

AUDIT REPORT



CITY OF NEW YORK
OFFICE OF THE COMPTROLLER
BUREAU OF FINANCIAL AUDIT
WILLIAM C. THOMPSON, JR., COMPTROLLER

Audit Report on the Administration Of the Institutional Network and Crosswalks Funds by the Department Of Information, Technology and Telecommunication

FM03-084A

June 21, 2004



THE CITY OF NEW YORK
OFFICE OF THE COMPTROLLER
1 CENTRE STREET
NEW YORK, N.Y. 10007-2341

WILLIAM C. THOMPSON, JR.
COMPTROLLER

To the Citizens of the City of New York

Ladies and Gentlemen:

In accordance with the responsibilities of the Comptroller contained in Chapter 5, § 93, of the New York City Charter, my office has conducted an audit to determine whether the Department of Information, Technology and Telecommunication (DoITT) accurately records and tracks the Institution Network and Crosswalks revenues and expenses; and whether DoITT ensures that these funds are spent on items for the Institutional Network and Crosswalks, as specified in the franchise agreements with the cable companies.

The results of our audit, which are presented in this report, have been discussed with DoITT officials, and their comments have been considered in preparing this report.

Audits such as this provide a means of ensuring that City agencies have adequate controls over fiduciary accounts and that moneys in these accounts are used in accordance with applicable rules and regulations.

I trust that this report contains information that is of interest to you. If you have any questions concerning this report, please contact my audit bureau at 212-669-3747 or e-mail us at audit@Comptroller.nyc.gov.

Very truly yours,

A handwritten signature in cursive script that reads 'William C. Thompson, Jr.'.

William C. Thompson, Jr.
WCT/gr

Report: FM03-084
Filed: June 21, 2004

*The City of New York
Office of the Comptroller
Bureau of Financial Audit*

**Audit Report on the Administration of the
Institutional Network and Crosswalks Funds by the
Department of Information, Technology and
Telecommunication**

FM03-084A

AUDIT REPORT IN BRIEF

This audit determined whether the City Department of Information, Technology and Telecommunication (DoITT) accurately records and tracks I-NET and Crosswalks revenues and expenses; and whether DoITT ensures that these funds are spent on items for I-NET and Crosswalks, as specified in the franchise agreements.

Since 1983, the City has entered into cable television service franchise agreements with various companies, which required the companies to make available approximately \$48 million for the City's Institutional Network (I-NET) and its public access cable channel—Crosswalks. Of the \$48 million, \$11.4 million was deposited into fiduciary accounts managed by the City,¹ and the remaining \$36.6 million was retained by the companies to be drawn down by the City as needed. As of December 31, 2003, \$29.4 million of the funds were spent, leaving a balance of \$18.6 million.

Audit Findings and Conclusions

DoITT accurately records and tracks I-NET and Crosswalks revenues and expenses. DoITT also ensured that funds were spent on items for I-NET and Crosswalks, in accordance with the franchise agreements. However, DoITT did not consult with the Borough Presidents and the Comptroller on the use of I-NET funds, as required by the franchise agreements with the

¹ Fiduciary accounts are used by City agencies to record financial resources held and administered in trust by the City of New York. A portion of the INET and Crosswalk funds and all of the Interconnection Working Group funds were held in the following five fiduciary accounts: the Interconnection Working Group, the Institutional Cable Fund, the Municipal Network Fund, the Municipal Channel Grant (Time Warner), and the Municipal Channel Grant (Cablevision).

cable companies. In addition, two of DoITT's five fiduciary accounts, which have a combined balance of \$438,878, have been dormant for several years.

Audit Recommendations

To address these issues, we recommend that DoITT:

- Consult with the Borough Presidents and the Comptroller on future expenditures of I-NET funds. In that regard, DoITT should provide a list of proposed projects and related costs to the Borough Presidents and the Comptroller for comment.
- Determine in conjunction with the City's Law Department whether the Interconnection Working Group Fund and the Municipal Cable Network Fund are necessary and legally required. If not, the accounts should be closed in accordance with the provisions of Comptroller's Directive 27, and the funds should be disbursed in accordance with the Law Department's guidance.

INTRODUCTION

Background

Since 1983, the City has entered into franchise agreements with various companies, which granted them the right to provide cable television services. The agreements required the companies to make funds available for the construction and support of the City's Institutional Network (I-NET)—a system that links various government and education networks. These companies are also required to fund Crosswalks—a public access cable channel. The City Department of Information, Technology and Telecommunication (DoITT) is responsible for administering these funds.

