Hugh L. Carey Battery Park City Authority

Annual Post-Audit Report to the Audit Committee
(Under AICPA AU-C Section 260)

For the Audit Year Ended October 31, 2013

Marks Paneth & Shron LLP
Certified Public Accountants & Consultants
IT ALL ADDS UP.

Marks Paneth & Shron LLP
Certified Public Accountants & Consultants

January 16, 2014

To the Audit Committee and the Members of the
Hugh L. Carey Battery Park City Authority

In accordance with auditing standards generally accepted in the United States of America ("U.S. GAAS"), Marks Paneth LLP ("Marks Paneth" or "us" or "we" or "our") is pleased to provide this communication in compliance with the American Institute of Certified Public Accountants ("AICPA") Auditing Standards AU-C Section 260 "*The Auditor's Communication with Those Charged with Governance*." In your case, the Audit Committee (or "you"), on behalf of the Members, the party charged with governance, has the responsibility to oversee the external audit of the Hugh L. Carey Battery Park City Authority (the "Authority") and the Battery Park City Parks Conservancy (the "Conservancy), collectively referred to as the "Organization." Marks Paneth has a responsibility to bring to the attention of the Members, through the Audit Committee, any accounting, auditing, internal control, or other related matters that we believe warrant their consideration or action. Matters in this communication are concerning the completion of the October 31, 2013 financial statement audit.

This report is intended solely for the information and use of the Audit Committee, Members and management of the Organization, and is not intended to be and should not be used by anyone other than those specified parties, unless permission is granted.

Very truly yours,

Marks Paneth LLP

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Hugh L. Carey Battery Park City Authority
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For the Audit Year Ended October 31, 2013

1. Auditors' Responsibility

Our responsibility as the independent auditors is to express an opinion on the Organization's financial statements as of and for the year ended October 31, 2013 based on our audit. Also, it must be emphasized that our audit does not relieve management, and those charged with governance, of their responsibilities.

Our audit was conducted in accordance with auditing standards generally accepted in the United States of America ("U.S. GAAS") and was designed to obtain reasonable, rather than absolute, assurance about whether the financial statements are free of material misstatement. Our audit included tests of the accounting records of the Organization and other procedures we considered necessary to enable us to express an unmodified opinion that the financial statements are fairly presented, in all material respects, in conformity with accounting principles generally accepted in the United States of America ("U.S. GAAP"). In addition, we conducted our audit of the Organization under standards for financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States ("GAS").

Based on our audit, we are prepared to issue an unmodified opinion on the financial statements, subject to the following open items being cleared:

A) Receipt of signed management representation letter

B) Receipt of signed legal representation letter from the Organization's general counsel

C) Acceptance of the draft financial statements by the Audit Committee.

D) Additional post balance sheet review by Marks Paneth to bring our audit report date to that of the management representation letter date.

2. Timing and Meetings Relative to the Engagement

	2013	2012
I. Review – April 30		
a. Review fieldwork start	June 2013	June 2012
b. Exit meeting and draft deliverables discussion with management	July/August 2013	July/August 2012
c. Issuance of review report	August 14, 2013	September 10, 2012
II. Audit – October 31		
a. Engagement letter issued	May 29, 2013	November 29, 2012
b. Presentation of preliminary audit plan to the Audit Committee	November 19, 2013	January 8, 2013
c. Audit fieldwork start	December 9, 2013	December 10, 2012
d. Exit meeting and draft deliverables discussion with management	Mid January 2014	Mid January 2013
e. Presentation of draft financials to the Audit Committee	January 28,2014	January 29, 2013
f. Issuance of signed financials after approval by the Audit Committee	Late January 2014	January 29, 2013

3. Management's Responsibility

The Organization's management is responsible for making all financial records and related information available to us and for the accuracy and completeness of that information. We have advised you about appropriate accounting principles and their application and assisted in the preparation of your financial statements, but the responsibility for the financial statements remains with you.

The management of the Organization is responsible for establishing and maintaining internal controls. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of the controls. The objectives of internal controls are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, that transactions are executed in accordance with management's authorizations and recorded properly to permit the preparation of financial statements in accordance with U.S. GAAP.

