



OFFICE OF THE CITY AUDITOR
COLORADO SPRINGS, COLORADO

15-31 Colorado Springs Urban Renewal Authority

November 2015



OFFICE OF THE CITY AUDITOR COLORADO SPRINGS, COLORADO

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15-31 Colorado Springs Urban Renewal Authority Audit

November 2015

Purpose

The purpose of the audit was to assess the internal controls used in day-to-day operations and transactions of the Colorado Springs Urban Renewal Authority (CSURA). Information was gathered concerning the effectiveness of the Authority as compared to similar organizations.

Highlights

We concluded that day-to-day operations and transactions of the CSURA utilized reasonable internal controls. A third party accounting firm was used for bookkeeping and financial statement preparation. We identified internal control improvement opportunities in the form of policies and procedures to ensure consistency and accountability. The CSURA Board and contractors have been very cooperative in this audit and we appreciate their assistance.

All urban renewal projects located within the boundaries of the City of Colorado Springs must be approved by City Council and developers must comply with standard development review processes. Approval to use sales tax as Tax Increment Financing must be approved by City Council. The City Council resolutions provide governance, accountability, transparency, and reporting on the use of incremental sales tax dollars associated with redevelopment activities.

In Colorado Springs, typically, TIF funds were used for public infrastructure improvements that support Urban Renewal plans such as the redevelopment of North Nevada Avenue. There were nine urban renewal areas approved by City Council represented on the current financial statements for CSURA. We reviewed various aspects of these projects to arrive at our conclusion on daily operations.

Three observations and four opportunities for improvement were identified. Details can be found in the attached report. Best practices and benchmarked activities of similar organizations were utilized in our conclusion and recommendations.

Management Response

Management was in agreement with our recommendations. Their complete responses can be found in the attached report.

Recommendations

1. CSURA should amend current written procedures for initiation and closure of incremental tax collection.
2. City management should include a right to audit clause in CSURA agreements.
3. CSURA and City management should coordinate to develop more accurate average actual sales tax data.

Opportunities for Improvement

1. Utilize performance metrics to measure Director's productivity.
2. Develop and utilize a checklist to review contract terms and conditions.
3. Utilize third-party cost estimation in negotiations.
4. Utilize performance metrics to measure project success.

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REPORT DETAILS

SCOPE AND OBJECTIVE

The purpose of the audit as stated in the 2015 Audit Plan was to assess the internal controls used in day-to-day operations and transactions of the Colorado Springs Urban Renewal Authority (CSURA). Information was gathered concerning the effectiveness of the Authority as compared to similar organizations.

CONCLUSION

We concluded that day-to-day operations and transactions of the CSURA utilized reasonable internal controls. A third party accounting firm was used for bookkeeping and financial statement preparation. We identified internal control improvement opportunities in the form of policies and procedures to ensure consistency and accountability.

During the course of the audit we identified three observations and four opportunities for improvement. These areas are discussed beginning on page 7 of this report. The CSURA Board, contractors and City staff have been cooperative in this audit and we appreciate their assistance.

BACKGROUND

According to the Colorado Springs Urban Renewal Authority's web site:

The Colorado Springs Urban Renewal Authority (CSURA) was established by the City of Colorado Springs City Council in 1970 through the approval of Ordinance No. 3995. CSURA is a tool to assist with the restoration and redevelopment of specified areas determined to meet the State Statutes for blight. CSURA projects encompass coordinated partnerships of private and public entities, financial institutions and the use of tax increment financing.

CSURA is a 9-member board appointed by the Mayor of Colorado Springs and approved by City Council members. There is a 5 year term for each member. CSURA is governed by Colorado State Statutes. CSURA has no employees and operates using contract services overseen by the board.

When CSURA partners with a private developer and provides assistance to help finance redevelopment of a blighted property in Colorado Springs, the main tool it uses is called tax increment financing or TIF. TIF is a mechanism to capture the net new or incremental property taxes created when a vacant or underutilized property is redeveloped and use those revenues to help finance the project for up to 25 years. Projects that generate sales tax revenue may also include the tax increment with the approval of Colorado Springs City Council. A redevelopment agreement between CSURA and the developer is negotiated that lays out the specifics for which