Under the agreements, the companies were required to pay the City approximately \$48 million; \$36.8 million for I-NET, \$10.5 million for Crosswalks, and \$700,000 for the Interconnection Working Group (IWG).² Of the \$48 million, \$11.4 million was deposited into fiduciary accounts managed by the City, and the remaining \$36.6 million was retained by the companies to be drawn down by the City as needed. As of December 31, 2003, \$29.4 million of the funds were spent, leaving a balance of \$18.6 million: \$11.8 million for I-NET, \$6.4 million for Crosswalks, and \$437,000 for IWG. With regard to those funds retained by the companies, the 1998 agreements with Time Warner and Cablevision state that "expenditures from the fund . . . shall be directed by DoITT in consultation with the Comptroller and Borough President."

² According to the 1983 Cable Franchise Agreements, the Interconnection Working Group consisted of a committee of Mayoral Appointees and Franchise Representatives responsible for establishing a plan to ensure that all cable systems within the City could effectively communicate with each other as well as with such systems outside the City. The franchisees shall bear the cost of the Interconnection Working Group.

Fiduciary accounts are established by the New York City Comptroller's Office, in conjunction with the City's Office of Management and Budget (OMB), at the request of various organizations, including City agencies and public benefit corporations. According to Comptroller's Directive 27 "Resources of Fiduciary Accounts are generally under the custodianship of the New York City Office of the Comptroller. The accounts are maintained and controlled by the City agency that requests their establishment." Directive 27 also states, "The City agency will then be responsible for recording all cash receipts and disbursements in FMS [Financial Management System] as well as ensuring that all activity in the account is in compliance with the purpose for which it was created."

Objectives

Our audit objectives were to determine whether DoITT:

- accurately records and tracks I-NET and Crosswalks revenues and expenses, and
- ensures that the funds are spent on items for I-NET and Crosswalks, as specified in the franchise agreements.

Scope and Methodology

This audit covered the period July 1, 2001, through June 30, 2002 (Fiscal Year 2002). Certain tests of expenses were extended to cover the period July 1, 2002, to December 31, 2003.

To accomplish our objectives, we reviewed the agreements to determine the specific amounts to be contributed and the guidelines for spending these funds. We interviewed various DoITT officials and conducted observations of I-NET facilities to gain an understanding of the processes for recording, reporting, and spending the funds and documented our understanding through flowcharts and written narratives. We evaluated the adequacy of the internal controls in place over these processes to determine the type and extent of audit testing needed.

To determine whether DoITT accurately recorded the funds, we examined DoITT's financial records and matched the beginning fund balances to the amounts specified in the agreements. In addition, we compared DoITT's records to the amounts listed on FMS (for funds in the fiduciary accounts) and on reports submitted by the cable companies (for funds held by the companies). We also ascertained whether DoITT's records accounted for interest on unused funds.

To determine whether funds were appropriately spent on items for I-NET and Crosswalks and whether those expenses were accurately recorded, we reviewed documentation related to all disbursements in Fiscal Year 2002. For our examination of expenses for the period July 1, 2002 to December 31, 2003, we selected a judgmental sample of 28 disbursements totaling \$1.6

million (representing 28 percent of the amount spent during this 18-month period.) The documentation reviewed for each disbursement included purchase requisitions, purchase orders, invoices, and payment vouchers. We also checked whether each disbursement was authorized by appropriate DoITT officials.

During our examination of the INET and Crosswalks funds and our review of the franchise agreements, we identified an additional fiduciary account—the Interconnection Working Group Fund. Therefore, we expanded the scope of this audit to include a review of the receipts and expenditures of this account. In addition, since we found that the Interconnection Working Group Fund account was dormant for several years, we requested that the City’s Law Department provide a determination as to the proper disposition of the funds remaining in this account.

* * * * *

This audit was conducted in accordance with generally accepted government auditing standards (GAGAS) and included tests of books and records and other audit procedures considered necessary. This audit was performed in accordance with the audit responsibilities of the City Comptroller as set forth in Chapter 5, § 93, of the New York City Charter.

Discussion of Audit Results

The matters covered in this report were discussed with DoITT officials during and at the conclusion of this audit. A preliminary draft report was sent to DoITT and discussed at an exit conference held on March 16, 2004. On March 29, 2004, we submitted a draft report to DoITT officials with a request for comments. We received a response from DoITT on April 12, 2004.

DoITT officials agreed that the agency accurately records and tracks I-NET and Crosswalks revenue and expenses. However, they strongly disagree that DoITT does not comply with its commitment to engage in consultation with the Comptroller and the Borough Presidents regarding expenditures from I-NET funds. In any case, DoITT officials indicated that they are prepared to discuss with the Comptroller’s Office new procedures for “consulting” on future I-NET expenditures.

The full text of the Department’s response is included as an addendum to this report.

