



Town of Palm Beach, Florida

Internal Audit Report Pooled Cash and Investments

March 2009

Town of Palm Beach, Florida

Internal Audit Report Pooled Cash and Investments

Table of Contents

I. Executive Summary	3
II. Results and Recommendations	5
Finding #1: Title – Bond Funds Investments	
III. Summary of Scope	6

I. Executive Summary

Crowe Horwath LLP (Crowe) performed a Pooled Cash and Investments analysis as part of the internal audit plan for the Town of Palm Beach (Town) as of March 2009.

BACKGROUND

The Town of Palm Beach primarily uses third party managers to invest surplus funds. Investment decisions are made based on direction from an independent Investment Advisory Committee which has assisted the Town in the selection of money managers and consultants. The Investment Advisory Committee was established by Town Ordinance and has adopted investment policies within the parameters of Florida Revised Statutes Section 218.415.

The scope of our analysis was the investment process for pooled cash and investments, excluding the investment of pension funds and other post employment benefits (OPEB) funds.

The Town pools all funds' cash for ease of investment. Through an agreement with Wachovia Bank, the Town deposits and expends funds through a primary account. Through a monthly account analysis, interest is paid on this account and deposited in the General Fund of the Town.

Excess cash is invested in a money market fund with interest allocated among all funds based on the pooled cash balance of each fund. Funds with negative pooled cash balances receive a negative allocation of interest effectively charging such funds for the use of pooled cash.

Funds with significant balances are invested in a pooled investment with earnings credited to those funds monthly based on the investment balance of each applicable fund.

In prior years, the Town invested a portion of its funds in the Florida State Board of Administration (SBA) Local Government Investment Pool and a portion in two funds managed by the Florida League of Cities Municipal Investment Trust (FMIvT). The Town withdrew all of its funds from the SBA Pool due to the issues surrounding the pool's investments and placed the funds in a money market account.

In 2009, the Town issued a request for proposals for investment advisors and as a result of the process selected PFM Asset Management LLC as the advisor for the Town. The Town also entered into an arrangement with TD Bank to act as custodian for the investments.

The Town's short term investments are managed through a money market account and longer term investments are managed in two specific investment portfolios through PFM's active management and the remaining bond funds held by FMIvT.

In 2010, the Town issued two bond issues for \$57.035 million and \$14.77 million respectively. The \$57.035 million bond issue was used to advance refund a prior bond issue by placing funds in escrow with a trustee and to provide a project fund for new construction (Town Capital Improvement Program). The \$14.77 million bond issue was used to currently refund a note and provide a project fund for new construction (Worth Avenue Commercial District Project). The advance refunding escrow was invested in US Treasury – State and Local Government Series (SLGS) investments which is typical practice for advance refunding transactions. SLGS are a special series of US Treasury Securities available to units of government to manage earnings restrictions on certain funds.

The remaining bond issue funds were invested based on a laddered investment recommendation received from PFM based on an anticipated draw schedule for the projects.

OVERVIEW

The overall objective was to review the controls over Pooled Cash and Investments as well as determine whether the Town's Pooled Cash and Investments policy conforms to Florida statutory provisions. We reviewed selected policies and procedures, discussed compliance with these policies and procedures with the Town's personnel, and tested certain detail records.

The Town Council approved our work plan, based on the annual internal audit risk assessment, and we communicated the work we did and our results to management.

REPORTING METHODOLOGY

In this report, we provide a summary of our results and recommendations as well as management's responses. To assist you in analyzing our recommendations, we have provided our suggestions for corrective action based on the finding's exposure to loss or increased regulatory scrutiny, as follows:

High – Requires *immediate* remedy and, if left uncorrected, exposes the Town to significant or immediate risk of loss, asset misappropriation, data compromise or interruption, fines and penalties, or increased regulatory scrutiny.

Moderate – Requires *timely* remedy and, if left uncorrected, may expose the Town to risk of loss or misappropriation of assets, compromise of data, fines and penalties, or increased regulatory scrutiny. These issues should be resolved in a timely manner, but after any high priority issues.