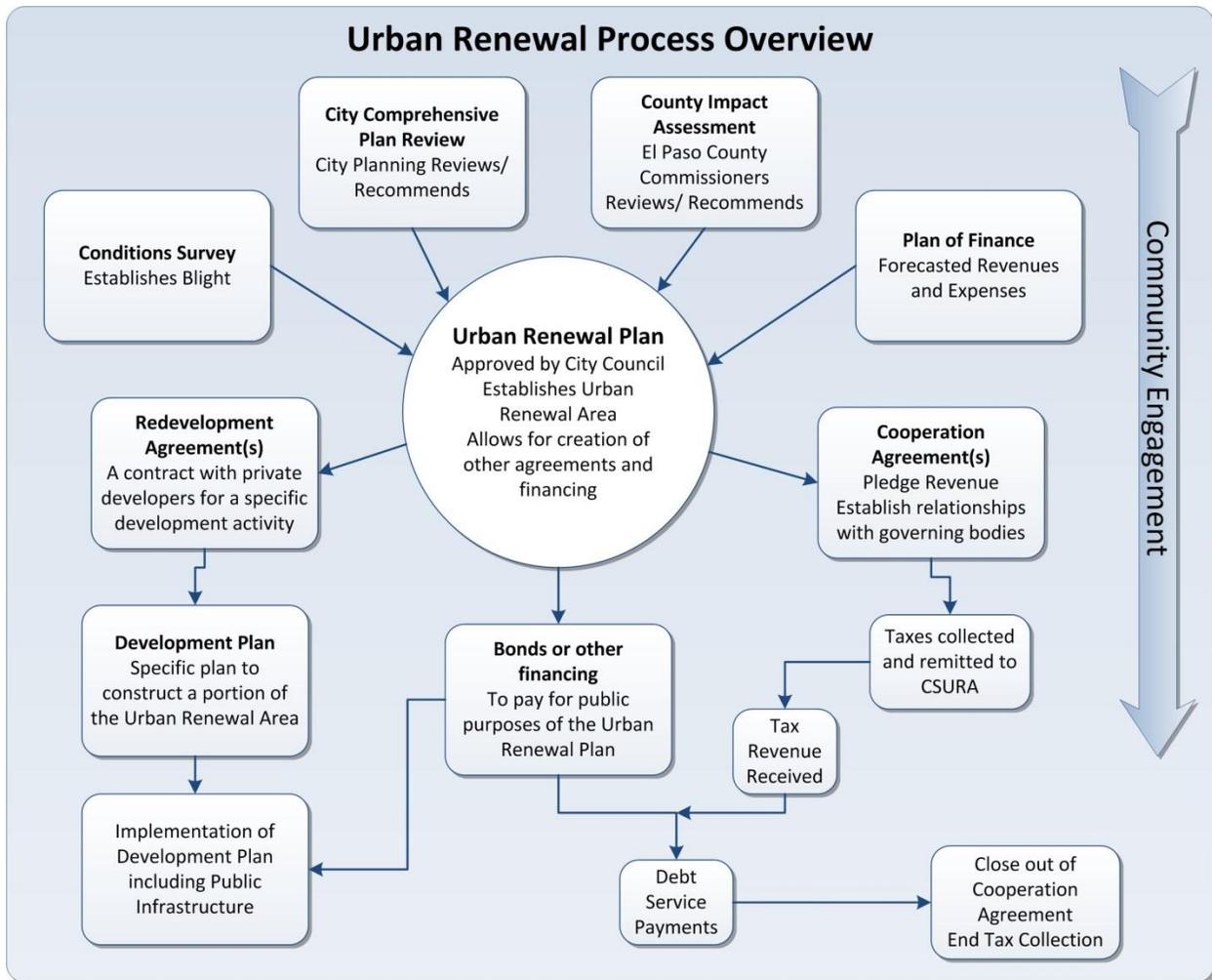
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developer incurred qualified expenses will be eligible for reimbursement as well as the total amount of increment that will be paid.

The mission of the CSURA is to encourage private investment and reinvestment which restores targeted areas with strong community benefits while strengthening the tax base of the whole city. The objective of CSURA is to facilitate development of balanced, sustainable environments where people live, work, and come together as community.

