

Office of Audit and Control

AUDIT REPORT

**Streetlight Purchase &
Serial Bonds CUSIP #012429**

April 2019

**Susan Rizzo
Chief City Auditor**

Audit Team

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A full copy of this report is available for download at our website:

www.albanyny.gov/Government/Departments/OfficeofAuditandControl

You may also contact our office by email at **srizzo@albanyny.gov**

Preface

The Office of Audit and Control (OAC) exists to provide oversight, transparency and public accountability as a means to improve the City of Albany Administration accountability. This audit is a part of that function.

When the OAC takes on an audit subject and, setting aside issues of misconduct, that City department(s) or entities concerned respond positively to address the audit's findings, it is the commitment of the OAC to support and encourage use of the audit process by City departments as a means to improve their operations.

The proper use of the audit findings in these circumstances is to provide for oversight of the resulting changes and as the basis for informed public policy discussions.

It would be unfair and damaging to the audit process for this audit's findings to be used for political gain. As such, the OAC will view the political use of this audit's findings as detrimental to our mission.

We thank the City's employees for their cooperation and commitment.

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Background

This audit was initiated because the OAC has been monitoring the City of Albany's borrowing practices and utility accounts. In its July 2018 Investment Procedural Audit, the OAC evaluated the City's borrowing and investment activities and it determined that the City was often incurring too much debt and borrowing too early for its capital projects. Additionally, the OAC has been aware of the City's ongoing negotiations to purchase streetlights as a result of its continuing efforts managing the City's utility accounts and its June 2018 National Grid Accounts audit.

Introduction

On February 6, 2019, the City issued a press release announcing the issuance of \$26 million of bonds, which occurred at the end of January, in order to finance its purchase of streetlights from National Grid. Later that day, the City Treasurer held a press conference in which he noted that the purchase had not yet closed and was uncertain of the timing. Also, the bid winner for the bonds was KeyBanc Capital Markets, a division of Key Bank, which is also the City's provider of its banking services as discussed in the previous audit.

The OAC decided to investigate the situation because it presented another instance in which the City may have borrowed too early. Also, the City normally borrows once per year but this was an additional borrowing event specifically for the streetlight acquisition. Since the bond winner was a division of Key Bank, the OAC wanted to review bid details. Based on the results of the previous audit, Key Bank has been less than helpful negotiating a market rate for the City's banking services. Key Bank had not increased the earnings credit rate in 2016 or 2017 when treasury rates started going up. It wasn't until after the 2018 audit that Key Bank increased the ECR from 0.20% to 0.90% to offset the City's banking services.

On February 8, 2019, the OAC emailed the Treasurer with an initial information request. On March 8, 2019 certain documents related to the initial request were provided to the OAC. After further review of these documents and others, the OAC initiated an official audit on March 25, 2019.

Following initial inquiries about the \$26 million bond issuance and the review of the status of the acquisition, the OAC learned that the transaction had been stalled at the regulatory approval step.

Pursuant to *New York Consolidated Laws, Public Service Law - PBS § 70-a*. Street lights, the acquisition of streetlights by a municipality requires the approval of its application by the New York Public Service Commission (PSC). The City's Article 70 Petition (Case 18-E-0707) had yet to be approved by the PSC, which could deny the application and terminate the acquisition.

The OAC continues to process the City's utility invoices and it noticed that the City was continuing to incur more than \$233,000 per month in facility fees related to "renting" the streetlights from National Grid. Subsequent to communication from the OAC regarding the ongoing facility fees, the Mayor wrote a letter to the PSC on March 21, 2019 urging it to approve the deal citing that "Each week that passes that our Petition is not approved, the City loses over \$64,000 in potential savings." However, the Mayor failed to note that the City had already borrowed \$26 million in anticipation of closing the acquisition nearly two months prior and has since been incurring approximately \$65,000 per month in interest expense. This interest expense has been partially mitigated by the investment of the funds in Treasury Bills, which was a direct result of the OAC's efforts surrounding the July 2018 Investment Procedural Audit.

The audit findings are as follows:

1. Procedurally, the City borrowed prior to required Board of Estimate and Apportionment approvals of both the bond ordinance and a budget amendment;
2. Bonds were issued for \$26 million prior to the acquisition closing primarily out of concern for rising interest rates first and foremost while the timing of the acquisition closing was a secondary concern; and
3. The special bond issuance cost the City \$48,919.25 since it was done on a standalone basis and not as part of the annual bond issuances for all City capital projects.

Scope, Objectives and Methodology

Scope

The audit covered the time period from the Common Council approval to purchase the streetlights on November 5, 2018 through the approval by the PSC on April 18, 2019.

