



**CITY OF COLORADO SPRINGS
OFFICE OF THE CITY AUDITOR**

**09-16 – COLORADO SPRINGS UTILITIES
CASH AND DEBT MANAGEMENT**

PUBLIC REPORT

JULY 15, 2009

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City Auditor

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Office of the City Auditor

Date: July 15, 2009

To: Honorable Mayor and Members of City Council

Re: 09-16 – Colorado Springs Utilities Cash and Debt Management

We performed an audit of Colorado Springs Utilities (CSU) Treasury functions for the year ended December 31, 2008. Treasury personnel manage CSU's cash, cash forecasting, debt and investment activities, and provide financial analyses, monitoring and compliance reports.

The purpose of the CSU Cash and Debt Management Audit was to evaluate the adequacy of existing risk management, internal control, and governance processes. We evaluated whether these processes were functioning as intended and enabled the organization's objectives and goals to be met. Our review focused on the internal control environment in which investment and debt transactions occur.

We conclude the overall risk management, internal control, and governance processes, as it relates to investment and financing activities, were adequate. We also conclude the processes were functioning as intended and enabled CSU's objectives and goals to be met. Nothing came to our attention during our fieldwork that indicated processes were not efficient.

As always, feel free to contact me if you have any questions.

Sincerely,

A handwritten signature in purple ink that reads "Jeff Litchfield".

Jeff Litchfield
City Auditor

Cc: Jerry Forte, Utilities Executive Director
Bill Cherrier, Chief Financial Officer
Nancy Briscoe, Manager, Treasury and Finance
Dave Maier, Enterprise Risk Management Services Manager
Debbie Griffin, Sr. Analyst, Enterprise Risk Management
Luann Wagar, Sr. Analyst, Enterprise Risk Management

CITY AUDITOR JEFF LITCHFIELD, CPA CIA CFE CGAP

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Abbreviations and Acronyms Used in this Report

CSU	Colorado Springs Utilities
Treasury	Treasury and Finance Department

Introduction

AUTHORIZATION

We performed an audit of Colorado Springs Utilities Cash and Debt Management functions. We conducted this audit under the authority of Chapter 1, Article 2, Part 7 of the City Code, and more specifically parts 703, 705, and 706, and part 709 (B) and (C) of the Code, which state:

1.2.703: ENSURE PUBLIC ACCOUNTABILITY:

The City Auditor shall ensure that administrative officials are held publicly accountable for their use of public funds and the other resources at their disposal. The City Auditor shall investigate whether or not laws are being administered in the public interest, determine if there have been abuses of discretion, arbitrary actions or errors of judgment, and shall encourage diligence on the part of administrative officials.

1.2.705: DETERMINE EFFECTIVENESS AND EFFICIENCY OF PROGRAMS:

The City Auditor shall determine the extent to which legislative policies are being efficiently and effectively implemented by administrative officials. The City Auditor shall determine whether City programs are achieving desired objectives. The City Auditor shall review the administrative control systems established by the enterprises, department, or group managers and by the City Manager, Colorado Springs Utilities Executive Director, and Memorial Hospital Executive Director and determine whether these control systems are adequate and effective in accomplishing their objectives.

1.2.706: EXAMINE BOOKS, RECORDS:

The City Auditor shall examine and inspect all books, records, files, papers, documents, and information stored on computer records or in other files or records relating to all financial affairs of every office, department, group, enterprise, political subdivision, and organization which receives funds from the City or under the direct or indirect control of the City Council. The Auditor may require any person to appear at any time upon proper notice and to produce any accounts, books, records, files, and other papers pertaining to the receipt or expenditure of City funds, whether general or special. If that person fails to produce the papers, then the Auditor may request Council approval to search for and take any book, paper, or record in the custody of that person or public official.

1.2.709: MAKE PERIODIC REPORTS TO COUNCIL:

The City Auditor shall make periodic reports to Council which shall include the following:

- B. Information of proposals deemed expedient in support of the City's credit, and recommendations for lessening expenditures, for promoting frugality and economy in City affairs, and for an improved level of fiscal management;
- C. Matters concerning the effectiveness and efficiency of the programs and operation of the City;

Introduction

ORGANIZATIONAL PLACEMENT

The Office of the City Auditor is structured in a manner to provide organizational independence from the entities it audits. This independence is accomplished by the City Auditor being appointed by and reporting directly to the City Council. The audited entity in this audit was Colorado Springs Utilities (CSU), under the direction of their Chief Executive Officer. Colorado Springs Utilities' Chief Executive Officer is also a City Council Appointee.