OVERVIEW OF URBAN RENEWAL PROCESS

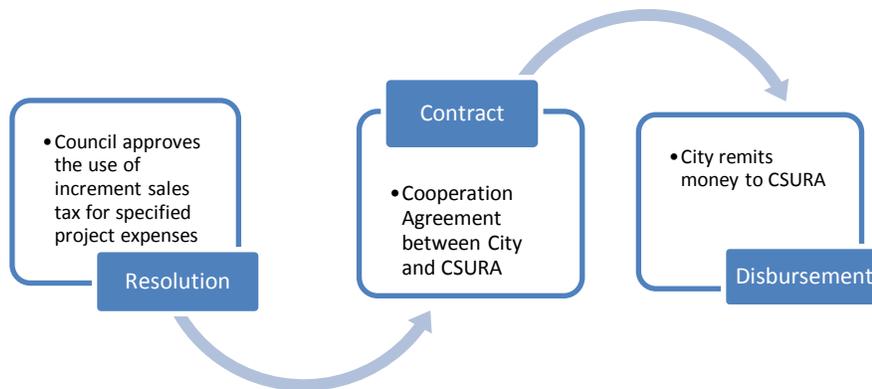
The following graphic depicts the process in place for CSURA at the time of the audit.





RELATIONSHIP BETWEEN CSURA AND THE CITY OF COLORADO SPRINGS

All urban renewal projects located within the boundaries of the City of Colorado Springs must be approved by City Council and developers must comply with standard development review processes. Approval to use sales tax as Tax Increment Financing (TIF) must also be approved by City Council. Outside of the approval for either the urban renewal plan or the TIF, CSURA’s statutory status as a separate legal entity limits the City’s authority. Approved urban renewal plans, as required by statute, are first memorialized in the form of a resolution passed by City Council. The approval of the urban renewal plan allows CSURA to collect incremental property tax. Projects that generate sales tax utilized for eligible capital improvements require the additional approval of the Colorado Springs City Council through a second resolution which authorizes the City staff to enter into a Cooperation Agreement with CSURA. Both the signed resolutions and the Cooperation Agreement provide a nexus to ensure governance, accountability, transparency, and reporting on the use of increment sales tax dollars associated with redevelopment activities.



In Colorado Springs, typically, TIF funds were used for public infrastructure improvements that support the development, rather than direct development costs. Examples include redevelopment of North Nevada Avenue and the collection of funds to assist in the construction of Powers Boulevard near Copper Ridge, also known as Polaris Pointe.

We also noted during our audit that certain City departments coordinated with the CSURA:

Process:	City Departments/Actions:
Identification of an urban renewal project area:	Review by City Planning. Approval by City Council via a resolution
Engineering development review/inspection:	Standard development review process by City Engineering. Acceptance of public infrastructure follows standard development process
Approval for use of City Sales Tax:	Approval by City Council via a resolution resulting in a signed Cooperation Agreement

