------------------------|--|
| <b>Chair</b>                | <b>Bernard Rosen</b>   |
| <b>Private Members</b>      | <b>Bud Larson<br/>Michael Spitzer<br/>Mark Kaplan</b>  |
| <b>Public Members</b>       | <b>Representing the Mayor – John Grathwol<br/>Representing the Comptroller – Michele Mark Levine</b>   |
| <b>Secretary</b>            | <b>Jacqueline Thompson</b>   |
| <b>Independent Auditors</b> | <b>Deloitte &amp; Touche LLP – James Curry, Mike Malloy, Jill Strohmeier, Glenn Friedrich</b>  |
| <b>Others</b>               | <b>NYC Water and Sewer (NYW) – Robert Balducci, Alan Anders, Valerie Mehallow, Thomas Paolicelli, Steve Lawitts, Mathilde McLean, Sheila Misra<br/><br/>Hudson Yard Infrastructure Corporation (HYIC) – Robert Balducci, Jay Olson, Warren Ruppel, Alan Anders<br/><br/>Hudson Yard Development Corporation (HYDC) – David Farber, Warren Ruppel<br/><br/>NYC Tax Lien Trusts (TRUST) – Jay Olson, David Spara, Joel Cooper, Andrea Gilbert, Alan Anders<br/><br/>NYC Transit Finance Authority (TFA) – Kemraj Narine<br/><br/>TSASC, Inc. (TSASC) - Robert Balducci, Jay Olson, Alan Anders<br/><br/>Sales Tax Asset Receivable Corporation (STAR) - Robert Balducci, Alan Anders, Jay Olson<br/><br/>Fiscal Year 2005 Securitization - Robert Balducci, Alan Anders, Jay Olson, Jeffery Roude<br/><br/>NYC Technology Development Corporation (TDC) – Robert Balducci, Eileen E. Cleary, Paul L. Herzfeld, Jill Strohmeier, Glenn Friedrich<br/><br/>New York City Office of Management &amp; Budget – Nicole Fleming, Enid Ellis,</b> |

**NYC Financial Information Services Agency- Richard McCarrick, Adrienne Edley, Rose Ellen Myers**

**New York City Mayor's Office of Operations – George Davis  
Office of the Public Advocate - Lawrence Schimmel**

**New York City Comptroller's Office – Maria Tavares, Thema Holder, Susan Cornwall, Berta Lara**

## Audit Committee Meeting-February 26, 2014

### **I. Review of the Draft Minutes of the Audit Committee Meeting held January 15, 2014**

Mr. Bernard Rosen, the Chair called the meeting to order at 9:30 a.m. The first agenda item was the approval of the draft minutes of the January 15, 2014, Committee meeting. Chair Rosen inquired if there were any comments on the draft minutes as presented. Subject to the editorial comments submitted to Ms. Jacqueline Thompson, Committee Secretary, the Committee approved the draft minutes of the January 15, 2014 meeting.

### **II. Financial Statements and Management Letters for the Following**

#### **1. New York City Water and Sewer System**

The next agenda item was the review of the financial statements and management letter for the New York City Water and Sewer System (“NYW”) for the fiscal year ended June 30, 2013. Mr. Robert Balducci, Deputy Comptroller at The New York City Municipal Water Finance Authority (“MWFA”), introduced the representatives of the MWFA, the New York City Water Board (“WB”) and noted that Deloitte & Touche LLP (“D&T”) was NYW’s independent auditor.

Mr. Balducci informed the Committee that in fiscal year 2013 NYW implemented two new Government Accounting Standards Board (GASB) Statements, GASB Statements 63 and 65. The old "Statement of Net Assets" was renamed "Statement of Net Position," which reflects the requirements of GASB 63.

Mr. Tom Paolicelli, Executive Director at MWFA, reported on MWFA's financial statements for fiscal year 2013. MWFA issued \$2.4 billion in bonds and paid about \$1.9 billion to The City of New York (the City) from its commercial paper bond proceeds for construction costs. On the revenue side, water and sewer revenues increased primarily as a result of an annual rate increases. WB increased rates by 5.6% and 7.0 % in fiscal years 2014 and 2013 respectively. Operating revenues increased by 7.6% in fiscal year 2013 from the prior year. On the expense side, there was a small decrease in operational maintenance expenses primarily due to a reduction in headcount in 2013. Other expenses decreased by about \$59 million. Due to Hurricane Sandy, \$17 million in asset impairment losses was recognized.