Objectives

The objectives of this audit were as follows:

1. Determine if all necessary steps and procedures were followed for the bond issuance;
2. Determine why the City borrowed before the acquisition closed; and
3. Determine costs associated with special bond issuance.

Methodology

The overall audit methodology consisted of the following:

- Collecting, reviewing, and analyzing documents related to the streetlight purchase and bond issuance
- Discussing the street light purchase and bond issuance with relevant City employees

Audit Results

Procedural Steps

Although discussed at some length in the City's 2019 budget, the actual purchase of the streetlights from National Grid was not budgeted in the 2019 Capital Plan or Five Year Capital Plan. However, \$525,000 in utility savings was budgeted, while the actual capital project to upgrade the streetlights was not budgeted. This will necessitate a budget amendment, which will require approval by the Board of Estimate and Apportionment.

On November 5, 2018 the Common Council approved Resolution Number 72.92.18R, which authorized the execution and delivery of the Purchase and Sale Agreement with National Grid for the purchase of streetlights and the consummation of the transaction for a total purchase price of approximately \$9.5 million. This resolution was required prior to the PSC approving the sale.

On December 3, 2018 the Common Council approved Ordinance Number 40.111.18, which authorized the Treasurer to borrow up to \$29.3 million in bonds for up to a 15 year term. Section 12 of the ordinance states: "This ordinance shall be dated November 5, 2018 and shall take effect upon its approval by the Board of Estimate and Apportionment of the City of Albany." However, Ordinance Number 40.111.18 has not yet been submitted for approval to the Board of Estimate and Apportionment.

The OAC has determined that the City borrowed for this capital project prior to Ordinance Number 40.111.18 was submitted to or approved by the Board of Estimate and Apportionment. Also, the City borrowed \$26 million for a capital project that was included in neither the 2019 Capital Plan nor the Five Year Capital Plan.

Bond Issuance Timing

At the end of 2018, there was a fluid dialogue between the Common Council and the Treasurer regarding the possibility of rising interest rates. The OAC also agreed that interest rates would continue to rise. On December 20, 2018, the Federal Open Market Committee (FOMC) increased the target federal funds rate range by 25 basis points (BPS) to 2.25%-2.50%. This represented the fourth rate increase in 2018 and the Treasurer indicated that there was a remote possibility that rates would increase again in the first quarter of 2019.

The Treasurer initiated the bond issuance process towards the end of the 2018 calendar year. On January 31, 2019, within approximately one month, the process was complete and the serial bond proceeds were delivered to the City of Albany. After the bonds were issued, there were still several steps remaining necessary for the acquisition to close before the City could begin upgrading the streetlights, including approval by the PSC and National Grid Board of Directors.

Bond Issuance Costs

In addition to interest expense that continues to accrue at a rate of \$65,000 per month, the special bond issuance cost the City \$48,919.25. These costs include expenses that are standard for each and every bonding process the City undertakes. The expenses related to the streetlight bonds are itemized below.

Vendor	Expense Type	Amount
Standard & Poor's Financial Services	Credit Rating Agency	\$ 22,800.00
Fiscal Advisors & Marketing	Financial Advisor	19,500.00
Roemer Wallens Gold & Mineaux	Legal Counsel	6,500.00
Albany Times Union	Bond Notice of Sale	<u>119.25</u>
Total direct streetlight bond expenses		\$ 48,919.25

Recommendations

1. The OAC recommends proper documentation is submitted to the Board of Estimate and Apportionment so that it can retroactively approve the bond ordinance and budget amendment.
2. The OAC recommends the City work in an expeditious manner to quickly close the acquisition of the streetlights, both to put the borrowed funds to work and to make it possible for the upgrade project to begin so the City can realize projected savings.
3. The OAC recommends, as it did in its July 2018 audit, that the City continue to review the timing of its borrowing relative to the timing in which the funds are required for capital projects. In this specific instance, the City should have ensured all necessary approvals were granted and procedures followed before borrowing occurred.

Conclusion

The purchase of the streetlights from National Grid has been an ongoing project and was recommended as a cost savings measure in New York State's PFM report. However, some procedural steps internal to the City of Albany were skipped and in the process \$26 million in bonds were issued for a transaction that has yet to close. The special bond issuance cost the City nearly \$50,000 and it is incurring approximately \$65,000 per month in interest expense during 2019. As a direct result of the efforts of the OAC and its July 2018 Investment Procedural Audit, this interest expense has been partially offset by investing the idle funds in treasury bills.