In addition, management is responsible for the design and implementation of programs and controls to prevent and detect fraud, and for informing us about all known or suspected fraud affecting the Organization involving (a) management, (b) employees who have significant roles in internal control, and (c) others where the fraud could have a material effect on the financial statements. Management is also responsible for informing us of their knowledge of any allegations of fraud or suspected fraud affecting the Organization received in communications from employees, former employees, regulators, or others. In addition, management is responsible for identifying and ensuring that the Organization complies with applicable laws and regulations.

4. Selection, Application or Changes in Significant Accounting Principles

The Organization follows specific accounting policies for maintaining its net assets, postemployment benefits and the recognition of revenue. The principles are discussed in detail in Note 3 to the Organization's financial statements.

There was a new accounting standard promulgated by the Governmental Accounting Standards Board ("GASB") that was adopted by the Organization during the year ended October 31, 2013. In addition, there was a change in the method of accounting for the Organization's interest rate swap agreements in the current fiscal year as a result of the refunding of the Organization's Series 2003 bonds.

A) GASB Statement No. 65, "*Items Previously Reported as Assets and Liabilities,* ("GASB No. 65")," is effective for financial statements for periods beginning after December 15, 2012, with earlier application encouraged. GASB No. 65 clarified the appropriate reporting of deferred outflows and deferred inflows of resources to ensure consistency in financial reporting. In addition, GASB No. 65 required that all lease and debt issuance costs, except any portion related to prepaid insurance costs, be recognized as an expense in the period incurred.

The Organization elected to adopt the provisions of GASB No. 65 during its fiscal year ended October 31, 2013. In accordance with GASB No. 65, the Organization reclassified or expensed certain items that were previously classified as assets and liabilities. The Organization also retroactively applied this statement to prior periods and adjusted the beginning balance of net position (deficit) for the earliest period presented for all lease and debt issuance costs except prepaid insurance costs, which are being reported as an asset and recognized as an expense over the duration of the related debt. The effect of the adoption of GASB No. 65 was a reduction to the Organization's prior year net position of approximately $22.2 million. Accordingly, the October 31, 2012 financial statements were restated to reflect the adoption of GASB No. 65.

B) *Accounting and Financial Reporting for Derivative Instruments, Deferred Outflows and Inflows of Resources, and Net Position*

In accordance with GASB Statement No. 53, "*Accounting and Financial Reporting for Derivative Instruments* ("GASB No. 53")," the Organization evaluated the effectiveness of six interest rate exchange agreements ("Swaps"), determined that the swaps were effective hedges and recorded the negative fair value as a deferred outflow of resources for the accumulated decrease in the fair value of the interest rate swaps and a liability for fair value of the Swaps of approximately $106.7 million as of October 31, 2012.

On October 23, 2013, the Organization currently refunded its Series 2003 bonds. The interest rates on these bonds were effectively hedged by the Swaps, which were bifurcated as of the date of the current refunding. Accordingly, the fair value of the Swaps on October 23, 2013 of negative $70.1 million was recorded as an imputed borrowing by the Organization. The Organization also recorded the $70.1 million as a deferred cost of refunding and reduced the deferred outflow of resources that had been recorded to offset the negative fair value of the interest rate swap to zero. Apart from the imputed borrowing, the Swaps, which continue in effect and continue as an effective hedge, had a fair value of zero at October 23, 2013, which increased to $1.6 million at October 31, 2013. This amount is recorded as an asset and a deferred inflow of resources on the Organization's statement of net position.

The unamortized bond insurance costs for the 2003 Bonds, which were refunded on October 23, 2013, have now become a component of the unamortized loss on extinguishment, which is being amortized over the remaining life of the original bonds.

5. <u>Significant Management Judgments and Accounting Estimates</u>

The preparation of financial statements requires the use of accounting estimates, by which management uses its best judgment in the determination of certain amounts to be recorded in those statements. These amounts are calculated using all information available at the time and applying the knowledge and expertise of management. These amounts are subject to revision as time passes and more information becomes available. Matters to note are as follows:

A) Fair Value of Interest Rate Swap Agreements

Based on management's determination that the Swaps, which continue in effect after the refunding of the 2003 Series C Bonds in fiscal year 2013, were effective hedges, the Organization has recorded the fair value of approximately $1.6 million as of October 31, 2013 as both an asset and a deferred inflows of resources. The fair value was provided by the Organization's financial advisor and was derived from financial models based upon reasonable estimates about relevant market conditions.