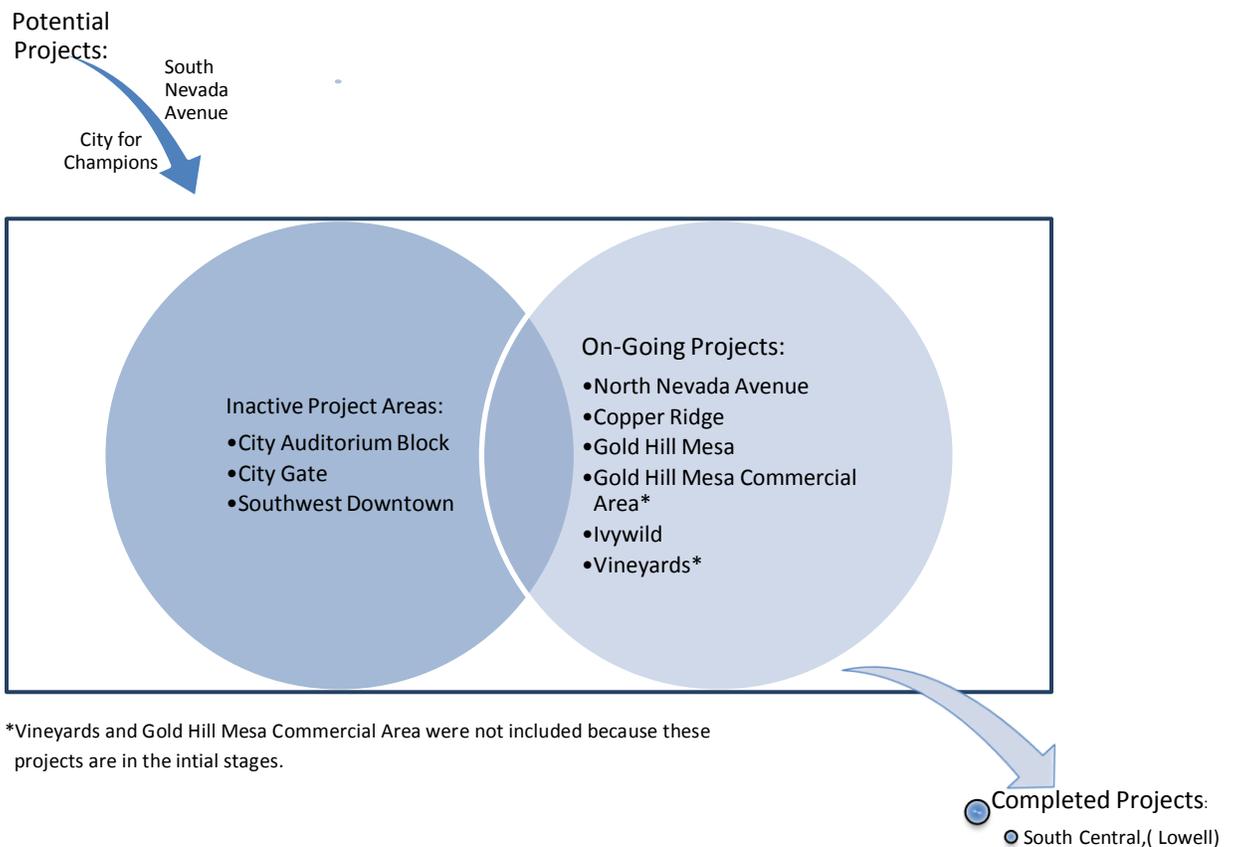


RELATIONSHIP BETWEEN CSURA AND THE DEVELOPER

After City Council has approved an urban renewal plan, CSURA can negotiate a Redevelopment Agreement with the selected developer(s), which lays out the specifics for which developer incurred qualified expenses will be eligible for reimbursement, as well as the total amount of tax increment that will be paid. In accordance with the state statute, a 25-year clock is set for each urban renewal project and that period begins with the approval of an urban renewal plan and the recording of the approved plan with El Paso County Clerk and Recorder. TIF can be collected and disbursed as reimbursement for allowable expenses for a maximum of 25 years.

CSURA PROJECTS BY STATUS

A total of nine urban renewal areas approved by City Council were represented on the 2014 financial statements for CSURA. CSURA was receiving incremental sales tax on three project areas: North Nevada Avenue, Copper Ridge, and Ivywild. All nine were also supported by incremental property tax administered through the El Paso County Assessor’s Office.



South Central (Lowell) expired as a TIF area in 2013, but will remain on CSURA’s financials for a short duration after closure for financial reporting reasons.