Appendix I

Budget Office Response



**CITY OF ALBANY
DEPARTMENT OF ADMINISTRATIVE SERVICES
BUDGET OFFICE**
24 EAGLE STREET
ALBANY, NY 12207
TELEPHONE (518) 434-5078

MEMORANDUM

TO: Susan Rizzo, Chief City Auditor
FROM: Michael Wheeler, Budget Director
DATE: May 22, 2019
RE: Streetlight Purchase Audit Response

The City of Albany's Budget Office has received and reviewed the Streetlight Purchase Audit.

Public Service Commission Rate Case & Streetlight Purchase

On November 20, 2015, Governor Andrew Cuomo signed into law the Streetlight Replacement and Savings Act, setting forth a process meant to empower municipalities to acquire ownership of its streetlights and upgrade them with energy-efficient and cost-saving LED lighting technology. Even though this created a process, the cost of acquisition would be determined by National Grid, who stood to lose a source of revenue.

In 2017, the City of Albany, through the New York Power Authority (NYPA), requested a purchase price on all National Grid streetlighting within the City. At that time, there was no methodology for determining the sale price of such an asset. Because National Grid was also negotiating and/or providing pricing to other cities such as Syracuse and Buffalo, and because they did not want the municipalities seeking pricing to communicate with one-another, National Grid required the City to sign a Non-Disclosure Agreement.

On August 4, 2017, National Grid provided the City with a Street Light Acquisition Pricing Proposal. In that proposal, they provided an original cost of equipment of \$14,743,364 and a Net Book Value (NBV) of \$9,180,625 (the original cost minus depreciation).

At this point, the City had four options:

1. Continue with National Grid, under the current agreement, forgoing any potential savings or LED conversion;
2. Move forward with the buyback, under unfavorable conditions, and have an extended payback or break-even timeframe;
3. Seek a legislative fix, which could take years; or

4. Become parties to the rate case – making the case for a fair pricing methodology to the PSC.

The City chose to become parties to the rate case, teaming up with Syracuse and Buffalo. During this period, the City and its NYPA representative attended countless hours of PSC/National Grid meetings. As a result, we successfully argued the most fair and equitable way for the municipalities to buy their streetlights without making other ratepayer classes subsidize the sale.

During the rate case, we successfully argued the City should still be able to purchase the streetlights at the NBV that was already provided, if the new methodology resulted in a higher NBV. When National Grid submitted their petition to the PSC on November 13, 2018, the NBV cited was \$9,611,237, an amount that was \$430,612 more than the previous NBV. **Because of our diligence, we saved the City \$430,612.**

Each of these steps were taken within extremely tight timelines. In order to purchase the streetlights under the NBV issued August 4, 2017, we were required to enter into a binding purchase agreement by September 1, 2018, leaving little time between the pricing received on June 26, 2018 and that dealing. As noted in the New York State Public Service Commission Joint Proposal—Case 17-E-0238, Section 9.3.2(b), NBV Sale Price:

Notwithstanding the foregoing, for any municipal customer with more than 10,000 luminaires listed in the Company's billing inventory files in the respective municipal tax district as of December 1, 2017, that enters into a binding purchase agreement on or before September 1, 2018 to acquire all of the street light assets serving it within the municipality's taxing jurisdiction, and that received a street light acquisition pricing proposal letter dated between June 1, 2017 and December 1, 2017 from the Company, the NBV sale price will be the NBV indicated in said letter.

Ultimately, the City of Albany signed the Joint Proposal to the above rate case, along with the cities of Syracuse and Buffalo, National Grid, and the Public Service Commission. Because of this agreement, there was no logical reason to conclude this purchase would not be approved under a Section 70 filing, since the regulators had been intimately involved and ultimately signers to the Joint Proposal. The Public Service Commission approved the sale of the streetlights on April 18, 2019.

The City of Albany had no control over the length of time for this process. In our presentations to the Common Council, it was clear that predictability in our forecasts was paramount. If the City chose NYPA's variable rate financing, we could not provide the level of certainty that the Common Council was requesting. In addition, it was unclear how long the Section 70 procedures would take or when the closing would be scheduled – even though the City was required to have the requisite funds on-hand at the time of closing.

Timing of the Bond

When NYPA engages with a municipality, they also offer financing to help complete the purchase of streetlights. At the time financing was being considered, NYPA's **variable** interest rate was estimated to rise to 2.93%, however the bond markets provided for bonding at a **fixed** 2.83% interest rate.

Rising interest rates have long been on the radar of municipalities within the State of New York. Since the Great Recession of the late 2000's, interest rates on Treasury Bills have been at historic lows. Due to Section 11 of the NYSGML, municipalities are only allowed to invest in extremely low-risk securities that are all strongly correlated to rates established by the Federal Reserve.

With the economy recovering well over the past decade, T-Bill interest rates entered an expansionary phase of their economic cycle.

