



Audit of the Uses of Series 2006 Certificates of Participation Proceeds

Report # 07-25

Prepared by
Office of Inspector General

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SOUTH FLORIDA WATER MANAGEMENT DISTRICT

February 13, 2008

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Re: Audit of the Uses of
Series 2006 Certificates of
Participation Proceeds
Report # 07-25

This audit was performed pursuant to the Inspector General's authority set forth in Chapter 20.055, F.S. The audit focused on determining whether the proceeds from the Series 2006 Certificates of Participation are being used for authorized purposes. This report was prepared by Jankie Bhagudas and Tim Beirnes.

Sincerely,

John W. Williams, Esq.
Inspector General

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BACKGROUND

In accordance with the Office of Inspector General's FY 2006 Audit Plan, we performed an audit to determine whether the proceeds from the Series 2006 Certificates of Participation are being used for authorized purposes.

On October 12, 2004, former Governor Jeb Bush approved the *Memorandum of Agreement Regarding Acceleration of the Comprehensive Everglades Restoration Plan* that is intended to hasten funding, design, construction and completion of several critical Comprehensive Everglades Restoration Plan restoration projects (Acceler8 projects) within the next seven years, more than ten years ahead of schedule. The acceleration of the projects was considered necessary to save money, and provide immediate environmental, social, and economic benefits. The District's long-term plan for funding the construction costs for Acceler8 projects will be through the issuance of Certificates of Participation.¹ On October 26, 2006, the District issued the Series 2006 Certificates of Participation at a par value of \$546,120,000, which sold for \$572,120,737 (a premium of over \$26 million).

Proceeds from Certificates of Participation are to be used for the following:

- Financing the acquisition, construction, installation and equipping of certain facilities and improvements to land for restoration, protection and preservation of the Everglades ecosystem.
- Repaying of interim financing that was used to commence construction of certain facilities. In January 2006, the District's Governing Board authorized management to obtain \$110 million in short term financing to cover a portion of certain construction and land acquisition costs for the Everglades Forever Act and Comprehensive Everglades Restoration Plan Acceler8 projects. Specifically, the Governing Board authorized \$40 million to be used for the Everglades Forever Act Acceler8 Projects and \$70 million for Comprehensive Everglades Restoration Plan Acceler8 Projects. The District borrowed \$82 million of the

¹ Certificates of Participation are a type of indebtedness that water management districts can incur to finance the undertaking of any capital or other projects for purposes permitted by Florida law.

authorized \$110 million. This loan has been repaid from Certificate of Participation proceeds.

- Paying certain costs of issuance of the Certificates of Participation.

In addition, the Offering Statement for the Certificates of Participation specified that proceeds should be used for the construction of specific phases of the following projects.

- Everglades Agricultural Area (EAA) Reservoir – Construction of Phase 1A.
- C-44 Reservoir/Stormwater Treatment Area Test Cells – Only construction cost of the C-44 Test Cells.
- C-43 West Reservoir Test Cells – Only construction cost of the C-43 Test Cells.
- EAA Stormwater Treatment Areas (STA) Expansion, Compartment B & C. This project includes seven components, however, construction cost for only the following four components will be funded:
 - Compartment B - STA 2 Cell 4;
 - Compartment C - STA 6-2;
 - Compartment C - STA 5 FW 3; and
 - Compartment C – US Sugar Corporation 139 Annex Pump Station

Net proceeds from the Series 2006 Certificates of Participation, after issuance cost and repayment of the short term loan, was approximately \$483 million. The interest rates range from 3.5% to 5.0% and were sold at yields ranging from 3.5% to 4.36%, depending on the maturity date. Proceeds are invested to generate interest income, which is also being used for design and construction. Debt service payments are approximately \$35 million annually and are paid from ad valorem revenues.

OBJECTIVE, SCOPE, AND METHODOLOGY

Our objective focused on determining whether the proceeds from the Series 2006 Certificates of Participation are being used for authorized purposes.

To accomplish our objective, we reviewed the Offering Statement for the Certificates of Participation to determine the authorized uses of the proceeds. We also interviewed Treasury and Accounting Divisions' staff to obtain an understanding of the procedures in place to ensure that the proceeds are used for the authorized purposes and examined various records to determine whether the proceeds are being used for the intended purposes and are accounted for properly (e.g., invoices, contract documents, bank statements, and the District's financial and project management systems).