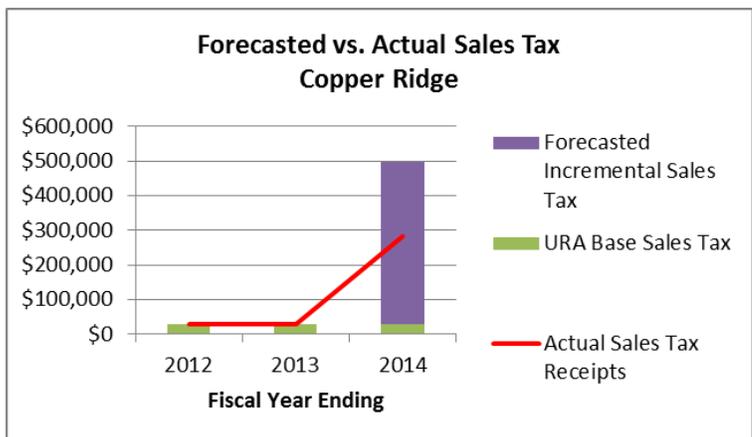
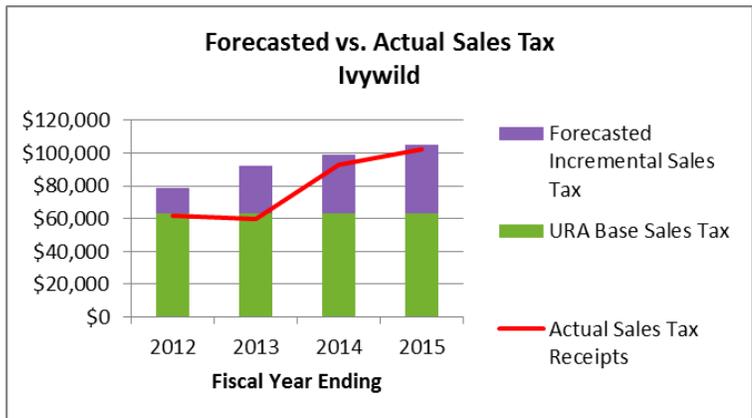
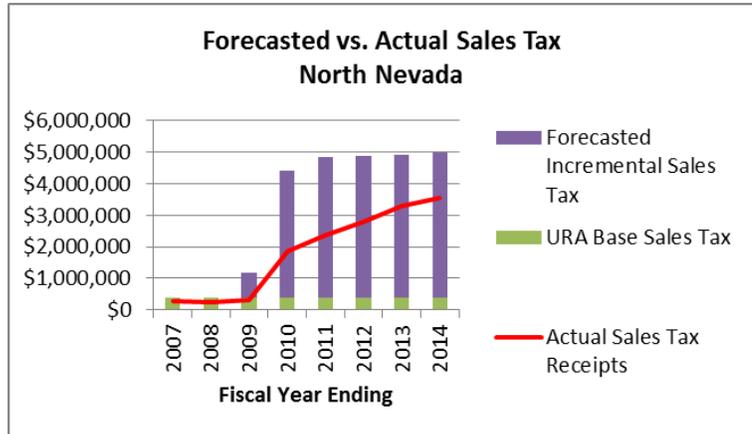
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PROJECTS FUNDED WITH CITY SALES TAX

Incremental tax revenue to be generated from the urban renewal areas was forecast by consultants for the CSURA as part of the development planning process. The base sales tax was also calculated as the amount of sales tax revenue the Urban Renewal Area would generate “but for” the project being considered. The base sales tax amount was retained by the City each year and the CSURA only received sales tax revenue which exceeded this base amount. Per the cooperation agreements with the City, sales tax and property taxes were pledged for financing the projects. CSURA has issued bonds for one urban renewal project, North Nevada Avenue. Per the bond indenture documents for North Nevada URA and other related financing documents, it was clearly stated that the City of Colorado Springs would not be responsible for any defaults on the bonds. Due to time and scope limitations, the OCA only reviewed the collection of incremental City sales taxes for this audit. Property taxes were not evaluated.

Forecasts were created in advance of the actual development of each area. Projected to actual incremental sales tax shortfall to date has been influenced by unanticipated factors, such as the economic downturn in 2008 and the developer’s ability to start construction according to schedule. Delays in beginning the project negatively impact the project life-to-date collected incremental tax revenue.

When considered on a life-to-date basis, all three projects have resulted in increased sales tax collections. However, the three projects have realized less incremental sales tax revenue than initially forecasted. In the cases of North Nevada and Ivywild, it





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appeared these projects were starting to come closer to the initial forecasts. Copper Ridge only has one full year of sales tax collections.

ADDITIONAL FINANCIAL OBLIGATIONS BETWEEN CSURA AND CITY OF COLORADO SPRINGS

In addition to our review of the current projects receiving incremental sales tax dollars, we reviewed other financial obligations between the two organizations. On July 10, 1990 CSURA entered into a loan agreement with the City of Colorado Springs in the amount of \$846,988 to bridge the financing needs of the South Central Lowell Urban Renewal Project. The Urban Renewal Plan for the Lowell development anticipated collection of up to \$11 million in incremental property tax to be used to reimburse the developer for costs associated with infrastructure. The loan was evidenced by a noninterest bearing promissory note and was subject to certain conditions and restrictions regarding the use of proceeds. Because repayment of the loan was exclusively from net property taxes received in excess of debt service obligations, and statutorily limited to 25 years, in 2015 the City of Colorado Springs wrote off the entire debt as unpaid and uncollectable.

On January 2009, CSURA entered into a Memorandum of Understanding (MOU) with the City of Colorado Springs with regard to sales tax base amount as it relates to the 2008 Bond issuance for North Nevada Avenue. The authority agreed that the City had previously overpaid CSURA with respect to sales tax increment and had agreed to repay the City \$158,474. The parties have agreed that the amount shall bear interest at the rate of 5% compounding annually until paid in full. This MOU was subordinate to the existing revenue bonds which were also behind in their scheduled repayment. Therefore, as of December 31, 2014, no payments had been made to the City under this agreement.