Low – Should be addressed as time and resources permit. While it is not considered to represent significant or immediate risk, repeated oversights without corrective action or compensating controls could lead to increased exposure or scrutiny.

Best Practice – Represents operational efficiencies or improvements for consideration by management based on industry best practices and Crowe's experiences.

SUMMARY OF RESULTS

No critical issues were identified during this assessment. Detailed observations and recommendations are provided in Section II – Results and Recommendations. These items are issues that do not represent a significant risk at this time, but offer opportunities for the Town to further strengthen controls and processes.

Thank you for this opportunity to report the results of our procedures. We also wish to thank the Town's finance personnel for their cooperation and assistance.

II. Results and Recommendations

Finding #1: *Bond Funds Investments*
Risk Rating: *Best Practice*

During 2010, the Town issued two tax exempt bond issues. One bond issue provided funds for the advance refunding of an older series of bonds and provided new money for construction (Town Capital Improvement Program). The other bond issue provided funds for the current refunding of an outstanding note and provided new money for construction (Worth Avenue Commercial District Project). The Finance Director and Assistant Finance Director demonstrated a good understanding of the investment restrictions and arbitrage rebate tracking issues related to their investment of tax exempt bond proceeds and understand the three year temporary period available for unrestricted investment of the project funds of the two bond issues. Federal tax law imposes severe restrictions on the investment of these funds beyond the three year temporary period.

As a part of the bond transactions, the Town adopted Reimbursement Resolutions which allow, but do not require, the Town to reimburse itself from bond proceeds for eligible disbursements made prior to the issuance of the bonds. The Town did reimburse itself for disbursements related to one project, but did not reimburse itself for other eligible project costs.

Recommendation

We recommend that as a part of its normal tracking of the disbursement of bond funds that the Town monitor its unspent balance as it nears the third anniversary of bond issuance, and, if there are unspent proceeds, consider exercising its ability to reimburse Town funds for any eligible disbursements that occurred prior to the issuance of the bonds under its Reimbursement Resolutions. Taking such action will reduce or eliminate that amount of remaining proceeds that could be subject to yield restriction prior to the end of the three year temporary period.

Management's Action Plan

It has been past practice with bond proceeds from prior bond issues to monitor expenditures and unspent balances to avoid any arbitrage rebate issues. We will continue this practice for the 2010 Bond proceeds.

Individual(s) Responsible: Jane Struder, Finance Director

III. Summary of Scope

The scope of procedures included inquiry and/or testing in the following activities and processes:

Pooled Cash and Investments

The specific procedures performed were based on the concepts of selective testing and included:

- Walkthrough of internal controls over pooled cash and investments
- Review of policies and procedures and the minutes of the Investment Advisory Committee
- Interviews with responsible individuals
- Analysis of policies, minutes and activities to Town Ordinance and Florida statutory requirements regarding pooled cash and investments
- Review of investment activity for conformance to policies
- Analyze the method of allocation and accounting entries for investment income and fair market value reporting

Although our testing was performed in some areas without exception, we can provide no assurance that exceptions would not have been detected had procedures been changed or expanded.

It should also be recognized that internal controls are designed to provide reasonable, but not absolute, assurance that errors and irregularities will not occur, and that procedures are performed in accordance with management's intentions. There are inherent limitations that should be recognized in considering the potential effectiveness of any system of internal controls. In the performance of most control procedures, errors can result from misunderstanding of instructions, mistakes in judgment, carelessness, or other factors. Internal control procedures can be circumvented intentionally by management with respect to the execution and recording of transactions, or with respect to the estimates and judgments required in the processing of data. Controls may become ineffective due to newly identified business or technology exposures. Further, the projection of any evaluation of internal control to future periods is subject to the risk that the procedures may become inadequate because of changes in conditions, and that the degree of compliance with procedures may deteriorate.