Mr. Paolicelli reported that cash and equivalents in investments were \$2.1 billion in fiscal year 2013, an increase of \$366 million from the prior year. On the *Combining Statement of Net Position for fiscal year 2013, pages 23- 24*, "Net position" was a negative \$483 million as compared to a negative \$809 million in fiscal year 2012. The primary driver of negative net assets is the payment for non-capital assets with bond proceeds. The cumulative amount of non-capital assets which were paid for with bond proceeds was about \$1.2 billion. Mr. Paolicelli informed the Committee that MWFA had two hedging derivatives and one investment derivative in fiscal year 2013, which provided a lower cost for funding.

Mr. Steve Lawitts, Chief Financial Officer at the Department of Environmental Protection, and Executive Director at WB, reported that as a result of Superstorm Sandy WB suffered close to \$100 million in damages to fourteen wastewater treatment plants and about half of the 95 wastewater pumping stations. WB continues to work with Office of Management and Budget and the Federal Emergency Management Agency ("FEMA") to cover the losses. The ultraviolet light disinfection facility in Westchester County for treatment of water from the Catskills and Delaware systems,

operated for its first full year in fiscal year 2013. The plant is the largest one of its kind in the world with a capacity of over 2 billion gallons of water a day.

Mr. Lawitts reported that construction began on "Water for the Future" in fiscal year 2013, which is a program that will permanently fix the leak in the Delaware Aqueduct, which carries 50% of the City's drinking water. Construction continued on the Brooklyn/Queens portion of Water Tunnel No. 3 in fiscal year 2013. The tunnel is active throughout Manhattan. The MWFA and the Port Authority are sharing the cost of construction on a new tunnel to carry water from Brooklyn to Staten Island. Start-up testing had begun in the Croton Water Filtration plant, full operation is planned for later in 2014.

Following the presentations there was a question and answer session regarding the following issues. WB released its Wastewater Treatment Resiliency Plan earlier in fiscal year 2013. WB is looking at proposals to get Federal assistance to fund a project to determine future preventive actions needed for wastewater treatment plants. It was reported that there are approximately 200 environmental police officers that protect the watershed. A contract settlement in fiscal year 2013 brought the police officers up-to-date to the other City unions with contracts that are current through 2009. The settlement eliminates a liability that had been carried on the books for unsettled labor grievances.

There being no further questions on the financial statements, Chair Rosen proceeded to NYW's management letter. NYW management provided clarification on the following issues. The summary report of accounts receivables now is now able to be reconciled to the individual accounts. The billing and collection system will now accurately age accounts receivables in cases when charges have been cancelled and rebilled. The WB will now have the ability to accurately age its accounts receivables. WB had spent approximately \$5 million on a project that IBM did not perform adequately. A settlement was reached with WB on this issue.

It was reported that the percentage used in the calculation of the "annual allowance for cost escalation due to inflation," is generally 3%. It was explained that rental expenses increased \$11.4 million. The rental expense calculation was based on 15% of debt service. The City calculates a fringe benefit rate based on actual fringe costs as a percentage of actual wages and salaries. Regarding the uncollateralized deposits, unlike municipal governments, the MWFA and WB are not required by state law to collateralize their accounts. Reliable banks are selected and money is saved by not having the balances collateralized. Custodial credit risk is minimal because of the nature of the securities and that the securities are recorded in the bank's records as accounts of the MWFA and the WB. The majority of the investments are in U.S. Treasuries or Agency securities. It was explained economic defeasance means the bonds are legally outstanding but there is an escrow set up with treasury agencies. The economic defeasance is related to bonds with New York State Environmental Facilities Corporation from which MWFA received subsidies. If there should be a legal defeasance of those bonds, the subsidy would be lost.

There being no further questions the Chair thanked the representatives of the NYC Water Board and Authority for their participation at today's meeting.

