



Village of Silver Creek

Property Acquisition

Report of Examination

Period Covered:

August 1, 2009 — September 19, 2011

2011M-229



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

February 2012

Dear Village Officials:

A top priority of the Office of the State Comptroller is to help local government officials manage government resources efficiently and effectively and, by so doing, provide accountability for tax dollars spent to support government operations. The Comptroller oversees the fiscal affairs of local governments statewide, as well as compliance with relevant statutes and observance of good business practices. This fiscal oversight is accomplished, in part, through our audits, which identify opportunities for improving operations and Board of Trustees governance. Audits also can identify strategies to reduce costs and to strengthen controls intended to safeguard local government assets.

Following is a report of our audit of the Village of Silver Creek entitled Property Acquisition. This audit was conducted pursuant to Article V, Section 1 of the State Constitution and the State Comptroller's authority as set forth in Article 3 of the General Municipal Law.

This audit's results and recommendations are resources for local government officials to use in effectively managing operations and in meeting the expectations of their constituents. If you have questions about this report, please feel free to contact the local regional office for your county, as listed at the end of this report.

Respectfully submitted,

*Office of the State Comptroller
Division of Local Government
and School Accountability*

Introduction

Background

The Village of Silver Creek (Village) is located in the Town of Hanover in Chautauqua County and has a population of approximately 2,600 residents. The Village provides various services to its residents, including general government support, street maintenance and improvement, and snow removal. Budgeted general fund appropriations for the 2011-12 fiscal year are approximately \$2.1 million and are funded primarily with real property taxes, grants and fees. The Village is governed by an elected Board of Trustees (Board) which is comprised of a Mayor and four Trustees. The Board is responsible for overseeing Village finances and setting policies governing Village operations.

In August of 2009, the Village's Department of Public Works (DPW) facilities were damaged beyond repair by flood waters. The damaged facilities, with a total of 13,782 square feet, included three buildings: a garage/office building, a truck storage building and a salt storage barn. The Village sought financial assistance to rebuild from the Federal Emergency Management Agency (FEMA). In January of 2010, FEMA approved a grant authorizing the Village to build a new DPW facility at an alternate¹ location.

The Board created a Building Committee comprised of two Trustees, two members of the DPW and a volunteer community member to research the Village's options for replacing the damaged facilities. In the meantime, the Village leased space for its DPW operations at a facility located just outside the Village.

The Building Committee considered several properties in the area as sites for the new facilities, which ultimately resulted in three options. In the spring of 2010, the Building Committee met with an engineering firm to develop conceptual designs for a new DPW facility.

Objective

Our audit focused on the Village's acquisition of a building to determine if the Board exercised due diligence and adequately protected the interests of Village taxpayers. Our audit addressed the following related question:

- Did the Board and Village officials acquire a building that adequately met the Village's needs and fulfill their

¹ The damaged DPW facilities were located in a floodplain. Therefore, in order to receive financial assistance from FEMA, the facilities had to be relocated to an area outside the floodplain.

responsibility to acquire the property at a reasonable cost while minimizing potential long-term costs to the greatest extent possible?

**Scope and
Methodology**

We evaluated the circumstances and decisions that were made by the Board related to the Village's acquisition of a building for the period August 1, 2009 to September 19, 2011.

We conducted our audit in accordance with generally accepted government auditing standards (GAGAS). More information on such standards and the methodology used in performing this audit are included in Appendix D of this report.

**Comments of
Local Officials and
Corrective Action**

The results of our audit and recommendations have been discussed with Village officials and their comments, which appear in Appendix B, have been considered in preparing this report. Village officials generally disagreed with our findings but indicated they would be taking corrective action with certain recommendations. Appendix C includes our comments on issues raised in the Village's response.

The Board of Trustees has the responsibility to initiate corrective action. A written corrective action plan (CAP) that addresses the findings and recommendations in this report should be prepared and forwarded to our office within 90 days, pursuant to Section 35 of the General Municipal Law. For more information on preparing and filing your CAP, please refer to our brochure, *Responding to an OSC Audit Report*, which you received with the draft audit report. We encourage the Board of Trustees to make this plan available for public review in the Clerk's office.