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OBSERVATION 1 – CSURA HAD NOT DEVELOPED A WRITTEN PROCEDURE FOR FINANCIAL CLOSE OUT OF AN URBAN RENEWAL PROJECT

We verified CSURA verbally notified the El Paso County Assessor's Office and the City Sales Tax Office when the Lowell Development 25-year TIF period ended. We identified that the current written procedures for the CSURA did not include requirements for written notification of initiation or closure of incremental tax collection for an urban renewal area. Our benchmarking, as well as review of best practices, indicates that the initiation and financial close out of a project would best be handled via written communication for documentation purposes. The close out of a project could also include the reconciliation/closeout of the project area fund. Without a formal written close out process the potential for the CSURA to over collect taxes is possible.

AUDITOR'S RECOMMENDATION

We recommend that CSURA amend their current written procedures to include the written notification for initiation and closure of increment tax collection. The close out process should include written notification to the entities from which funds were received.

MANAGEMENT RESPONSE

The CSURA Board agrees with the recommendation. Management will develop a written policy establishing notification procedures and closeout requirements in coordination with the El Paso County Assessor's Office for property tax increment collection periods and the City Sales Tax Office with regards to sales tax collection periods.

C.R.S. 31-25-107 requires notification to the County Assessor's Office by the "Municipality" on the approval or modification of an urban renewal plan as well as completion of financial obligations and the purpose of the authority have been achieved for the URA.

Implementation is expected by May 31, 2016.



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OBSERVATION 2 – A RIGHT TO AUDIT CLAUSE WAS NOT INCLUDED IN THE COOPERATION AGREEMENT

The Cooperation Agreement signed by the CSURA and the City authorizing the use of incremental sales tax revenues did not include a right to audit. The right to audit sales tax funds exists by virtue of City Code. The Cooperation Agreement is signed by both the City and CSURA. The Council resolution authorizing CSURA TIF funding included language that the CSURA and City would verify all costs and expenditures undertaken with TIF revenues. However, the resolution is not signed by the CSURA. Without a mutually authorized right to audit clause, there could be a misunderstanding of the City's right to validate use of funds.

AUDITOR'S RECOMMENDATION

We recommend that City management include a right to audit clause in CSURA Cooperation Agreements where City revenues are involved.

MANAGEMENT RESPONSE

City management acknowledges the recommendation and will include a right to audit clause in future CSURA Cooperation Agreements where City revenues are involved.

The CSURA Board agrees with the recommendation. CSURA will draft the Cooperation Agreements and the City will submit its preferred language for an audit right to be included in the Agreement



OBSERVATION 3 – ACTUAL SALES TAX COLLECTIONS WERE BELOW FORECAST

Incremental tax revenue to be generated from the urban renewal areas was forecast as part of the development planning process in advance of the actual development of each area. The forecasts, created using national industry guidelines, were for the anticipated sales to be generated from the type of development expected in the urban renewal area. Apart from information presented in the financial statements, there were no regular reports or comparisons made between the forecasted and actual taxes collected.

Actual sales and tax collections from specific retailers is confidential information. Therefore, the City Sales Tax office could not release detailed data on performance of a specific retailer to the CSURA for analysis. However, we identified the possibility for various City departments to coordinate on developing better data that would more accurately reflect the local market and provide more realistic forecasts for future projects.

The forecasted incremental tax revenue was pledged toward the repayment of bonds and/or loans incurred to construct infrastructure. If the forecasts are not accurate, the associated debt may not be repaid according to the planned debt service schedule.

Three CSURA projects which utilized sales tax incremental financing (TIF) were reviewed to compare actual to forecasted sales tax collections. All three projects were below forecast both on a life-to-date basis and compared to the fiscal 2014 year-end data. As stated elsewhere in this report, the trend in sales tax revenue appeared to be increasing for North Nevada and Ivywild. Copper Ridge has too little actual sales tax collection history to evaluate a trend.

Forecast to actual sales tax collected		
As a % of amount forecasted		
Project	Project life-to-date	Fiscal year 2014
North Nevada	50%	70%
Ivywild	56%	82%
Copper Ridge	26%	54%
Note – Sales tax collection periods do not necessarily match calendar years and were not the same for all projects. The reported periods reflect the most recent full 12 months of data that was available.		

