



ULSTER COUNTY COMPTROLLER'S INVESTMENT FOLLOW UP AUDIT

2023

Office of the
Ulster County Comptroller
March S. Gallagher





ULSTER COUNTY OFFICE OF THE COMPTROLLER

Investment Follow Up Audit

comptroller.ulstercountyny.gov

Released December 2023

Objectives

- Determine if Ulster County complied with the Ulster County Investment Policy during the audit period.
- Determine if Ulster County maximized cash investment opportunities, while maintaining appropriate diversification during the audit period.

Executive Summary

Why this audit is important?

Ulster County regularly maintains more than \$200 million in cash that could be more strategically invested to maximize the potential for investment earnings. In May of 2023, the County Legislature adopted a new Investment Policy to address the findings of our previous audit. As a result, we have performed this audit to determine if the County has complied with the new Policy, and to determine if appropriate changes have been made to address the recommendations made in our initial audit of investments. The period for this follow-up audit is from January 1, 2022, through September 30, 2023.

Findings

Our follow up audit revealed noncompliance with several sections of Ulster County's new Investment Policy. Specifically, an Investment Advisory Board has yet to be convened as required by the Policy. According to the updated Policy, the Investment Advisory Board is required to meet quarterly to review the performance of the County's investments and cash flow projections. The Board must report to the County Executive and the County Legislature no less than annually on the performance of County investments.

Since the prior audit, Ulster County has transferred a total of \$128.0 million from a lower interest-bearing account to a higher interest-bearing account within the Bank of Greene County ("BOGC") and generated \$4.21 million more in interest revenue as a result. While this is a shift in the right direction, this follow up audit reveals that interest revenues realized are still not being maximized within the current investment structure. This is because surplus cash remained in the Deposit Account which could have produced an additional \$2.4 million in supplementary interest revenue. Had a cash flow analysis been completed in accordance with the new Policy, we believe that more cash would have been transferred to higher interest-bearing accounts that would have achieved diversification.

Our initial investment audit also found that the Commissioner of Finance had not established written procedures for the operation of the Investment Policy as required by the Ulster County Charter. Our follow up audit revealed that this finding remains unaddressed.

What we recommend

We recommend the Investment Advisory Board be established and convened immediately as outlined in the Investment Policy. The Commissioner of Finance should establish written procedures to ensure that the County complies with the reporting and documentation requirements included in the current Investment Policy.

The procedure should establish formal documentation of the receipt of depository listings and Executive approval, as well as formal documentation of the submission, receipt, and review of the annual investment report.

The procedures should require that the following information be provided to the Investment Advisory Board:

1. A monthly listing of all investments and the market value of those investments.
2. A quarterly analysis of investment earnings.
3. A monthly cash flow analysis that will allow the board to determine the desired cash floor for the pooled Deposit Account and ensure that all excess cash is generating optimal interest revenues, while maintaining diversification.

The Commissioner should also report the current anticipated interest rates of bonding and related debt to Investment Advisory Board to compare to the amount of interest being earned on cash balances to the cost of debt being issued. This will allow for cash investments to be considered versus cash deployments to conduct an effective debt analysis.

The Department of Finance should monitor arbitrage liability and any calculations prepared by the Department or County vendors should be presented to the Investment Advisory Board for consideration, as presently increasing interest rates create the potential for arbitrage earnings on unexpended bond proceeds. Arbitrage occurs when tax-exempt bond proceeds are invested in higher yielding taxable securities, resulting in a profit.

New Findings & Recommendations

Finding 1: An Investment Advisory Board was not established or convened.

Condition: The County did not commence the establishment of the Investment Advisory Board. The Board is designed to guide the Commissioner of Finance in the implementation of the Investment Policy.

Effect: The Board did not meet quarterly to review the performance of the County's investments, cash flow projections or future economic forecasts. Without guidance and analysis of the essential information, the investment program of the County did not optimize interest revenues or appropriately diversify the investments of the County.