The City of Albany recognized this upward trend early in 2018 and was able to produce significant revenues through temporary investments, generating \$353,485.33 over the course of last year, far exceeding the budgeted amount of \$30,000. Much of this success is due to the Treasurer's Office investing in short-term, 7-day Treasury Bills purchased from the secondary market. With rising interest rates, a short-term bill allows for the principal to mature faster and be re-invested into a new security with a higher interest rate. It also allows for increased liquidity to be able to handle any variance in cash flow.

As rising interest rates pose a great opportunity for our cash-on-hand investment strategies, they pose an equal-if-not-greater threat to our borrowing strategies. An increase in interest rates of just 1% (100 basis points) would cost the City an additional \$3.9 million over the life of the bond. In 2018, interest rates on 10-year Treasury bonds had a range of 82 basis points between their highest and lowest rates.¹ As the financing for the streetlights was discussed before the Common Council in 2018, the City Treasurer, Budget Director, and Chief City Auditor all acknowledged the likelihood of interest rates continuing to rise during the upcoming year.

A significant benefit (referenced, but not quantified in the audit) to bonding early is the value of temporarily investing the bonded funds prior to the purchase of the asset as referenced previously. The interest rate on our 15-year bond for the streetlights is 2.83%. Our current rate of return on temporary investments is approximately 2.35%.² From the time the bond was finalized (January 31, 2019) until the first payment date, the City of Albany is accruing interest at a net rate of 0.48% instead of 2.83% due to the temporary investment of funds in Treasury Bills. **The “net-interest” projects to save the City \$50,916.67 per month until the first payment of \$9.35 million is made.**

As we wait for the remainder of the bonded amount to be paid, the City is projected to save \$33,291.65 per month. The savings is calculated with the assumption that if we waited until just before the scheduled purchase date of the streetlights to bond, we would accumulate interest at a net rate of 2.83% for the duration of the entire 15-year bond as opposed to paying just 0.48% over the period in which we wait to make our initial payment.

¹ https://ycharts.com/indicators/10_year_treasury_rate

² <https://fred.stlouisfed.org/series/DGS1MO>

Financial Analysis of Streetlight Audit

<u>Assumptions:</u>		<u>Est. Payment Date</u>
Total Bonded Amount	\$ 26,000,000.00	
Initial Payment	\$ 9,359,817.00	5/17/2019
Final Payment	\$ 16,640,183.00	*est. 1 year from purchase date
Issuance Costs	\$ 48,919.25	
Interest Rate of Bond	2.83%	
7-Day Treasury Yield	2.35%	
Bond Start Date	1/31/2019	
1st Payment Calculations:		
# of weeks between receipt of funds and first payment: 15 Weeks		
Interest payment accrued	\$ 212,250.00	
Yield on investment of 1st payment	\$ 63,448.76	
Yield on investment of 2nd payment	\$ 112,801.24	
Total yield on temporary investments	\$ 176,250.00	
Net interest accrued	\$ 36,000.00	
<i>Net interest as an interest rate on total principal</i>	<i>0.48%</i>	
2nd Payment Calculations:		
# of weeks between 1st payment and second payment		1 Year
Interest payment accrued	\$ 735,800.00	
Yield on investment of 2nd payment	\$ 391,044.30	
Total yield on temporary investments	\$ 391,044.30	
Net interest accrued	\$ 344,755.70	
<i>Net interest as an interest rate on total principal</i>	<i>1.33%</i>	
Total Summary:		
Total Interest Accrued	\$ 948,050.00	
Total Yield on Investment (What we are saving by bonding early)	\$ 567,294.30	
Special Bond Issuance Costs	\$ 48,919.25	
Actual Cost to the City of Albany	\$ 429,674.95	

Board of Estimate & Apportionment

In December 2018, the Common Council passed an ordinance authorizing the City Treasurer to borrow up to \$29.3 million for up to a 15-year term. The ordinance stated the authorization shall take effect upon its approval by the Board of Estimate & Apportionment. On May 7, 2019, the Board of Estimate and Apportionment unanimously approved an updated capital plan and schedule of principal of interest payments as part of the 2019 budget. As it relates to this audit, this finding has already been rectified. The Board of Estimate & Apportionment's approval did not take place immediately after the Common Council's approval due to a failure of the Office of Audit and Control to include it on the Board of Estimate & Apportionment's agenda as it has done in the past. Approval by the Board is also non-material to the issuance of debt by the City Treasurer.

Professional Conduct

The Chief City Auditor is currently running against the City Treasurer for an elected position and therefore the appropriateness of this audit should be examined in that context.