FINDINGS

DoITT accurately records and tracks I-NET and Crosswalks revenues and expenses. In addition, DoITT ensured that funds were spent on items for I-NET and Crosswalks, in accordance with the franchise agreements. However, DoITT did not consult with the Borough Presidents and the Comptroller on the use of I-NET funds, as required by the franchise agreements with the cable companies. In addition, two of DoITT's five fiduciary accounts, which have a combined balance of \$438,878, have been dormant for several years.

Borough Presidents Offices and the Comptrollers Office Not Consulted on Use of I-Net Funds

As mentioned earlier, with regard to those funds retained by the companies, the 1998 agreements with Time Warner and Cablevision state that "expenditures from the fund . . . shall be directed by DoITT in consultation with the Comptroller and Borough President."

DoITT did not consult with the Comptroller or Borough Presidents despite spending more than \$14.2 million in I-NET funds. Instead, DoITT merely sent letters to the Comptroller's Office and the Borough Presidents Offices requesting proposals for future I-NET projects. These letters certainly fall short of the consultation specified in the agreements.

DoITT's Response: "DoITT strongly disagrees with the Draft Report's evaluation of DoITTs compliance with the commitment of DoITT to engage in 'consultation' with the Comptroller and Borough Presidents regarding expenditures from the Institutional Network ('I-NET') fund. Prior to deciding how to direct such expenditures, DoITT solicited in writing the views of the Comptroller and the Borough Presidents, received written suggestions from them, reviewed and discussed those suggestions, and took those suggestions into serious consideration. DoITT further offered to meet with the staff of the Comptroller's Office and Borough Presidents' Offices to discuss their respective recommendations, an offer that was accepted by the Comptroller's Office. DoITT staff and staff of the Comptroller's Office met to discuss the Comptroller's suggestions regarding I-NET expenditures and the goals of the I-NET project. DoITT took all of the Comptroller's and Borough Presidents' suggestions, both written and oral, into account in making final decisions as to how to direct expenditures of I-NET funds."

Auditors' Comments: DoITT's response is somewhat disingenuous in that its offer to hold meetings did not occur until after such meetings were requested by the Comptroller's Office. In addition, we still maintain that DoITT's efforts fall short of the consultation specified in the franchise agreements. For example, DoITT's January 24, 2004 letter to the Comptroller on planned I-NET applications did not indicate that it was providing the information pursuant to its obligations under the franchise agreements, nor did it outline budgets for the proposed projects or information on additional funds available for other applications. Instead, the letter outlined initial and planned I-NET applications that were developed by DoITT. The Comptroller's Office was not consulted in developing these proposals and there is no indication that the Borough Presidents were consulted. The letter then closed with a perfunctory statement that the

Comptroller's Office should contact DoITT if it had suggestions about additional I-NET applications that it would like DoITT to consider. Regarding other requests for I-NET proposals, DoITT has not provided any information to establish that it consulted with the Comptroller's Office or Borough Presidents regarding any proposals submitted to DoITT.

Inactive Accounts

The Interconnection Working Group Fund and the Municipal Cable Network Fund have been dormant for several years, and it appears that the purposes for establishing these funds have been fulfilled. As of December 31, 2003, the Interconnection Working Group Fund had a balance of \$437,167, and the Municipal Cable Network Fund had a balance of \$1,711.

According to Comptroller's Directive 27:

"If an agency determines that a Fiduciary Account is no longer necessary and the account is no longer legally required, the agency should immediately recommend its closure. . . . The closure proposal should provide the name and any remaining balance in the account, a confirmation that the remaining resources are no longer legally required to be held in a custodial account, the agency's recommendation as to the disposition of any remaining resources and any other pertinent information. All closing procedures must conform to the terms of the trust agreement, if specified."

Based on our review of the agreements and DoITT records, we are unable to determine the appropriate disposition of the funds in the dormant accounts. The City Law Department recommended that "the remaining funds in the account . . . be held by the City in a separate interest bearing account while the Department of Information Technology and Telecommunications ('DoITT'), acting promptly, determines whether (1) there are appropriate City uses for such funds pursuant to the applicable franchise agreements which appropriate City uses would exhaust such funds and, (2) if such funds would not be thus exhausted, what the appropriate final distribution of any remaining funds pursuant to the franchise agreement should be."

RECOMMENDATIONS

DoITT should:

1. Consult with the Borough Presidents and the Comptroller on future expenditures of I-NET funds. In that regard, DoITT should provide a list of proposed projects and related costs to the Borough Presidents and the Comptroller for comment.

DoITT's Response: Although DoITT's response did not fully address this recommendation it stated that "in the interest of on-going amicable and cooperative joint effort between DoITT and the Comptroller's Office, DoITT is prepared . . . to further discuss with the Comptroller's Office new procedures to be utilized in the future for the implementation of the contemplated 'consultation' as to I-NET expenditures. DoITT looks forward to fruitful discussions as to such future procedures."