Under the Swaps, the Organization is to pay the counterparties interest calculated at 3.452% of the notional amount (the outstanding principal balance) on the first of May and November of each year and the Organization receives interest from the counterparties calculated at 65% of the LIBOR rate. Marks Paneth noted that the fair value was determined by taking the net present value of future interest to be received from the counterparties and interest to be paid to the counterparties. Marks Paneth noted that the discount factor is calculated based on the LIBOR rate at October 31, 2013, the last business day of the Organization's fiscal year. Based on the procedures performed, the fair value of the Swaps recorded by the Organization appears reasonable.

B) OPEB Liability and Expense

In determining the amount of expenses and liabilities to be recorded for the postemployment benefits other than pension ("OPEB") in accordance with GASB Statement No. 45, "*Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions* ("GASB No. 45")," management, with the aid of an actuary, made assumptions or estimates for rates of return on assets and costs of health care premiums (healthcare cost trend rate). Based on these estimates, management has recorded the OPEB expenses and liabilities for these benefits.

GASB No. 45 permits a plan with less than 200 members, such as the Organization, to perform an actuarial valuation every three years. Accordingly, an updated actuarial valuation as of November 1, 2012 was necessary to reflect the Organization's OPEB liabilities as of October 31, 2013 and the related expenses for the year then ended.

Marks Paneth reviewed the qualifications of the Authority's actuary and the assumptions used by the actuary and found the factors used to be reasonable and in accordance with the provisions of GASB Statement No. 45. Marks Paneth also agreed the current year's OPEB costs and checked the accuracy of the rollforward of the OPEB liabilities to the actuarial valuation reports.

Based on our audit procedures, management's estimate of OPEB expenses and the related liabilities appears reasonable.

C) Recoverability Period of Project Assets

Depreciation of project assets is being provided for by the straight-line method over the estimated useful lives of the related assets, which are the remaining lease years (to 2069) for site improvements, 50 years for residential building and through the first appraisal date of each lease for condominium units. The recoverability period used by management appears to be reasonable.

6. <u>Significant Recorded and Proposed Unrecorded Audit Adjustments</u>

We are required to inform the Audit Committee about adjustments or misstatements arising from the audit that could, in our judgment, either individually, or in the aggregate, have a significant effect on the Organization's financial reporting process.

Adjusting journal entries recorded:

There were none.

Uncorrected misstatements due to non-materiality:

There were none.

7. <u>Significant Issues Discussed, or Subject to Correspondence, with Management</u>

Throughout the year, routine discussions regarding the application of accounting principles or auditing standards were held with management in connection with transactions that have occurred, transactions that are contemplated, or reassessment of current circumstances. In our judgment, such discussions were not held in connection with our retention as auditors.

8. Disagreements with Management and Audit Difficulties

For purposes of this letter, professional standards define a disagreement with management as a financial accounting, reporting or auditing matter, whether or not resolved to our satisfaction that could be significant to the financial statements or the auditors' report. We are pleased to report that no such disagreements arose during the course of our audit. We received the full cooperation of management and staff throughout the process of performing our audit procedures.

9. Fraud or Likely Illegal Acts/Conflict of Interest Matters/Other Governance Issues

Our audit procedures did not detect any such items. We advise all our clients that there is always a risk that fraud or illegal acts may exist and not be detected by any audit firm in performing an audit.

We understand that the Authority has adopted a Code of Ethics for its employees and its Members, and there is an Ethics Officer whose responsibility is to ensure compliance with the Code of Ethics.

10. Internal Controls: Control and Significant Deficiencies and Material Weaknesses

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis.

A deficiency in *design* exists when a control necessary to meet the control objective is missing; or an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met.

A deficiency in *operation* exists when a properly designed control does not operate as designed; or the person performing the control does not possess the necessary authority or competence to perform the control effectively.