Property Acquisition

As stewards of public funds, the Board is responsible for ensuring that real property acquisition is undertaken only after a process of due diligence. The Board should acquire property that meets the Village's needs, fully evaluate and consider all viable options and ensure that potential costs are fully investigated. The Board has a fiduciary duty to acquire property in the public's best interest at the most beneficial terms including price.

The Board was unable to demonstrate that the purchase of a building for \$725,000 was the most prudent use of taxpayer resources because the Village paid more than twice the apparent market value. Village officials could not demonstrate that they fully evaluated or considered the long-term costs and/or potential consequences of purchasing and renovating an older facility rather than constructing a new building. Further, the Board could not demonstrate that the decision was the result of a thorough and deliberate process that fully considered all suitable options.

This inadequate process has also exposed the Village to other uncertainties. For example, because the Board decided to purchase a used building rather than construct a new facility, Village officials have no assurance how much, if any, Federal and State reimbursement will be received. As a result, Village taxpayers could potentially become responsible for the full cost, over \$900,000, of the building and improvements.

Building Cost

In determining the reasonableness of the price to be paid for a building, it is essential for the Board to obtain an independent appraisal of real property. Under most circumstances involving purchases of real property, buyers obtain the services of professional appraisers to help establish the market value of the property. Because no appraisal can establish value with absolute precision, the use of two appraisals for substantial purchases would better enable the Board to establish the value of the property and substantiate the price ultimately paid.

We found that Village officials failed to obtain a formal appraisal of the property. At the time of the sale, the Town of Hanover Assessor estimated that the market value of the property was approximately \$327,000.² In December of 2010, the Town Assessor also obtained an independent appraisal of the property in order to update her records.

² Real property in the Town is assessed at full value (that is, assessed value approximates market value).

At that time, the property was deemed to have an approximate market value of between \$300,000 and \$325,000. However, the Village purchased the property for \$725,000, more than double the apparent market value.

Village officials indicated they were aware of the property's approximate market value at the time of the purchase but could not explain how the price paid was established or provide a rationale to justify paying two times the apparent market value. In the absence of documentation to demonstrate that the purchase price was negotiated in good faith, Village officials did not adequately protect the interest of taxpayers.

Building and Funding Options

The Board had intended to use a combination of State and Federal grants, and local funds to finance the cost of purchasing land and building a new DPW facility. In December of 2009, the Village requested approval from FEMA to purchase land and build new facilities to house the DPW. The Village's grant request was approved by FEMA in January of 2010. At that time, the Board anticipated that FEMA would reimburse the Village 75 percent of the total cost to purchase property and build a new facility similar in size to the facilities lost in the flood. The remaining costs were expected to be shared equally by the State and the Village. The Village intended to issue debt to finance the cost of the project while awaiting reimbursement and to finance the Village's share of the project cost.

To assist the Board in the process of finding a new site for the DPW, the Board charged a newly created committee, the Building Committee, with the responsibility of locating and researching potential properties upon which the Village could build a new facility. The Building Committee Chairperson (Chairperson) stated that the Building Committee initially identified five or six available sites and then focused on the three most suitable options. The Village's engineering firm estimated that it would cost approximately \$1.8 million to build a facility similar in size and functionality to the facilities lost in the flood. Based on the three sites identified by the Building Committee and estimates provided by the engineering firm, the Village would spend an average of about \$510,000 to purchase one of the three sites and clear the property, and an additional \$1.8 million to construct a facility. Using these cost estimates, the Village would have been eligible³ to receive a total reimbursement averaging

³ FEMA will typically provide at least 75 percent of the eligible costs. When the project is complete, the State determines the final cost of accomplishing the eligible work and submits a report on the completed project to FEMA. After reviewing the State's report, FEMA may adjust the amount of the grant to reflect the actual cost for eligible work only, because funds will only be provided for costs that are within the scope of work approved by FEMA.

almost \$1.8 million from FEMA and the State (see Appendix A for specifics of the different new build options).

