



**U.S. Department of the Interior
Office of Inspector General**

AUDIT REPORT

FINANCIAL ARRANGEMENTS BETWEEN THE GOVERNMENT OF THE VIRGIN ISLANDS AND FINANCIAL INSTITUTIONS

**REPORT NO. V-IN-VIS-0069-2004
SEPTEMBER 2004**



United States Department of the Interior

OFFICE OF INSPECTOR GENERAL

Eastern Regional Office
381 Elden Street – Suite 1100
Herndon, Virginia 20170

September 30, 2004

AUDIT REPORT

Honorable Charles W. Turnbull
Governor of the Virgin Islands
No. 21 Kongens Gade
Charlotte Amalie, Virgin Islands 00802

Subject: Audit Report on “Financial Arrangements Between the Government of the Virgin Islands and Financial Institutions” (Report No. V-IN-VIS-0069-2004)

Dear Governor Turnbull:

This report presents the results of our audit of the financial arrangements between the Government of the Virgin Islands and financial institutions. The objective of our audit was to determine whether (1) the acquisition of banking services was done in accordance with applicable laws and regulations and (2) the Government received maximum benefits from its existing banking relationships. Our audit covered all loans obtained and all bank accounts held by the Government during fiscal years 1999 through 2004. The audit did not include financial arrangements of the Government’s independent instrumentalities.

BACKGROUND AND SCOPE

The Public Finance Authority was created to aid the Government of the Virgin Islands in performing its fiscal duties and to raise and manage capital for public projects. Government of the Virgin Islands legislation empowers the Authority to borrow money and issue bonds, lend bond proceeds or other money to Governmental agencies and private entities, and invest its own funds as well as the Government’s. Acting in this capacity, during 1999 and 2003, the Authority assisted the Government in obtaining two short-term loans and preparing one short-term bond issuance. These were the \$31.55 million Y2K Compliance Financing Loan and the \$100 million Bridge Loan, both of which the Government later refinanced by the floating of bonds, and the \$35 million Short Term Payroll Note.

For regular banking, the Government of the Virgin Islands used the only two domestic banks in the territory (Banco Popular and First Bank) to secure services such as checking, saving, and direct deposit accounts. A total of 55 accounts were divided between the two banks. For example, the Government’s General Fund accounts are handled by Banco Popular, while the Special and Other Funds accounts are handled by First Bank.

We obtained a list of all loans issued to the Government during fiscal years 1999 to 2004 from the Department of Finance. The list confirmed that the Government obtained short-term financing on three occasions: the \$31.55 million Y2K Compliance Financing Loan, the \$100 million Bridge Loan, and the \$35 million Short Term Payroll Note. We then obtained and examined the documents related to the three short-term loans from the Public Finance Authority and the Department of Finance.

We conducted our audit in accordance with the “Government Auditing Standards,” issued by the Comptroller General of the United States. Accordingly, we included such tests of records and other auditing procedures that were considered necessary under the circumstances. We concluded our audit at the end of the survey phase because we determined that the continuation of the audit would not identify any material weaknesses. Therefore, the scope of the audit was limited to those procedures performed during the survey phase. As a result, our review of management controls and testing of transactions was limited.

RESULTS OF AUDIT

We found that the Government of the Virgin Islands did not have specific requirements in the Virgin Islands Code or its regulations for procuring banking services. That notwithstanding, the Public Finance Authority provided the opportunity for competition to the two domestic banks when obtaining the short-term loans. Further, it was apparent that the Government received the best possible interest rates on the loans processed during our review period. Details follow:

- **Y2K Compliance Financing Loan of \$31.55 Million.** The Government obtained loans totaling \$31.55 million on April 13, 1999, that were then refinanced by the floating of bonds on the same date to purchase hardware, software, firmware, and related services and computer equipment for Y2K compliance. General obligation bonds were issued by the Government to Banco Popular and to IBM Corporation for a total of \$18 million (\$9 million each). Those bonds accrued interest at 6.5 percent. A project revenue bond was simultaneously issued by the Public Finance Authority to U.S. Trust Company in the amount of \$13.55 million. This bond accrued interest at 6.25 percent.
- **Bridge Loan of \$100 Million.** The Government borrowed \$100 million from Banco Popular for the period of September to December 2003 at 3.25 percent until proceeds in the amount of \$268 million from the issuance of series 2003A bonds became available. The purpose of the loan was to cover payments to vendors and refunds to taxpayers.
- **Short Term Payroll Note of \$35 Million.** The Government issued \$35 million in bonds to satisfy salary and payroll requirements on July 12, 1999, on the terms that they would mature on July 10, 2000, and would bear interest at the rate of 5.8 percent.

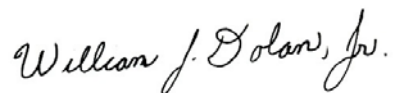
We did not find records of negotiation for any of the loans at the Public Finance Authority or the Department of Finance. However, we interviewed the vice-president responsible for handling Government accounts at First Bank (formerly Chase Bank) to determine if the bank had been afforded the opportunity to compete for any of the Government’s banking services. The vice-president explained that First Bank was given every opportunity to compete for the two

loans she knew about: the \$31.55 million Y2K Compliance Financing Loan and the \$100 million Bridge Loan. She further stated that she was the liaison for the bank on both loans. Although First Bank officials never actually sat at a table for any negotiations with Government or Public Finance Authority officials, the bank submitted proposals for both loans. Our review of the proposal documents revealed that First Bank actually ended up providing the Government with \$35 million of the \$100 million Bridge Loan through a separate agreement made with Banco Popular. According to the vice-president, although they submitted a proposal for the Y2K Compliance Financing Loan, they were unable to respond to the Government's information requests regarding this loan in a timely manner because decisions for their bank (part of the Chase Bank chain at the time) were not made locally.

Additionally, we found that for the three instances where the Government received short-term financing, the bond rates were less than the prevailing London Inter Bank Offered Rate (LIBOR rate) for commercial lending at the time. Therefore, it would appear that it was more beneficial for the Government to issue bonds.

This report does not contain any recommendations; therefore a response is not required. However, if you have any questions, please contact Mr. Arnold van Beverhoudt, Jr., Field Office Supervisor, at (340) 774-8300.

Sincerely,

A handwritten signature in cursive script that reads "William J. Dolan, Jr.".

William J. Dolan, Jr.
Regional Audit Manager

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