SCOPE AND METHODOLOGY

The purpose of the CSU Cash and Debt Management Audit was to evaluate the adequacy of existing risk management, internal control, and governance processes as it relates to investment and financing activities. We evaluated whether these processes were functioning as intended and enabled the organization's objectives and goals to be met.

We conducted our audit in accordance with the *International Standards for the Professional Practice of Internal Auditing*, a part of the Professional Practices Framework promulgated by the Institute of Internal Auditors. Our audit included such tests of records and other supporting documentation, as we deemed necessary in the circumstances.

Our audit scope included short-term cash management and compliance with terms of bond agreements, CSU's Investment Policy and applicable statutes. Additionally, we reviewed to ensure that interest rate swaps and debt issuances were approved and monitored in accordance with CSU's Financial Risk Management Policy. Our audit scope did not include review of CSU's methodology for accounting for derivative instruments as this is within the scope of the external audit. Further, energy derivatives such as gas hedges did not fall within the Treasury and Finance Department's (Treasury) responsibilities and were not examined in this audit.

We reviewed the internal control structure surrounding activities such as wire transfers and securities purchases to ensure they required involvement of multiple employees to accomplish and that duties were appropriately segregated between Treasury and Accounting. Additionally, we determined that controls were in place to ensure these transactions were recorded accurately and timely, and that systems access was restricted to authorized employees. Our audit process included confirming that oversight activities such as reports to management required by CSU policy were in place.

Since the City Auditor's office reviewed coverage ratios required by bond covenants as part of quarterly Executive Limitations reviews, we did not review them in this audit.

Sufficient competent evidential matter was gathered to support our conclusions. Our audit period was January 1 through December 31, 2008.

BACKGROUND

The City Auditor established a practice of methodically assessing all major functions and systems at least once every five years. The purpose of these audits is to evaluate internal controls that are used to ensure the reliability of financial information. The Cash and Debt Management function is one of the major processes that is audited on a rotating basis.

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Treasury was responsible for managing operating cash, debt issuance and payment, assuring compliance with bond covenants, and investment of funds in the various portfolios. Treasury reports to the Financial Services unit within CSU's Planning and Finance Division. Treasury employees are responsible for executing investment purchases and sales along with the movement of funds between accounts while CSU Accounting records and reconciles these transactions.

Treasury managed short term cash balances (90-120 days). Additionally, Treasury was responsible for coordinating the debt issuance process, as well as, any interest swap arrangements related to bond issuances in consultation with external Bond Counsel. Additional oversight is required by the Risk Management Committee in the Executive Limitations.

Bond ordinances required that restricted funds be established for bond proceeds, and to repay principal and interest. These agreements specified that reserve accounts be established or a bond purchased to provide further assurance to bondholders. Capital expenditures were reimbursed by Treasury personnel from bond proceeds accounts. In the interim, balances in these restricted accounts were invested. Additionally, unrestricted cash was invested. Investment advisory services were retained to suggest the timing of purchases and sales of securities in the current portfolio to maximize returns. During 2008, monies set aside in the Financial Risk Mitigation fund for contingencies were also invested, but this portfolio had been liquidated by the end of 2008 due to significant required collateral postings under interest rate swap agreements.

CSU's Investment Policy sets out investment objectives in priority order as safety, liquidity, and yield along with and specifying investments allowed by policy. The majority of investments were held in cash, or U.S. Government or Agency securities.

Scorecard measures of liquidity and yield were in place and reported monthly to management.

As of December 31, 2008, the total balance of restricted and unrestricted cash and investments was \$333 million. Investments comprised approximately \$132 million of this total.

CSU has entered into agreements to hedge its exposure to changing interest rates for variable rate bond issues through the use of interest rate swaps. CSU's Financial Risk Management Policy required that no more than 30% of variable debt was unhedged. At December 31, 2008, the percentage unhedged by swap arrangements was approximately 8.5%. In 2008, Utilities did not enter into any new interest rate swap agreements.

COMMENDABLE PRACTICES

During our audit period, the Treasury experienced turnover of two positions. We noted that Treasury members absorbed this workload on an interim basis in an effective manner. The Treasury function subsequently filled these open positions during our fieldwork.

Additionally, Treasury staff members identified and documented some of the control processes previously performed by employees that had left the department. Documentation of control procedures is a good business practice that should ensure key procedures and controls are in place during any future personnel transitions.

Introduction

OVERALL OPINION

We conclude the overall risk management, internal control, and governance processes, as it relates to investment and financing activities, were adequate. We also conclude the processes were functioning as intended and enabled CSU's objectives and goals to be met. Nothing came to our attention during our fieldwork that indicated processes were not efficient.