A *significant deficiency* is a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

A *material weakness* is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

We did not observe any material weaknesses as a result of our audit (see Tab 3). However, we made certain recommendations and suggestions, which, if implemented, could further strengthen the internal controls and business practices. We communicated these matters in the separately issued letter disclosing the observations and recommendations relating to the Organization's information technology environment (see Tab 5).

11. Consultation with Other Accountants

We are not aware of any consultations with other accountants about auditing and accounting matters during the year ended October 31, 2013.

12. Auditor Independence

We affirm that Marks Paneth is independent with respect to the Organization in accordance with the AICPA's *Code of Professional Conduct.*

13. Future Deliverables to be Issued and Other Matters

A) Future Deliverables to be Issued

Form 990: The original due date for the Conservancy's Federal Form 990 is March 15, 2014 and we anticipate the Form 990 will be filed with the Internal Revenue Service prior to the initial due date. We expect to issue a draft Form 990 to the Conservancy for its review in February 2014 provided that the necessary tax return information is received from the Conservancy's management.

B) Other Matters

I. Contingencies

The Organization's management, general counsel and outside legal counsel have advised us of several pending or threatened litigation matters. Such matters are disclosed in Notes 20 and 22 to the Organization's financial statements.

II. Other

We have read certain tax and other government filing items to ensure that they have been filed timely, including the payroll tax filings (IRS Forms 941, W-2 and 1099). However, we caution you that it is not our practice to look at all potential filings the Organization may be required to complete. We are unaware of any tax or other governmental filing exposure items.

14. Industry Updates

See the pre-audit presentation to the Audit Committee on November 19, 2013. New industry updates subsequent to the November 19, 2013 pre-audit presentation that might be significant to the Organization are summarized below.

A) New York State Nonprofit Revitalization

On June 21, 2013, the New York State Assembly and the Senate passed the "Nonprofit Revitalization Act." The Act was signed into law by Governor Cuomo on December 19, 2013, with most provisions taking effect on July 1, 2014.

Some of the more significant provisions are as follows:

Audit Requirements:

- Threshold for audit increased to annual revenues of greater than $500,000 with a phase-in to a $1,000,000 threshold by 2021.
- Requirement for establishment of audit committee consisting of independent directors (or the independent directors of the board must function as the audit committee) to:
  - oversee audit process,
  - communicate with the auditor,
  - retain auditor, and
  - implement and oversee governance policies.

- For organizations with greater than $1,000,000 in annual revenue; the audit committee is also responsible for:

  - reviewing the scope and planning of audit with the auditor;
  - discussing the audit findings, including internal control concerns with auditor; and
  - reviewing performance and independence of auditor (annually).

Governance Requirements:

- Electronic and videoconferencing communications permitted, including conduct of board meetings.
- Elimination of board approval requirement for entering into ordinary leasing transactions.
- Permit majority of committee approval (rather than full board) for non-substantial property transactions.
- Prohibit employees from serving as chair of board.
- Eliminate the public notice requirement for private foundations.
- Mandate requirements for conflict of interest policies for all organizations to be affirmed annually
- Determination by board that related-party transactions are reasonable (in certain circumstances, enhanced procedures and documentation required).
- Related party cannot be present during board deliberations regarding potential transactions.
- Mandate whistleblower policy for certain sized organizations.
- Deliberations of compensation arrangements must be made without party in question present.

B) Form 990 – Changes for 2013

Part VI Independent Director

Independent director compensation continues to be an issue. If the director is compensated in the capacity as a director and the compensation is reasonable, then the director's independence is not impaired. However, if the director is paid as an officer or employee, or over $10,000 for services as an independent contractor, then the director is not independent. If a director is paid over $600 it must be reported on Form 1099-MISC. Whether reimbursable expenses are accounted for as compensation or not depends on whether the organization has an accountable reimbursement policy. If directors are given an "allowance" for which they do not have to account, it would be reported as compensation described above. If the reimbursement is accountable, i.e., reported through an expense report, then it would not be treated as compensation.

Revocation of Exempt Status

In January of 2014, the IRS issued Revenue Procedure 2014-11 outlining revised procedures for organizations that lost their exemption as a result of the Pension Protection Act. The loss of exemption is the result of not filing or reporting for a three-year period. The IRS is following a procedure where the three-year period begins on the date of incorporation and not on the date the Employer Identification Number ("EIN") was issued or the organization began to do business or hold assets.