Cause: The May 2023 Investment Policy does not address who should be the individual or the branch of government to initiate the Investment Advisory Board. Because the Policy is vague on the initiation of the Board, the initial steps were not taken, such as, the County Executive did not appoint two members for the Board, nor did the Chair of the Legislature appoint one member, or the Minority Leader appoint one member. The Comptroller recently named her one appointed member to the Board in an effort to get the process underway. The Policy does not specify who is responsible for the for the administration of the Board.

Criteria: The May 2023 Investment Policy added section IV related to the Investment Advisory Board. The Board shall comprise of five members, two appointed by the County Executive, two by the Legislature, and one by the Comptroller.

Recommendation 1: We recommend that members be appointed to an Investment Advisory Board as outlined in the Investment Policy and that the Board meet and review initial information regarding the performance of the investment program and other relevant data regarding cash flow projects and economic forecasts. We also recommend the Investment Policy be updated to address who is responsible for the administration of the Investment Board as well as the scheduling the quarterly meetings.

Recommendation 2: The Investment Advisory Board should meet quarterly as outlined in the Policy and in addition to reviewing historical investment data, the Board should be presented other investment opportunities the County is currently not participating in that could be beneficial to satisfying revenue optimization as well as increasing diversification by financial institution.

Finding 2: Lack of diversification by financial institution.

Condition: The County does not diversify its deposits and investments by financial institution. Ulster County maintains over 96% of cash balances in one relatively small financial institution, the Bank of Greene County. According to the Bank of Greene County's June 2023 Consolidated Statements of Financial Condition, the Bank had total deposits of \$2,437,161,000. Ulster County had \$237,333,528 deposited at that time, or 9.74% of entire bank deposits. Also of note, as of June 30, 2023, the Bank of Greene County only had \$196,445,000 in the form of cash and cash equivalents. If the County attempted to withdraw all its deposits from the bank on that day, the bank may have struggled to meet its obligation to the County.

Effect: This concentration poses a significant financial risk to Ulster County, as it could potentially expose most available cash to the vulnerabilities and fluctuations associated with one institution. This could lead to a dependency on its services and any disruptions in the bank's operations, changes in policies, or deterioration in its financial health could disrupt the entity's cash management, causing inconvenience or financial loss. These risks are only partially mitigated through the required collateralization and the use of IntraFi.

Cause: Lack of investment strategy allowed the County to maintain an abnormal percentage of total available cash within one institution. Had an Investment Advisory Board met quarterly and discussed the need for diversification in accordance with the Investment Policy this may have been averted.

Criteria: Similar to the prior Policy, the Investment Policy adopted by Ulster County in May 2023 explicitly states in Section VII the necessity of diversifying deposits and investments across various financial institutions, investment instruments, and maturity schedules.

Recommendation 1: Implement a diversification plan that adheres strictly to the Investment Policy. This involves reallocating funds across multiple financial institutions, diversified investment instruments, and a varied maturity schedule to reduce risk exposure.

Recommendation 2: The Investment Policy should expand on the diversification section to establish maximum percentages allowable in one financial institution. Also, the quarterly meeting for the Investment Advisory Board should discuss and strategize diversification. This proactive approach will ensure consistent evaluation and adjustment of the investment portfolio.

Follow Up to Prior Findings & Recommendations

Prior Finding 1: Interest revenues were not optimized.

This finding has been partially addressed. Since our previous audit, the County invested \$128,000,000 over the period into more lucrative financial instruments. This updated investment strategy earned the County an additional \$4.21 million over the period when compared to what the County would have earned by leaving the funds in the traditional deposit account as they had been.

The County's traditional Deposit account with Bank of Greene County maintained an average cash balance of over \$90 million from January 2022 through September 2023 and the County has yet to perform a cash flow analysis to determine the required amount of cash to be maintained in the Deposit account to cover operating expenses. We refer to this amount in this report as the "cash floor". The Deposit account earns minimal interest at 1%, so once a cash floor amount is determined, the amount in excess of the cash floor should be distributed to other investment opportunities to optimize interest earnings as many would yield over 4% more.