For bonds that cannot be repaid within the 25 year statutory timeframe, tax collections could continue until the bond holders are fully repaid if the Urban Renewal Plan provides for the time frame to be extended or if the City Council agrees to modify the plan. As mentioned above, the City is not under any obligation in the event CSURA defaults on these bonds.



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The Lowell development project, however, was partially financed using a bridge loan from the City to the CSURA. The forecasted revenues from that development were not sufficient to repay the debt and in 2015 the City of Colorado Springs wrote off the entire outstanding balance of \$846,988 as unpaid because the 25 year period had expired. This loan was between the CSURA and the City. The City continues to collect property taxes from the development area as part of its normal tax collections.

AUDITOR'S RECOMMENDATION

We recommend that the Colorado Springs Urban Renewal Authority and the Office of Economic Development work with the City Finance department to develop more accurate average actual sales data by retailer type and size to be used for comparison when evaluating the potential incremental tax revenue from a proposed development.

MANAGEMENT RESPONSE

The CSURA Board agrees with the recommendation. The assistance of the OED and the City Finance Department in compiling local sales tax data will increase the reliability of financial models. More specificity on retail performance and sales tax revenue will also enable better assessment of actual performance vs. projections. An implementation date has not been determined.



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OPPORTUNITY 1 – THE CONTRACT FOR THE COLORADO SPRINGS URBAN RENEWAL AUTHORITY’S DIRECTOR DID NOT INCLUDE PERFORMANCE MEASURES

The CSURA’s Board of Directors utilizes an independent contractor to represent the CSURA and act as their Executive Director. The contract did not include performance goals or an annual review process. Some of the URAs contacted for this audit retained municipal employees for the position of director rather than utilizing independent contractors. These benchmarked organizations each included some expectations of performance measurement and/or an annual review for their directors. Because the CSURA contract was with an independent contractor, it was more general in nature than might be expected for an employee. However there are ways to improve the contract to provide clear communication of goals and measure accomplishments without violating the independent contractor’s status.

AUDITOR’S RECOMMENDATION

We recommend the CSURA utilize performance metrics to establish expectations and measure the Executive Director's productivity and efficiency.

MANAGEMENT RESPONSE

The CSURA Board agrees with the recommendation. The Executive Director’s current contract will be considered for renewal in 2016. CSURA will establish performance metrics for the Executive Director as part of the contract conditions that will be established during 2016.



OPPORTUNITY 2 – INCONSISTENCIES WERE NOTED BETWEEN FOUR URBAN RENEWAL DEVELOPMENT AGREEMENTS

CSURA utilized written Redevelopment Agreements to document the plans for work to be done on each project. These agreements were executed between the developer and the CSURA. Each development agreement was negotiated with legal representation protecting the interests of CSURA. The intent is to continue this process in the future.

Although projects have unique aspects, we reviewed and compared four development agreements for consistency. We identified several instances where the terms of the contracts were inconsistent. For example, we found that two of the four contracts contained a requirement for the CSURA to complete a “Certificate of Completion” acknowledging the contractor’s completion of required activities. Three of the four contracts included a change control process.

The unique aspect of each project may warrant variation of certain terms. However, best practices suggest the utilization of a checklist to document consideration and intent when leaving certain terms out of a contract. For example, a project where the developer is not being asked to build anything might warrant leaving out a “Certificate of Completion”. A checklist could also provide assurance to CSURA Board of Directors that the necessary terms were adequately addressed in the contracts.

AUDITOR’S RECOMMENDATION

We recommend the CSURA develop and utilize a checklist to ensure terms and conditions are standardized for future development agreements.

MANAGEMENT RESPONSE

The CSURA Board agrees with the recommendation. CSURA currently utilizes a standard format for development agreements. A checklist will be developed that will be reviewed at the initiation of each new development agreement to determine the appropriate sections to be included. Since each development activity or project presents unique circumstances, the agreements will be modified as necessary.



OPPORTUNITY 3 – PROPOSED PROJECT COSTS DID NOT ALWAYS HAVE THIRD PARTY REVIEW

A representative of the CSURA appropriately negotiated the projects that would be funded subject to City Council approval through TIF funding. In each of the four projects reviewed, TIF funds were used for public improvement and infrastructure. The projects were necessary for viability of the overall commercial project success.