However, despite opposition from the public and the Village Planning Board, the Board ultimately chose to significantly alter its original plans and purchase a 30-year old vacant⁴ building for \$725,000 instead of building a new facility. Although the building purchased currently meets the DPW's space and program needs, the Village will incur additional costs for repairing the roof, making it handicapped accessible and remedying safety concerns regarding the driveway. Village officials estimate these improvements will total approximately \$192,000. The Village issued a bond anticipation note⁵ for \$995,000 to be repaid within one year for the acquisition and repair costs while it awaits reimbursement from FEMA and the State.

The Chairperson, who is also a Board member, stated that she felt that in the long-term, the best option for the Village would have been to build a new facility. As such, she initially voted against the rest of the Board's decision to abandon the original plan of building a new facility. She explained that the new build option gave the Village an opportunity to build a brand new facility with significant financial assistance, something she felt the Village would not have been able to afford on its own. The Village Planning Board also recommended that the Board build a new facility and opposed the decision to buy the facility primarily due to safety concerns.

At public hearings held in May and June of 2010, other members of the Board discussed the Village's options and presented their rationale for abandoning the original plan and purchasing an existing building instead. They stated that the Federal and State reimbursement would still be based on the estimated cost to build a new structure even if the Village purchased an existing building. Because purchasing an existing building would cost less than building a new facility, they believed there would be excess funds available for other purposes such as purchasing equipment and making repairs to other Village buildings.

Village officials stated that FEMA representatives had advised them that funding could be used in this manner. However, Village officials could provide no documentation to support these assertions and stated that they relied on verbal assurances from FEMA representatives that funding would be provided for not only purchasing an existing

⁴ Until 2008 the building was used as a warehouse by a beverage distribution business. The warehouse stood vacant until being leased by the Village as temporary space for the DPW in October of 2009.

⁵ The Board approved a resolution for up to \$2 million in bonds to be paid over five years.

facility but also for other projects. The only documentation regarding funding from FEMA indicated that funding had been approved for a new building project, not relocating to an existing building. Additionally, information available on FEMA's website indicates that funding could not be provided as officials indicated.

On June 10, 2010, the Village submitted information to the State Emergency Management Office (SEMO) requesting funding to purchase the vacant building and equipment, and to finance several other projects in lieu of funding a project to build a new DPW facility. The Village received a letter dated March 22, 2011, from SEMO stating that the Village's assumptions regarding funding for the project were incorrect and there would be no funding provided for equipment and repairs to other buildings. As such, it appears that the Village's decision to purchase the existing building was made at least in part based on inaccurate information and apparently a significant misunderstanding on the part of Village officials.

Although the Village's request was denied, the Board decided to continue with the purchase and to reapply for funding based on the actual cost to purchase and repair the building. At that time, the Village had not yet purchased the property and had no assurances that it would receive any reimbursement. Two Trustees indicated that their decision remained unchanged because they would like to eventually dissolve the DPW and contract with the Town of Hanover for services. Therefore, they indicated that building a new facility for a department that may not exist in a few years seemed to be a waste of money. Although the Village has not officially explored the option of consolidating services with the Town, these representations from Board members further demonstrate that they did not adequately consider the long-term implications of their actions. If the Board's intention was to consolidate services, then it should have fully evaluated this option prior to committing to a long-term decision to purchase a building. In the short term, the Village could have continued leasing a facility until the Board fully explored the consolidation issue.

Although the purchase and improvement costs of the building are eligible for reimbursement from FEMA and the State, as of September 19, 2011, FEMA has not yet approved the Village's funding request for this project. The Village has requested a partial payment from FEMA and the State and anticipates being reimbursed approximately \$478,000 in total, when the project is completed. The Village would then be responsible for financing the remaining costs including any other future repair or maintenance costs. Village officials indicated that although they have received no written assurance from FEMA that the project will be approved, they believe

the costs will be reimbursed based on verbal communication with their project liaison from the State. A representative from SEMO stated that the Village's grant request will most likely be approved by FEMA but he was not certain when the request would be approved or whether the entire amount would be eligible for reimbursement.