For every \$1,000,000 invested during the audit period, the potential interest on the funds actually invested could have been \$55,495 which is an additional \$41,541 in interest revenue that could have been generated over the investments we did make. The following additional interest revenues could have been attained in each of the following investment accounts the County either currently has or could opt into:

Interest Per \$1,000,000 invested 1/1/2022		
Financial Instrument	Potential Interest	Forgone Revenue
BOGC Deposit	\$ 13,954	\$ -
Salisbury MM	\$ 18,899	\$ 4,944
M&T MM	\$ 23,120	\$ 9,165
Webster MM	\$ 26,190	\$ 12,236
BOGC Deposit PLUS*	\$ 52,221	\$ 38,267
NYLAF	\$ 52,535	\$ 38,581
NYCLASS PRIME	\$ 55,495	\$ 41,541

*Deposit PLUS was created in April 2022, so Deposit account rates were used for January to March 2022.

A cash flow analysis would determine the surplus amount of cash available for investment by revealing a desired cash floor amount of the Deposit account. The cash floor amount may vary over months or specific periods based on the cash flow of the County. To simplify computations, we have calculated the additional interest amount that could have been attained at three different static cash floor levels. We have determined the County could have made an additional \$2.4 million over the period if a static \$25 million cash floor was applied. The County's cash flow analysis will determine a cash floor that should change over course of the year based on cyclical expenditures.

Additional Interest			
Cash Floor	NYCLASS PRIME	NYLAF	Deposit PLUS*
\$ 40,000,000	\$ 1,822,357	\$ 1,673,189	\$ 1,671,882
\$ 25,000,000	\$ 2,426,007	\$ 2,234,625	\$ 2,228,838
\$ 15,000,000	\$ 2,828,441	\$ 2,608,915	\$ 2,600,142

*Deposit PLUS was created in April 2022, so Deposit account rates were used for January to March 2022.

The investment opportunities reviewed provide a 1-3-day period to transfer assets back to liquid form. We recognize that currently, there are not adequate controls in place to ensure accurate as well as timely financial reporting and consequentially performing a cash flow analysis may not be possible at this time. As a result, we recommend strengthening controls surrounding accurate and timely financial reporting, especially entries that involve cash accounts.

Prior Finding 2: Lack of written procedures and oversight.

The finding regarding the lack of written procedures and oversight in Ulster County's investment practices remains unaddressed, with the recommendations for improvement remaining unimplemented. Because the Board has not been convened, the Commissioner of Finance has not complied with mandatory annual reporting requirements or submitted necessary reports to the County Executive and Legislature as outlined in the County's Investment Policy. The absence of comprehensive investment reports and established procedures has resulted in a potential inability to maximize investment revenues and ensure proper diversification, exposing the County to risks associated with concentration in one institution or investment type. The absence of documented oversight and submission of reports has left key decision-makers unaware of investment activities, hindering informed financial decision-making. The audit recommendations advised adherence to Policy requirements, timely completion of necessary reports, and the establishment of written procedures to ensure compliance, approval, and oversight in line with the County's Investment Policy.

Scope

This audit period ran from January 1, 2022, through September 30, 2023. The analysis included a review of the County's Investment Policy and the required deliverables for the period, as well as the compilation of data related to the County's earnings on investments including average cash balances, interest rates, and historical municipal rates.

Background

The investment options available to municipalities are restricted by state and local laws to reduce the risk of loss related to highly volatile investments, while still allowing municipalities to generate some level of investment earnings from surplus cash. The amount of investment risk allowed is low, and as a result the investment reward is similarly low. While municipalities are often limited to investing in low-risk investments, because of the large volume of cash the County has available to invest, even small changes in rates of return can have a significant impact on the County's ability to maximize revenues with these funds.

Section 11 of General Municipal Law ("GML") contains statutory provisions on the authority to invest and types of investments permitted. Section 39 of GML requires governing boards to adopt a comprehensive Investment Policy that details the government's operative policy and instruction to officers and staff regarding the investing, monitoring, and reporting of funds of the local government.