The preface of all audits published by the Office of Audit and Control state “[p]oliticized use of this audit's findings is unfair and damaging to the OAC process and will be viewed as detrimental to our mission.” After reviewing the last several audits conducted by the Office of Audit and Control, one may reasonably conclude that said examinations were an attempt to criticize the Office of the Treasurer through the inspection of collateral functions while veiled under a cloak of impartiality.

This audit demonstrates the Office of Audit and Control has a sincere lack of understanding regarding the City of Albany's streetlight purchase process as well as basic municipal bonding and investment principles. The Budget Office would like to remind the Office of Audit and Control that formal training and credentialing, such as the Certified Government Auditing Professional (CGAP) and IIA's Certified Internal Auditor certifications, is encouraged, and we stand by our commitment to fund formal auditing education, training, and credentialing.

The Budget Office also reminds the Chief City Auditor and Office of Audit and Control of their responsibilities under the United States Government Accountability Office's & Comptroller General of the United States' “Government Auditing Standards – 2018 Revision.”³

Standard 3.11 of the *Government Auditing Standards* expressly states “[a]uditors' objectivity in discharging their professional responsibilities is the basis for the credibility of auditing in the government sector” and includes “being free of conflicts of interest.” (emphasis added)

As per Standard 3.42, “[e]xamples of circumstances that create undue influence threats for an auditor or audit organization include existence of...external interference with the selection or application of engagement procedures or in the selection of transactions to be examined....”

Standard 3.47 states “[a] threat to independence is not at an acceptable level if it either (a) could affect the auditors' ability to conduct an engagement without being affected by influences that compromise professional judgment or (b) could expose the auditors or audit organization to circumstances that would cause a reasonable and informed third party to conclude that the

³ <https://www.gao.gov/assets/700/693136.pdf>

integrity, objectivity, or professional skepticism of the audit organization, or an auditor, had been compromised.”

One of the safeguards designed to prevent deviations from these standards is detailed in Standard 3.50 of the *Government Auditing Standards*. This includes “removing an auditor from an engagement team when that auditor’s financial or other interests or relationships pose a threat to independence.” (emphasis added)

Standard 3.59 states “[a]uditors should conclude that independence is impaired if no safeguards have been effectively applied to eliminate an unacceptable threat or reduce it to an acceptable level.”

As per Standard 3.60, “[w]hen auditors conclude that independence of the engagement team or the audit organization is impaired under paragraph 3.59, auditors should decline to accept an engagement or should terminate an engagement in progress....”

The Chief City Auditor’s direct questioning of the City Treasurer’s judgment at this time and the lack of safeguard implementation is a clear deviation from the above-referenced professional governmental auditing standards.

Conclusion

The City has worked on incredibly tight deadlines, and at each stage of this project has made extremely prudent financial decisions that saved the City of Albany more than \$400,000. We also reinvested the bonded funds, lowering the short-term cost of borrowing to the City from 2.83% to 0.48% as the final PSC approval took place.

It was undoubtedly in the City’s best interest to bond well before June 2019. By waiting to bond until the sale was officially approved, and a closing date was provided, it would have financially irresponsible and injurious to our residents and taxpayers due to the uncertainty surrounding the bond markets and the lack of investment potential.

Throughout this process, the City has worked closely with our partners at NYPA as well as our consulting engineers and contractors to ensure that we have the most up to date information, the best design, the materials ready for order, and a complete work plan to ensure that as soon as the City of Albany owns the street lighting system, we can begin work. This work will improve the light quality, safety, and aesthetics throughout the City, while continuing to save our taxpayers millions of dollars every year.

Auditor's Response

Auditor's Response

The OAC would like to thank the Budget Director for his review of and response to the Street Light Bond Audit. After reviewing this response, the OAC would like to take the opportunity to address specific items discussed in the response and other issues that have come to the OAC's attention since the draft audit was shared with the Treasurer and Budget Director.

Before discussing the substance of the OAC's response, it is necessary to first address accusations by the Budget Director and the Mayor that the OAC has been inappropriately auditing the functions of the Treasurer's Office because of a campaign between the Treasurer and the Chief City Auditor for Albany County Comptroller. The Mayor posted the Budget Director's response, with her own conclusory commentary, to the official Facebook page for the Mayor of the City of Albany. This "extraordinary step" was taken by the Mayor in coordination with the delivery of the Budget Director's emailed response to the OAC at the end of business on May 22, 2019 one day prior to a candidate forum/debate between the Treasurer and Chief City Auditor. The timing of the Mayor's public disclosure of an audit response by the Administration is in itself ethically suspect. The draft audit had not been finalized or disclosed to the public by the OAC.