Cost Uncertainties

The acquisition of an older building can have a significant impact on future operating budgets. While capital assets tend to have a long useful life, they do deteriorate and need repairs. Older buildings typically require a greater commitment of time and money to adequately maintain them. Although the construction of a new building often requires a larger initial outlay, it could have produced certain savings. For example, new buildings with energy-efficient designs and energy-efficient equipment can significantly reduce utility costs.

Village officials could not demonstrate that they considered or evaluated the cost effectiveness and long-term cost implications associated with operating and maintaining a 30-year old facility versus building a new facility. Instead, Village officials based their decision primarily on an analysis of short-term costs and could not demonstrate that they considered the potential long-term consequences of their decision to purchase an older building.

Village officials stated that their decision to purchase the building was due primarily to the lower cost of buying an existing building rather than building a new facility. By selecting a less expensive option, they would lessen the burden on taxpayers because the amount borrowed would be lower. However, had Village officials opted to build a new facility, the majority of the \$2.3 million total estimated cost would have been eligible for reimbursement from FEMA and the State. Although the Village would need to finance approximately \$172,000 more if it opted to build a new facility, the funding request was already approved by FEMA. As such, the Village would have avoided the risks and uncertainties associated with buying an older property and initiating a project without guaranteed funding from the Federal and State governments.

Although representatives from SEMO have indicated that FEMA will likely approve the Village's request for funding, without certainty, the Board has placed Village taxpayers at risk. The Board has committed a significant amount of resources to a project based on an assumption that grant funds will be provided. If FEMA denies the Village's request, then taxpayers would be responsible for the project costs which could total more than \$900,000, significantly greater than the estimated local share for a new facility. Had officials been diligent in protecting the interest of taxpayers, they would have requested

funding from FEMA and received funding approval for the project before committing Village funds.

Recommendations

1. The Board should obtain one or more independent appraisals on any real property it intends to purchase to ensure the price is reasonable.
2. The Board should exercise due diligence when acquiring real property using a deliberate process that fully considers all suitable options and long-term implications.
3. The Board should take appropriate action to determine how much, if any, Federal and State aid reimbursement the Village will receive and develop a plan to address any shortfalls in expected reimbursement.

APPENDIX A

ESTIMATED COSTS FOR A NEW FACILITY

New Build Options				
	Site 1	Site 2	Site 3	Average Cost
Estimated Property Acquisition Cost	\$50,000	\$650,000	\$150,000	\$283,333
Estimated Site Clearing Cost	\$202,000	\$188,000	\$290,000	\$226,667
Estimated Building Cost	\$1,790,000	\$1,790,000	\$1,790,000	\$1,790,000
Total Cost	\$2,042,000	\$2,628,000	\$2,230,000	\$2,300,000
Less Penalty – No Flood Insurance	(\$275,614)	(\$275,614)	(\$275,614)	(\$275,614)
Total Amount Allowable	\$1,766,386	\$2,352,386	\$1,954,386	\$2,024,386
FEMA Share 75%	\$1,324,790	\$1,764,290	\$1,465,790	\$1,518,290
New York State Share 12.5%	\$220,798	\$294,048	\$244,298	\$253,048
Total Reimbursement	\$1,545,588	\$2,058,338	\$1,710,088	\$1,771,338
Net Local Share	\$220,798	\$294,048	\$244,298	\$253,048
Plus Penalty	\$275,614	\$275,614	\$275,614	\$275,614
Total Local Share	\$496,412	\$569,662	\$519,912	\$528,662

APPENDIX B
RESPONSE FROM LOCAL OFFICIALS

The local officials' response to this audit can be found on the following pages.