Ulster County adopted an Investment Policy pursuant to Section 39 of GML and the New York State Office of the State Comptroller, Local Management Guide – Investing and Protecting Public Funds, with Resolution #35 of 2013. The County's Investment Policy is required to be updated annually with any potential enhancements noted from the annual investment report. The investment report should detail the interest earned for the year at each of the financial institutions that held County funds under Department of Finance control. The report should show cash balances for each financial institution and the associated interest rates, as well as an indication if there were other investments pursued during the year, and any recommendations for changes to the Investment Policy. The Comptroller's Office is only aware of one report produced during the 2021 Investment Policy Audit.

In 2021, NYS moved to expand investment opportunities to upstate counties that had been previously granted to New York City during the pandemic. (Chapter 255, Laws of 2021 - A. 7209 (Thiele). This authorization, which originally was set to expire on July 1, 2023, has since been extended for three more years.

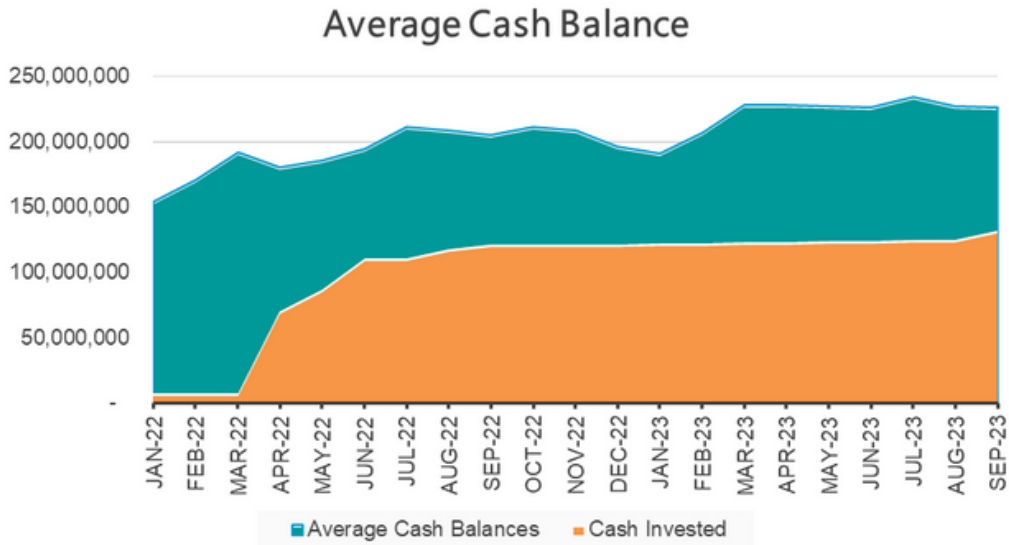
This statute permits counties to invest in:

- General obligation bonds and notes of any state other than New York, provided that such bonds receive the highest rating of at least one independent rating agency,
- Obligations of any corporation organized under the laws of any state, provided that such obligations received the highest rating of two independent rating services and that no more than \$250 million is invested in any one corporation,
- Bankers' acceptances maturing within 270 days which are eligible for purchase in the open market by federal reserve banks,
- Obligations of, or instruments issued by, any agency or instrument of the USA, including federal home loans banks, the Tennessee Valley Authority, the Federal National Mortgage Association, Federal Home Loan Mortgage Association, and the United States Postal Service, provided that no more than \$250 million is invested in any one agency, and
- No load money market mutual funds, provided that such funds are limited to investments in obligations of agencies or instrumentalities of the USA, where payment is guaranteed by the USA;

The expanded investment opportunities came at a time that the County had significantly more cash on hand as a result of pandemic funding and multi-year budget surpluses.

In response to our 2021 audit of the County's Investment Policy compliance and the expanded investment opportunities under state law, the Policy was strengthened by Resolution 317 of 2023 to create an Advisory Board, define and curtail conflicts of interest, and tighten the time to deposit funds from one week to 48 hours. The Policy was also amended to make it clear that the former interpretation that collaborative municipal investment funds were not available to Ulster County because they were not "depository institutions" located in the County was not correct. Finally, the new Policy requires a depository institution report to the Clerk of the Legislature and Comptroller annually.