The project cost and scope of work was included in the development agreement between CSURA and the developer. Our review noted the proposed TIF funded costs were not always reviewed by an independent third party prior to the negotiation of the contract. An independent review of proposed costs based upon work to be performed would ensure that funds were used effectively, were reasonable, and reflect current construction costs.

We validated that CSURA had a process to ensure developers spent the total funds required by the contract by utilizing a third party. If costs for a particular item were underspent the developer would be required to fund additional public improvements equal to the total amount specified in the contract, or could fund other project cost categories, provided the total reimbursement obligation was not increased.

AUDITOR’S RECOMMENDATION

We recommend that the CSURA include independent cost estimation for work to be performed in their administrative processes and negotiation with the developer. This information should be provided to City Council when a resolution for sales tax funding is before them.

MANAGEMENT RESPONSE

The CSURA Board agrees with the recommendation. CSURA will continue to utilize independent consultants as required to analyze various aspects of project financing and implementation depending upon the type and complexity of the development activity. Project invoices are approved by a third party project manager or engineer prior to payment authorization by CSURA. This will be uniformly applied to all development projects in the future.

City for Champions expenses funded through the RTA grant require the certification of all costs as “qualified expenses” by an independent auditor.



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OPPORTUNITY 4 – DOCUMENTED PROJECT MANAGEMENT PROCESSES WERE NOT IN PLACE

The Colorado Springs Urban Renewal Authority website lists eight goals:

- Cure blight
- Promote projects which provide public benefit
- Be proactive- player versus performer
- Create quality sustainable places
- Raise standards of development
- Create jobs
- Promote public art
- Facilitate delivery of affordable housing

In connection with the approval of an urban renewal plan, City Council authorizes the use of Property Tax, and potentially Sales Tax, increment to achieve these goals. The authority should ascertain the extent to which each of the project areas help support the goals and objectives of the organization and measure the success of the project against the greater goals of the CSURA. The purpose in measuring the projects against performance goals would be to document and support the ongoing mission of the CSURA. The overall goal of this objective should be promoting continuous improvement in operations of the CSURA.

Reporting of project performance was intermittent. Without meaningful performance metrics, managers could find it difficult to evaluate projects, processes, or individuals. Organizations that measure and manage performance are more likely to achieve operational and financial goals.

AUDITOR'S RECOMMENDATION

We recommend that CSURA develop performance metrics which assess the success of a project. The performance metrics should tie back to the mission of the authority. The objective should be promoting continuous improvement in the operations of the organization. As an implementer of the City's approved Urban Renewal Plan, the CSURA should consider developing some method of regularly reporting on metrics back to the City of Colorado Springs on the progress of each project.

MANAGEMENT RESPONSE

The CSURA Board agrees with the recommendation. CSURA will periodically publish economic impact reports for the active urban renewal areas to measure the effectiveness of the development activity in leveraging public funds to private investment, job creation potential as well as current and future tax revenue generated. Periodic project status reports which include the goals and objectives for each



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urban renewal plan are currently provided to City Council as well as the CSURA Board on a regular basis and will continue to be presented for discussion at CSURA Board meetings.

CITY COUNCIL'S OFFICE OF THE CITY AUDITOR

About our Office

The mission of the Office of the City Auditor is to provide City Council with an independent, objective and comprehensive auditing program for operations of the City. Our auditing program includes:

- Evaluating the adequacy of financial controls, records and operations
- Evaluating the effectiveness and efficiency of organizational operations
- Providing Council, management and employees objective analysis, appraisals, and recommendations for improving systems and activities

The Office of the City Auditor is responsible for auditing the systems used by the City of Colorado Springs and its enterprises, including Colorado Springs Utilities. We perform a variety of audits for these entities, including financial audits, performance audits, contract audits, construction audits, and information system audits. We also perform follow-up on a periodic basis to monitor and ensure management actions have been effectively implemented.

Authorization and Organizational Placement

Our audits are conducted under the authority of Chapter 1, Article 2, Part 7 of the Colorado Springs City Code, and more specifically parts 703, 705 and 706 of the Code. 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.

Audit Standards

The audit was conducted in a manner that conforms 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.

The audit included interviews with appropriate personnel and such tests of records and other supporting documentation as deemed necessary in the circumstances. We reviewed the internal control structure and compliance tests. Sufficient competent evidential matter was gathered to support our conclusions.