The Budget Director and the Mayor somehow believe that the Treasurer's Office is a victim of audits of its "collateral functions" by the OAC. In fact, the exact opposite is true. The Street Light Bond audit is a natural follow-up to the previous audit of the National Grid accounts and the City's borrowing procedures because it is a combination of these two previously examined issues. Only two out of six completed audits in 2018 related to the Treasurer's Office and addressed three of its primary functions. The Accounts Receivable audit was an audit of the Treasurer's primary function of collecting the City's revenues in a timely manner and maintaining accurate financials. The Investment Procedural audit was an audit of two of the Treasurer's most important functions as the City's Chief Fiscal Officer: borrowing money on behalf of the City and managing the City's cash. As a direct result of the Investment Procedural audit, the City earned nearly \$623,000 more interest income in 2018 than in 2017 on its combined debt reserve and general fund cash balances. The OAC would like to emphasize the Investment Procedural audit was initiated in part due to the concern of the Budget Director's staff, which brought the issue of insufficient interest income to the OAC's attention and the inability to convince the Treasurer to invest in higher yielding treasury bills. The importance of \$623,000 to a financially stressed city such as Albany is clear. Indeed, the Treasurer and Administration's responses to these previous two

audits were not taken as an attempt to “criticize” the Treasurer. Rather, they generally accepted the OAC’s findings and agreed to do better. The OAC recognizes that there are pros and cons to procedural audits and financial audits. The OAC has recently focused on audits that have a direct financial impact because the prior Chief City Auditor performed mostly procedural audits.

This audit and auditor’s response were delegated to be performed and written by the Deputy Chief City Auditor. The Deputy Chief City Auditor in turn, aware of the political sensitivity of the situation, deliberately omitted several observations and inferences from the draft audit, which could have been construed as political in nature. However, in light of the coordinated effort to impugn the integrity of the OAC, it is necessary to disclose aforementioned concerns.

The Deputy’s observations, which heretofore had not been included in this audit, are the following:

- 1) It was unusual to hold a press conference in City Hall announcing the completion of the bond issuance. The Deputy did not recall a press conference occurring in June or July 2018, which was the last time the City completed a bond offering, and is unaware of press conferences related to any other previous bond issuance.
- 2) At the press conference, the Deputy Chief City Auditor noticed and stood next to the Mayor’s Deputy Chief of Staff, who was taking pictures of the Treasurer during the press conference. Later, the Deputy Chief City Auditor noticed that these pictures had been used on the Treasurer’s campaign Facebook page linking to the Treasurer’s main campaign website. On the main campaign website, the official City press release was reprinted verbatim.
- 3) The Administration has never publicly issued a response to an audit in advance of the publication of a completed audit report.

These observations led the Deputy Chief City Auditor to conclude either:

- a) The Treasurer was taking advantage of the bond issuance to polish his financial bona fides for the County Comptroller election by using City resources in coordination with the Mayor’s Office; or
- b) The timing of the borrowing was deliberately separate from the annual bonding in an attempt to polish the Treasurer’s financial bona fides before the Democratic

primary on June 25th. In prior years, the annual bonding occurred at the end of June or beginning of July, which would have occurred after the primary vote.

Initially, the Deputy Chief City Auditor was inclined to believe that it was the former; however, one may reasonably conclude that the Budget Director and Mayor's coordinated effort was an overt act in furtherance of the latter.

- 4) It was incredibly difficult to obtain documents related to the street light bonds for this audit. In some instances, the OAC requested the same document multiple times in writing from the Treasurer's Office. Prior to initiating an official audit, a document request was submitted to the Treasurer by the Deputy Chief City Auditor as part of a pre-audit inquiry. Multiple documents were requested, including invoices related to the bond issuance. One month after the initial request for documentation at the deadline, the Treasurer sent only two documents: a calendar of steps necessary to complete the bond offering (created by Fiscal Advisors) and the serial bonds' Final Official Statement, which was already publicly available from the MSRB (Municipal Securities Rulemaking Board) website. It was only after this insufficient response that the OAC initiated its formal audit.

In the interim period after the draft audit was submitted to the Treasurer and Budget Director, among others, the OAC received and processed an additional invoice related to the issuance of the street light bonds. Premier Printing provided printing and electronic distribution services related to the bond offering for \$3,100. This additional invoice resulted in total expenses of \$52,019.25 related to the bonds. The invoice, dated January 31, 2019, was withheld from the document request but was discovered on May 14, 2019 when it was submitted to the OAC to be processed for payment.

In his response, the Budget Director notes that National Grid cited a NBV that was \$430,612 higher than the previous agreed-upon NBV and likened this twice to saving the City of Albany over \$400,000. In actuality, this did not save the City any money but prevented the City from being overcharged, intentionally or not, by National Grid. Double checking the purchase price for an asset acquisition is the most basic function of legal and financial professionals working on the transaction.