The chart below displays the monthly average cash balance and breaks out the amount the county has invested over the period:



As seen from the chart above the amount of cash invested since we undertook our prior audit grew substantially by June 2022 to over \$110 million. The County has made progress in investing cash since our last report; however, there remains a substantial amount of cash available for investment with potential for greater earnings. A cash flow analysis should be performed periodically to establish the desired cash floor amount.

Interest rates started at a minimal level but have grown with the federal rate increases over the last year and now the difference between idle cash and invested cash can mean substantial amounts of forgone revenue to the County. See the average rate chart below for various investment rates throughout the period:

Month	Salisbury MM	M&T MM	Webster MM	BOGC Deposit	BOGC Deposit PLUS	BOGC IntraFi	NYCLASS/ PRIME*	NYLAF
Jan-22	0.130%	0.050%	0.080%	0.120%			0.035%	0.005%
Feb-22	0.130%	0.050%	0.080%	0.120%			0.199%	0.009%
Mar-22	0.130%	0.050%	0.080%	0.120%			0.356%	0.063%
Apr-22	0.160%	0.050%	0.140%	0.180%	0.290%		0.567%	0.182%
May-22	0.260%	0.050%	0.160%	0.410%	0.610%		0.796%	0.555%
Jun-22	0.300%	0.050%	0.460%	0.670%	0.900%		1.061%	0.951%
Jul-22	0.300%	0.050%	0.820%	1.000%	0.900%		1.573%	1.431%
Aug-22	0.300%	0.050%	1.210%	1.000%	2.010%		2.203%	2.078%
Sep-22	0.300%	0.050%	1.270%	1.000%	2.430%		2.477%	2.360%
Oct-22	0.300%	0.600%	1.590%	1.000%	2.430%		3.032%	2.896%
Nov-22	0.300%	1.100%	1.760%	1.000%	3.580%		3.739%	3.552%
Dec-22	0.300%	1.100%	2.030%	1.000%	4.000%		4.120%	3.918%
Jan-23	0.300%	1.750%	2.160%	1.000%	4.000%		4.426%	4.229%
Feb-23	0.300%	1.750%	2.190%	1.000%	4.660%		4.681%	4.464%
Mar-23	1.250%	2.500%	2.260%	1.000%	4.660%		4.659%	4.599%
Apr-23	2.610%	2.500%	2.300%	1.000%	4.660%	4.563%	4.898%	4.752%
May-23	3.000%	2.500%	2.420%	1.000%	5.040%	4.956%	5.051%	4.941%
Jun-23	3.000%	2.500%	2.470%	1.000%	5.070%	5.080%	5.092%	4.969%
Jul-23	3.050%	2.500%	2.470%	1.000%	5.070%	5.080%	5.192%	5.120%
Aug-23	3.000%	4.100%	2.520%	1.000%	5.270%	4.956%	5.374%	5.197%
Sep-23	3.000%	4.100%	2.570%	1.000%	5.280%	5.156%	5.397%	5.266%

*NYCLASS/ PRIME rates are the traditional NYCLASS rates for January 2022 combined with the NYCLASS PRIME rates for the remainder of the period. The rates of the Deposit PLUS account and the IntraFi account are not listed or available prior to the County banking statements which list the yield percentages.

ULSTER COUNTY EXECUTIVE

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December 12, 2023

March Gallagher
Ulster County Comptroller
244 Fair Street
Kingston, NY 12401

Re: Investment Audit Follow-Up

Dear Comptroller Gallagher:

On behalf of my office and the Department of Finance, I offer the following comments in response to the draft Investment Policy audit.

The subject of this audit is the County's amended Investment Policy, which was adopted in May of this year, only four months before the end of the audit period. As the audit points out, the Investment Advisory Board has yet to be fully appointed and convened. Responsibility rests with the appointing authorities, including the Comptroller's office, the Chair and Minority Leader of the Legislature, and my office. The Comptroller made her appointment two days before submitting this draft audit. I expect to announce my appointments this week. The Legislative Leadership has yet to make appointments. It seems premature to assess compliance with the amended policy only four months after its adoption and before the Investment Advisory Board has been appointed.