Our audit was conducted in accordance with Generally Accepted Government Auditing Standards. These standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

AUDIT RESULTS

Executive Summary

Our review disclosed that there are controls in place to ensure that the Certificates of Participation bond proceeds are used for authorized costs. The proceeds and interest earnings are held by Deutsche Bank National Trustee (Trustee) and in order to drawdown funds from the Trustee, the District is required to submit Reimbursement Requests certifying that the amounts being requested are for authorized expenses that have been properly incurred. In addition, along with each Reimbursement Request the District is required to submit supporting documentation, which includes an itemized listing of the amounts being requested, names of the corresponding projects, copies of approved invoices, and other relevant documentation.

However, a minor improvement should be considered to ensure that all interest earned is accurately reflected in the District's records. Specifically, the Accounting Division is responsible for recording the interest earned on the Trustee account into the District financial system. The interest income entry is made based on the amounts reflected in the reconciliations prepared by the District's Treasurer. However, there are no procedures in place for the Accounting Division to verify that the amounts on the reconciliation to the Trustee statements, in order to ensure that the reconciliations are accurate. Although we are recommending this procedure be implemented as a preventative measure, it should be noted that no errors have actually occurred.

Certificates of Participation Proceeds are Being Used Only for Authorized Expenses

Our review disclosed that there are controls in place to ensure that the Series 2006 Certificates of Participation bond proceeds are used for authorized costs. The proceeds and interest earnings are held by Deutsche Bank National Trustee (Trustee) and in order to drawdown funds from the Trustee, the District is required to submit Reimbursement Requests certifying that the amounts being requested are for authorized expenses that have been properly incurred. In addition, along with each Reimbursement Request the District is required to submit supporting documentation, which includes an itemized listing of the amounts being requested, names of the corresponding projects, copies of approved invoices, and other relevant documentation.

Further, our examination disclosed that proceeds from the Certificates of Participation are being used to pay for authorized costs. Specifically, during the period November 2006 to December 31, 2007, the proceeds have been used for the following:

- Paying costs of issuing the Certificates of Participation.
- Repaying of interim financing that was used to commence construction of certain Acceler8 projects, including accrued interest.
- Paying construction costs for the phases of the projects indicated in the Certificates of Participation's Offering Statement. Our conclusion was based on various tests including a detailed review of five reimbursement requests totaling \$38,865,398 that were used to make 38 payments in connection with 17 contracts and work orders.

The following table shows proceeds from the issuance of the Series 2006 Certificates, interest earned on the proceeds, uses of the proceeds, and the balance as of December 31, 2007.

Bond Proceeds and Interest Earned (as of December 31, 2007)		
Bond Proceeds		\$ 546,120,000
Bond Premium		26,000,737
Interest Earned, as of December 31, 2007		23,587,177
Total Available Cash		\$ 595,707,914
Uses of Proceeds		
Issuance Costs		
Various Issuance Costs	\$ 801,202	
Underwriter's Discount	1,496,374	
Bond Insurance Premium	1,779,919	
Title Insurance	161,749	
Total Issuance Costs	\$ 4,239,244	(4,239,244)
Payoff of Interim Financing (\$82M) including Accrued Interest		(84,510,067)
Withdrawals from Trustee for Construction Expenses and Other Authorized Expenses		(129,491,445)
Total Amount Used		(218,240,756)
Ending Balance, as of December 31, 2007		\$377,467,158

Accounting Division Should Verify Interest Earnings to Trustee Statements

During our review, we noted that the District's Treasurer is responsible for the following:

- Requesting funds from the Trustee, which are wired directly to the District's operating bank account.
- Preparing monthly bank account reconciliations of the various accounts containing the proceeds from the Certificates of Participation issuance and determining the total interest earned each month.

Accounting Division staff enters the interest earned into the District's financial system based on the amounts in the reconciliation prepared by the Treasurer. We noted that there is no confirmation process in place to ensure that the interest amounts are

accurate. Although we concluded that the correct interest earnings were posted in SAP, additional steps should be taken to substantiate interest earnings from the Trustee statements before they are posted. We are recommending this procedure be implemented as a preventative measure; however, it should be noted that no errors have actually occurred.

Recommendation

- 1. Implement procedures to ensure that Accounting Division staff substantiates interest earnings before posting it to the District's financial system.**

Management Response: Management concurs with the recommendation. Accounting now requires that copies of the monthly account statements be provided as a basis for posting interest earnings.

Responsible Department: Finance and Administration/Accounting and Financial Services

Estimated Completion: Completed