The Budget Director does correctly note that the City was "required to have the requisite funds on-hand at the time of closing." However, only \$9.5 million was required to complete the acquisition from National Grid. The remaining funds will be spent over the course of the refurbishment of the street lights. As noted by the Budget Director in a meeting with the OAC, the City could have utilized \$9.5 million from the General Fund to complete the acquisition and replenish it after completing a bond

offering. This strategy is regularly employed by the City for other capital expenditures but was not for the street light purchase.

The OAC appreciates the Budget Director's attempt to quantify the effect of investing the proceeds of the \$26 million bond offering in his response. The draft audit did refer to the offset provided by investing the idle funds in treasury bills; however, the OAC was unable to quantify the actual amount due to the resistance it received from the Treasurer's Office throughout the audit. Also, it is important to point out the following inaccuracies and differences between the Budget Director's hypothetical analysis and how the process will actually occur.

- 1) Per the executed purchase and sale agreement, the purchase price for the street lights is \$9,450,674.81, including transition and transaction costs. The OAC is unaware of any change that would result in the \$9,359,817.00 figure utilized in the Budget Director's analysis.
- 2) The total proceeds of the bond offering is actually \$26,376,109.44 including a premium of \$376,109.44. The premium paid by Key Banc Capital Markets is the reason the net interest rate is 2.83% rather than the 3.00% at which the interest expense accrues. This additional \$376,109.44 improves the analysis if the premium was also invested in treasury bills.
- 3) Issuance costs now total \$52,019.25, an increase of \$3,100 from printing expenses that were omitted from the documents provided to the OAC.
- 4) The estimated payment date of May 17, 2019 in the Budget Director's analysis has passed. The OAC is aware that the acquisition was completed on June 21, 2019. In total, the acquisition occurred 142 days after the funds were borrowed and the City accrued \$307,666.67 in interest over this period on the \$26 million serial bonds.
- 5) The "final payment" of the remainder of the borrowed funds, assuming the total project costs exactly \$26 million, will not occur one year from the purchase date. In actuality, the contractor that is performing the upgrades to the street lights will be paid in multiple progress payments as the work is completed. This is standard for all of the City's large capital infrastructure projects. The vendor will not accept payment terms as stipulated in the Budget Director's analysis.

- 6) Most importantly, all of the funds from the bond issuance are not invested in U.S. treasury bills. The OAC is aware that approximately \$9 million has been diverted to lower yielding money market investments in preparation for the acquisition closing. However, these funds have been earning less than half of the interest that is paid on the treasury bills for approximately two months despite communication from the OAC of this fact. This is indeed an actual instance of actions that are "financially irresponsible and injurious to our residents and taxpayers" as stated in the Budget Director's response.
- 7) An issue that was not addressed in the Budget Director's analysis is the source of the funds from which the bond will be repaid. The monies necessary to repay the bond principal and interest will be generated by savings from eliminated monthly facility fee payments to National Grid and lower electricity costs from increased energy efficiency. Neither of these financing sources has been generating the cash flow necessary to repay the debt during the approximately five months before the target closing date.

A principal theme of the Budget Director's response and the Treasurer's rationale for borrowing was the concern of rising interest rates. As part of the analysis, the Budget Director makes the claim that "[a]n increase in interest rates of just 1% (100 basis points) would cost the City an additional \$3.9 million over the life of the bond." This claim is inaccurate and reflects either the Budget Director's sincere lack of understanding of basic municipal bonding principles or a deliberate attempt to mislead readers that are financially unsophisticated. This \$3.9 million figure is derived by calculating 1% interest on \$26 million of debt for 15 years. In actuality, the City's serial bond has an amortization schedule that pays principal every year. An increase of 1% in the interest rate only results in an additional \$2.3 million over the course of a 15 year serial bond with the established amortization schedule. Please see the below analysis for the accurate calculations. The Budget Director's calculation assumes an interest only loan, which is not how municipal serial bonds work.

Also, interest rates have not jumped by 100 BPs in recent history. In 2018, the federal funds rate increased by 100 BPs incrementally over the course of the entire year, which was the total of four separate increases of 25 BPs each. Choosing 1% as a hypothetical is an alarmist attempt to justify early borrowing as is the erroneous calculation of incremental interest using a method that does not accurately reflect the actual repayment of the serial bonds.