2. Determine in conjunction with the City's Law Department, whether the Interconnection Working Group Fund and the Municipal Cable Network Fund are necessary and legally required. If not, the accounts should be closed in accordance with the provisions of Comptroller's Directive 27, and the funds should be disbursed in accordance with the Law Department's guidance.

DoITT's Response: DoITT's response did not address this recommendation.



DEPARTMENT OF INFORMATION TECHNOLOGY AND
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GINO P. MENCHINI
Commissioner

AGOSTINO CANGEMI
*Deputy Commissioner
Franchise Administration and
Planning/General Counsel*

April 12, 2004

Mr. Greg Brooks
Deputy Comptroller
Office of the New York City Comptroller
Policy, Audits, Accountancy and Contracts
One Centre Street
New York, New York 10007 - 2341

Re: Audit Report on the Administration
Of the Institutional Network and
Crosswalks Funds by DoITT
FM03-084A

Dear Mr. Brooks:

I write on behalf of Commissioner Menchini with this agency's comments on the March 29, 2004 draft "Audit Report on the Administration Of the Institutional Network And Crosswalks Funds by DoITT" (the "Draft Report").

DoITT agrees with and endorses the primary conclusion of the Draft Report, that "DoITT accurately records and tracks I-NET and Crosswalks revenue and expenses. In addition, DoITT ensured that funds were spent on items for I-NET and Crosswalks in accordance with the franchise agreements." See Draft Report, page 5.

However, DoITT strongly disagrees with the Draft Report's evaluation of DoITT's compliance with the commitment of DoITT to engage in "consultation" with the Comptroller and Borough Presidents regarding expenditures from the Institutional Network ("I-NET") fund. Prior to deciding how to direct such expenditures, DoITT solicited in writing the views of the Comptroller and Borough Presidents, received written suggestions from them, reviewed and discussed those suggestions, and took those suggestions into serious consideration. DoITT further offered to meet with the staff of the Comptroller's Office and Borough Presidents' Offices to discuss their respective recommendations, an offer that was accepted by the Comptroller's Office. DoITT staff and staff of the Comptroller's office met to discuss the

Comptroller's suggestions regarding I-NET expenditures and the goals of the I-NET project. DoITT took all of the Comptroller's and Borough Presidents' suggestions, both written and oral, into account in making final decisions as to how to direct expenditures of I-NET funds.

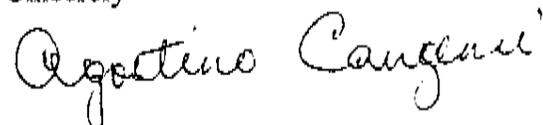
DoITT disagrees with both factual and interpretive observations in the Draft Report with respect to the "consultation" question. The Draft Report suggests that "DoITT merely sent letters to the Comptroller's Office and Borough Presidents['] Offices requesting proposals for future I-NET projects. These letters certainly fall short of the consultation required under the agreements". See Draft Report, page 5. Even if it were factually correct that DoITT activities in this respect were limited to "merely sending letters... requesting proposals" such would have been sufficient to meet the standard of "consultation". Webster's New Collegiate Dictionary defines "consult" as to "ask the advice or opinion of" and defines "consultation" as "the act of consulting or conferring." Even if DoITT had only sent letters to the applicable City officials asking their advice or opinion as to as to how to expend I-NET funds, such solicitation of advice or opinion would have been in accordance with the definition of consultation. But as a factual matter, DoITT engaged in an even more thorough consultation than the minimum required, beyond "merely sending letters" as suggested in the Draft Report. As discussed above, DoITT followed up its written solicitation of advice and opinion with additional discussion and consideration of views. DoITT urges the Comptroller's Office to revise the Draft Report so that a final audit report in this matter is amended to:

- (1) reflect as a factual matter the full scope of DoITT's interaction with the Comptroller's Office and Borough Presidents' Offices with respect to I-NET expenditures; and
- (2) reflect DoITT's view that it has complied with both the letter and the spirit of its commitment to engage in "consultation" as to I-NET expenditures with applicable City officials.

Regardless of DoITT's views as to the language of the Draft Report, however, in the interest of on-going amicable and cooperative joint effort between DoITT and the Comptroller's Office, DoITT is prepared (as it indicated in discussion with the auditors preparing the Draft Report) to further discuss with the Comptroller's Office new procedures to be utilized in the future for the implementation of the contemplated "consultation" as to I-NET expenditures. DoITT looks forward to fruitful discussions as to such future procedures.

Thank you for consideration of this matter and again thank you for your favorable analysis of DoITT's performance with respect to the main topic of the draft report, the proper handling of I-NET funds and the proper use of such funds for the purposes for which they were intended.

Sincerely



Agostino Cangemi

cc: Gino Menchini
Margery Brown