## **2. Hudson Yards**

The next agenda item was the review of the financial statements and management letters for the Hudson Yards Infrastructure Corporation ("HYIC") and the Hudson Yards Development Corporation ("HYDC") for the fiscal year ended June 30, 2013. Mr. Balducci noted that Marks Paneth & Shron LLP was HYIC and HYDC's independent auditor.

Mr. Alan Anders, President at HYIC, reported that HYIC completed all its bond financings. Construction still needs to be completed on the No. 7 Subway and on the park and boulevard part of the

project. Mr. David Farber, Senior Vice President and General Counsel at HYDC, reported that the tunnels for the No. 7 Subway were completed and the remaining structures are almost complete. The ongoing work includes installation of systems, electrical track lighting, communications and architectural work. The No. 7 Subway will go from Times Square to 34th and 11th. The first station will open during the second half of calendar 2014.

Mr. Farber reported that Phase I of the park and boulevard part of the project was deemed essential to the commercial development that drives the debt service and is within HYIC and HYDC's project budget. The boulevard component is more than 90% complete. The park component is about 30% complete. It is contemplated that in 10 to 20 years the station will be the most heavily used station in the entire system, and it is designed for that capacity. Two-thirds of \$153 million/year of interest is budgeted to be paid by the City. Fiscal year 2013 had less interest budgeted to be paid by the City because of the receipt of more positive payments from developers for district improvement bonuses in the amount of \$46 million.

During a question and answer session, it was reported that the City paid over \$2 billion toward the extension of No. 7 Subway. So far the project is largely on schedule and on budget. It was reported that HYIC is entitled to the amount of money that was invested in the transferrable development rights plus the cost of the money, until it is earned back by the sale of those rights. It was reported that HYIC's term bonds are long-term and have a single maturity and several amortizations, whereas the serial bonds mature at regular intervals.

There being no further questions the Chair thanked the representatives of HYIC and HYDC for their participation at today's meeting.

### **3. Transitional Finance Authority**

The next agenda item was the review of the financial statements and management letter for Transitional Finance Authority (“TFA”) for the fiscal year ended June 30, 2013. Mr. Balducci, Deputy Comptroller at TFA, noted that D&T was TFA’s independent auditor.

Mr. Jay Olson, Treasurer of TFA, responded to a question from a Committee member by explaining that the term "parity bond" is synonymous with "subordinate bond," and recovery bonds are a subset of parity debt. Mr. Olson reported that there was about \$5 billion in both issuances and re-issuances for the Future Tax Secured bonds. Building Aid received was around \$965 million, and of that about \$300 was retained for debt service for future years. In response to Committee members’ questions, Mr. Olson reported that the sequestration costs were well under \$10 million of subsidy. The bonds that are subject to the sequestration costs are still extremely cost-effective. Of the entire City financing, 20% is General Obligation and 40% is TFA, which have been used interchangeably to finance the non-water City portion of capital spending.

There being no further questions the Chair thanked the representatives of TFA for their participation at today’s meeting.

### **4. TSASC, Inc., Sales Tax Asset Receivable Corporation and Fiscal Year 2005 Securitization Corporation**

The next agenda item was the review of the financial statements and management letters for TSASC, Inc. (“TSASC”), Sales Tax Asset Receivable Corporation (“STAR”) and the Fiscal Year 2005 Securitization Corporation (“FSC”) for fiscal year 2013. Mr. Balducci, Deputy Comptroller at TSASC, STAR and FSC, noted that Marks Paneth & Shron LLP was TSASC and STAR’s independent auditor, and Bollam, Sheedy, Torani & Co. LLP, was FSC’s independent auditor.



Mr. Anders, Executive Director at TSASC, STAR, and FSC, began his presentation by stating that TSASC, STAR and FSC are non active entities.

Mr. Anders reported that TSASC refinanced in fiscal year 2003. TSASC earned tobacco settlement revenues of \$187 million in fiscal year 2013. After expenses of \$70 million, \$63 million of interest and \$7 million of principal, \$117 million was passed through to the City. Mr Anders stated that the new electric cigarettes are not included in the scope of the master settlement agreement.