Year	Maturity	Bond Years	Calendar Year	KeyBanc Capital Markets		3.25% Interest Rate		4.00% Interest Rate	
				3.00%	28,893.75	3.250%	31,301.56	4.000%	38,525.00
0.958333333	1,005,000	963,125.00	2020	3.00%	28,893.75	3.250%	31,301.56	4.000%	38,525.00
1.958333333	1,435,000	2,810,208.33	2021	3.00%	84,306.25	3.250%	91,331.77	4.000%	112,408.33
2.958333333	1,480,000	4,378,333.33	2022	3.00%	131,350.00	3.250%	142,295.83	4.000%	175,133.33
3.958333333	1,530,000	6,056,250.00	2023	3.00%	181,687.50	3.250%	196,828.12	4.000%	242,250.00
4.958333333	1,580,000	7,834,166.67	2024	3.00%	235,025.00	3.250%	254,610.42	4.000%	313,366.67
5.958333333	1,630,000	9,712,083.33	2025	3.00%	291,362.50	3.250%	315,642.71	4.000%	388,483.33
6.958333333	1,685,000	11,724,791.67	2026	3.00%	351,743.75	3.250%	381,055.73	4.000%	468,991.67
7.958333333	1,740,000	13,847,500.00	2027	3.00%	415,425.00	3.250%	450,043.75	4.000%	553,900.00
8.958333333	1,800,000	16,125,000.00	2028	3.00%	483,750.00	3.250%	524,062.50	4.000%	645,000.00
9.958333333	1,860,000	18,522,500.00	2029	3.00%	555,675.00	3.250%	601,981.25	4.000%	740,900.00
10.958333333	1,920,000	21,040,000.00	2030	3.00%	631,200.00	3.250%	683,800.00	4.000%	841,600.00
11.958333333	1,985,000	23,737,291.67	2031	3.00%	712,118.75	3.250%	771,461.98	4.000%	949,491.67
12.958333333	2,050,000	26,564,583.33	2032	3.00%	796,937.50	3.250%	863,348.96	4.000%	1,062,583.33
13.958333333	2,115,000	29,521,875.00	2033	3.00%	885,656.25	3.250%	959,460.94	4.000%	1,180,875.00
14.958333333	2,185,000	32,683,958.33	2034	3.00%	980,518.75	3.250%	1,062,228.65	4.000%	1,307,358.33
Totals	\$ 26,000,000	\$ 225,521,666.66			\$ 6,765,650.00		\$ 7,329,454.17		\$ 9,020,866.67

360 days interest calculation

345 days for first year

$345/360 = 0.958333333$

Gross Interest Calculation

3.00% Rate (Actual) 6,765,650.00

3.25% Rate 7,329,454.17

4.00% Rate 9,020,866.67

Incremental Interest

25 BPs 563,804.17

100 BPs 2,255,216.67

The Treasurer's Office is currently going through its annual borrowing process for the 2019 capital projects. While potentially rising interest rates were of utmost concern that necessitated the standalone street light bond, the Treasurer appears not to be concerned about this any longer. All of the borrowing for the 2019 capital projects is being done in short term bond anticipation notes (BANs) that have a one year maturity. These BANs will not be able to be refinanced into long term bonds until the next borrowing cycle, which poses a 12 month period in which the City risks rising interest rates, as opposed to the five months between the street light bonds issued on January 31st and the standard borrowing cycle at the end of June.

Finally, the Budget Director addresses the lack of approval by the Board of Estimate and Apportionment (E&A), which has since been rectified by a retroactive approval at a meeting on May 7, 2019. Additionally, he places the blame for non-approval prior to borrowing on the OAC for not including it on the agenda after the bond ordinance was approved by Common Council. **Ultimately, it is the Treasurer's responsibility to ensure that he is in compliance with Common Council ordinances prior to borrowing money on behalf of the City, not the OAC.** The agenda for E&A is aggregated and composed by the OAC; however, the OAC is not the only department responsible for

adding items to the agenda. All departments are able to submit items for inclusion on the agenda. The board currently consists of five members: Chief City Auditor, Treasurer, Common Council President, Corporation Counsel, and Budget Director (as delegated on behalf of the Mayor's seat). The Common Council President was obviously aware of an ordinance passed by the council that required E&A approval. The Treasurer should have been aware of requirements necessary prior to borrowing. Corporation Counsel has an attorney specifically assigned to the Common Council and its meetings. The Budget Director should have been aware of the requirement as well since his department has been working intently on the street light acquisition. None of these persons or departments requested to add the ordinance to an agenda until the OAC realized the oversight during this audit.

The Budget Director responded that the “[a]pproval by the Board is also non-material to the issuance of debt by the City Treasurer.” On the contrary, it was of the utmost importance in this case. If the ordinance was brought to E&A by the Treasurer in a timely manner, a more in depth conversation regarding interest rates and the timeline of the street light acquisition could have occurred prior to borrowing \$26 million. An audit of the borrowing process and acquisition timing would have been unnecessary.