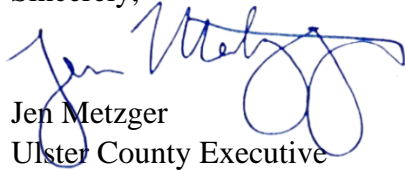
Second, the Comptroller's analysis of "forgone revenue" includes financial instruments that may not be the most appropriate choice for the County. As stated in the Investment Policy, the County's primary investment goals are to safeguard the County's finances, mitigate risk, ensure sufficient liquidity, and obtain a reasonable rate of return. The return on investments in higher-yielding accounts is of secondary importance compared to the portfolio's safety and liquidity objectives.

Third, the County's investments are more diversified than the draft audit suggests. While it is true that 96% of cash balances are managed by the of Bank of Greene County, over 20% of those funds have been invested by the Bank in Intra-FI, which is a separate, diversified, FDIC-

insured instrument that spreads this investment over hundreds of financial institutions. This decision was taken at my direction in consultation with then-Acting Finance Commissioner Juras prior to the appointment of the new Finance Commissioner. I wholeheartedly agree that diversification is critical to protecting the financial assets of the County.

I appreciate the Comptroller's diligence in auditing compliance with the County's Investment Policy, and I have every confidence that Finance Commissioner Daw, working together with the Investment Advisory Board, will manage the safety, liquidity, and investment return of the County's finances with great care.

Sincerely,

A handwritten signature in blue ink, appearing to read "Jen Metzger", with a large, stylized flourish at the end.

Jen Metzger
Ulster County Executive

ULSTER COUNTY OFFICE OF THE COMPTROLLER

March S. Gallagher, Esq.
Comptroller



Alicia DeMarco, CPA
Deputy Comptroller

Charles Dinstuhl, CPA
Director of Internal Audit & Control

Comptroller's Office Comments on Management's Response

Thank you for your response to our follow up audit on the County's Compliance with the Investment Policy. We appreciate the Administration's efforts to improve the County's management and strategy towards investment. We wanted to address your comments specifically, as outlined below, to provide some additional clarity regarding our findings and recommendations.

While the Policy is new to Ulster County, it is effective as of the date of the resolution. Management asserts that because a new Policy was adopted in May 2023 and the audit period only covered four months of the new Policy that it is premature to assess compliance with the Policy. While we understand that the Administration may not have been immediately prepared to respond to the Policy and its requirements, a timeline for corrective action would ensure that the County is moving towards compliance. We continue to recommend the County Legislature update the investment Policy "to address who is responsible for the administration of the Investment Board as well as the scheduling of the quarterly meetings." We also note that this was a follow up to a March 2022 audit and as of December 2023, many of the recommendations of that prior audit have still not been implemented.

Management states that the analysis of forgone revenues includes "financial instruments that may not be the most appropriate choice for the County." Our analysis included examination of only those investment alternatives limited to specific asset classes allowed by state law for municipalities. The response does not address that a cash flow analysis is not being performed at all. Additionally, our analysis included three different investment instruments, one of which the County currently utilizes. Simply transferring cash from the Deposit Account to the Deposit PLUS Account could have yielded an additional \$2.2 million, however this would not address diversification.

We agree that Intra-Fi provides diversification by instrument, however, having one institution responsible for managing 96% of cash still represents a risk, especially when that amount represents 10% of entire bank deposits in the financial institution. The investment Policy requires diversification by financial institution, by investment instrument, and maturity schedule. Even using management's logic and carving out Intra-Fi, 75% of cash balances (an avg of \$175 million) remain in one financial institution. We continue to recommend "the investment Policy should expand the diversification section to establish maximum percentages allowable in one financial institution." The Policy diversification goes beyond the added protection offered by Intra-Fi, which covers only a portion of the County's cash funds.