Mr. Anders reported that Star implemented a refinancing of the Municipal Acceptance Corporation (“MAC”) debt. The State Legislature agreed that STAR could refinance all of the MAC bonds and save \$500 million a year in budget benefit from the State to the City. The STAR bonds have a 30 year in maturity and are secured by \$170 million of State sales tax paid annually by the New York State Local Government Assistance Corporation (“LGAC”). In response to a Committee member’s question, Mr. Anders clarified that the payments are not a pass-through of City sales tax but an annual payment to the City of State funds through LGAC which will end at some point. The bonds will be extinguished and the LGAC payments will end in 2033.

Mr. Anders reported that FSC was created to restructure a City refunding escrow, which was established to provide for debt service through final maturity. Interest rates had gone down so the value of the escrow increased and it would be financially advantageous for the City to liquidate the escrow and create a new escrow which would provide for debt service until the first call date. IRS rules would not allow liquidation of the escrow. The value was realized by creating a new entity and buying the securities in escrow. The remnant of the old escrow pays the new FSC bonds rather than the old City bonds

## 5. NYCTL Trusts

The next agenda item was the review of the financial statements and management letters for the NYCTL Trusts (“TRUSTS”) for the fiscal year ended June 30, 2013. Mr. Anders, Deputy Director for Finance at OMB, noted that Toski & Co., P.C. was the independent auditor for TRUSTS listed below:

- NYCTL 1998-2 Trust
- NYCTL 2011- A Trust
- NYCTL 2012- A Trust
- NYCTL 2013- A Trust

Mr. Anders stated that Marks, Paneth & Shron, LLP was the outside consultant who compiled the TRUST’s financial statements.

Mr. Anders reported that the TRUSTS are the current enforcement mechanism for property tax and water and sewer fees. The collection rates on property taxes were from 92 to 93%. He noted that the proceeds are about \$100 million every year with about \$600 million of liens. The program is a great vehicle for collection because the property owners are put on notice to pay their taxes or they will be included in the lien sale which will greatly increase the amount due and can ultimately lead to foreclosure proceedings being initiated by the Trust. In response to a Committee member question, Mr. Anders confirmed that the program was for multi-family residential and commercial properties. Interest rates are high as determined by law. The interest rate is a delinquent debt interest rate and is meant to encourage timely payment, which it apparently does.

There being no further questions the Chair thanked the representatives of TSASC, STAR, FSC and the TRUSTS for their participation at today’s meeting.

## **6. Technology Development Corporation**

The next agenda item was the review of the financial statements and management letter of the Technology Development Corporation (“TDC”) for the period January 1, 2013 (inception) through June 30, 2013.

Ms. Eileen Cleary, Acting President at TDC, noted that D&T was TDC’s independent auditor. TDC began operations in January of 2013 to enhance the City’s ability to manage and deploy information technology projects. TDC was created to help with the City large-scale technology projects that often were not completed on time, completed over budget, or were not completed at all. Currently TDC is staffed with nine full-time, highly skilled technology project service management providers. TDC works closely with agencies that are looking to implement software solutions typically in the range of \$25 million or more. TDC is now working on about nine different assignments and some of the larger ones were for work on the City’s website, NYC.gov. TDC is also working on an outdoor Wi-Fi system in Harlem..

It was reported that typically projects are given to TDC or recommended through the Department of Information Technology. TDC is governed by a Board made up of a maximum of seven members, all of whom are appointed by the Mayor; two based upon the recommendation of the Comptroller and one is appointed by recommendation of the Speaker of the Council. Three members have to be non-City, private individuals; four have to be City officials but the City positions they serve in is not predetermined. (i.e., not ex-officio)

There being no further questions the Chair thanked the representatives of the TDC for their participation at today’s meeting.

### **III. Approval of Draft Audit Committee Report**

Chair Rosen commented that the Audit Committee Report is routine and has been prepared based on previous years' reports. He pointed out some minor editorial changes. There was a motion and a second and unanimous approval of the report, as amended

There being no additional business, Chair Rosen adjourned the open portion of today's meeting and the Committee went into Executive Session; from which it adjourned directly.