Significant Changes and Concerns

- A short period return cannot be filed electronically unless it's an initial or final return for which the "Initial Return" or "Terminated" box is checked in Item B of the Form 990 heading.

- If a Form 990-N filer changes its accounting period, it must report this change either on Form 990/990-EZ or Form 1128.
- Returns with a name change can only be paper filed. In addition, corporations must submit a copy of the amendment to the articles of incorporation and proof of filing with the appropriate state authority.
- Clarification has been provided on which donors can be left off Schedule B based on the$5,000/>2%. Only organizations described under Code section 509(a)(1) and reported in Part II of Schedule A can avail themselves of the 2% rule, whereby only donors giving more than the greater of $5,000 or 2% have to be reported. Organizations meeting the Code section 509(a)(2) definition can only avail themselves of the $5,000 rule.
- Line 25b instructions, Part IV, have been clarified when an organization needs to answer "Yes" to report that it became aware of an excess benefit transaction with a disqualified person in prior years. If prior to filing a return (including extensions), an organization discovers that there has been an excess benefit transaction in a prior year, then 25b should be answered "Yes."
- Line 26 instructions, Part IV, have been clarified that an organization must file Schedule L, Part II, if it reported any amounts on Part X, lines 5, 6 or 22 for receivables from or payables to interested persons. Questions 26 -28 are mandatory and require additional disclosure on Schedule L.
- Instructions for Part VII, compensation of Officers, Directors, Trustees, Key Employees, Highest compensated Employees, and Independent Contractors:

    - Clarify that director's compensation for non-director independent contractor services to the organization and related organizations must be reported in Part VII, Section A. Also, corporate directors are considered independent contractors, not employees, and director compensation, if any, generally is required to be reported on Form 1099-MISC.
    - If a voting director of the organization is to be compensated by the organization for services unrelated to his/her services as a director, then that compensation would appear in Section A.
    - Clarify that compensation from a management company to one of the organization's officers, directors, trustees, key employees, or highest compensated employees is generally not reportable in Part VII, Section A. (Warning: New York bases the classification on common law employee status which may be different from the Federal interpretation).

<u>Other Miscellaneous Changes</u>

- Line 1 instructions for Part VIII, Statement of Revenue, clarifies that discounts on services cannot be reported as contributions.
- Line 11 instructions for Part IX clarify how to report expense payments and reimbursements to contractors. If the organization is able to distinguish between fees paid for independent contractor services and expense payments or reimbursements to the contractor, report the fees paid for reimbursements on the applicable lines in Part IX (including line 24 if no other line is applicable). If the organization is unable to distinguish between service fees and expense payments or reimbursements, report all such amounts on line 11.
- Clarifies and "reinforces" that contributions include neither donations or services nor discounts provided on sales of goods in the ordinary course of business.

15. New Accounting and Auditing Matters on the Horizon

See the pre-audit presentation to the Audit Committee on November 19, 2013. New accounting and auditing matters subsequent to the November 19, 2013 pre-audit presentation that might be significant to the Organization are summarized below.

A) **GASB Statement No. 71, "*Pension Transition for Contributions Made Subsequent to the Measurement Date – An Amendment of GASB Statement No. 68* ("GASB No. 71"),"** eliminates a potential source of understatement of restated beginning net position and expense in a government's first year of implementing GASB Statement No. 68, "*Accounting and Financial Reporting for Pensions* ("GASB No. 68")." To correct this potential understatement, GASB No. 71 requires a state or local government, when transitioning to the new pension standards, to recognize a beginning deferred outflow of resources for its pension contributions made during the time between the measurement date of the beginning net pension liability and the beginning of the initial fiscal year of implementation. This amount will be recognized regardless of whether it is practical to determine the beginning amounts of all other deferred outflows of resources and deferred inflows of resources related to pensions.

The provisions are effective simultaneously with the provisions of GASB No. 68, which is required to be applied in fiscal years beginning after June 15, 2014. The Organization has not completed the process of evaluating the effects of GASB No. 68 and GASB No. 71 on its financial statements.

****END****