VILLAGE OF SILVER CREEK

OFFICE: MUNICIPAL BUILDING 172 CENTRAL AVENUE SILVER CREEK, 14136-1397 716-934-3240 FAX 716-934-2700
TDD phone number: 1-800-662-1220

Trustees
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ANNA FREDERICKSON
ANDREW VOLK
THOMAS HARMON

KURT LINDSTROM
Mayor

KERRIEANN W. PELLETTER
Village Clerk
JANET J. ST. GEORGE
Treasurer/Registrar
ANDREW KEHRER
Village Attorney

January 30, 2012

Office of the State Comptroller
Robert Meller, Chief Examiner
295 Main Street, Room 1032
Buffalo, NY 14203-2510

Dear Mr. Meller,

The Village of Silver Creek is in receipt of the State Comptroller's Office audit of the Village of Silver Creek. We are writing to provide you with the Village's response to the findings contained in your report, and to provide you with the Village's intended actions regarding the recommendations.

The State Comptroller's audit focused on the Village's purchase of a Department of Public Works (DPW) building after a catastrophic flood devastated the Village, destroyed our DPW building and all of the contents within it. During that time period many decisions had to be made very quickly and were made only after meetings that were held with Federal Emergency Management Agency (FEMA), State Emergency Management Office (SEMO), local disaster and Chautauqua County emergency management personnel, and public hearings open to all Village residents. Additionally during this time period, the Village was given one year from the first FEMA flood meeting to determine the best option to either build a new DPW building (which would allow the Village only a DPW building, no equipment would be funded through the FEMA or SEMO monies) or an alternate project which would have allowed funding for the purchase of an existing building, equipment need for DPW operations that was lost in the flood, and roof repairs to the Village Hall. The additional amount of funding through the alternate project was estimated at approximately \$700,000. The Village adopted a Board resolution to accept the alternate project. The Village Board made every effort during this difficult time period to always take into consideration the best interests of its taxpayers.

See
Note 1
Page 16

Response to recommendations:

1. *The Board should obtain one or more independent appraisals on any real property it intends to purchase to ensure the price is reasonable.*

The Board will in the future obtain one or more independent appraisals on the purchase of real property.

2. *The Board should exercise due diligence when acquiring real property using a deliberate process that fully considers all suitable options and long-term implications.*

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The Board respectfully disagrees with this finding. The Board established a Search Committee to identify possible sites for either a new building or alternate project for purchasing an existing property. Properties were evaluated for property add-ons and inherent costs with the assistance of Urban Engineers and half of these properties were eliminated due to their shortcomings in meeting building requirements. The Village is not a large Village with many options for acceptable building sites. Additionally, the affect of the costs of building a new building versus the costs of an alternate project were evaluated based on the potential effect that these costs would have on future tax rates. This included comparing the costs of a new building that would house only the Village's DPW and the associated costs which would have included re-purchasing all equipment that was destroyed, and having to pay for the lease payments of the temporary site out of Village funds. These new building costs were compared with purchasing an existing building, and receiving an additional \$700,000 under an alternate project. The additional \$700,000 could be used to replace the equipment that was destroyed and would cover the cost of a new roof that was needed on the Village Hall. Also, all lease payments made prior to the purchase of the building were deducted from the purchase price of the building under the alternate project. FEMA representatives came to the Village and visited and reviewed all sites and accepted the existing building that was purchased as sound since it provided the Village with 4,000 additional square feet from the destroyed former DPW building. It was determined at that time that the cost to the Village would be less and the Village would gain more by selecting the alternate project which FEMA and SEMO representatives informed the Village it was eligible for. The Board also held two public hearings to take into consideration the residents' viewpoints regarding their options. It was only after all decisions were made and after the one year time frame to make decisions that the Village was informed that it did not qualify for the additional \$700,000 portion of the alternate project. The Village however still qualifies for funding of the purchase of the existing building. With regards to the Board inadequately evaluating consolidation with the Town of Hanover's DPW, the State Comptroller's office suggested that a study should have been undertaken to evaluate the potential costs savings. Due to the time constraints regarding the decision that had to be made, there was not adequate time to perform this study. The Board is still considering this option and the building purchased is located within the Town and would function appropriately should a consolidation be undertaken. The State Comptroller's office also cited safety concerns as a reason not to purchase the existing site. There are two driveways that can be used to access the site. The DPW employees have been instructed to and currently only use the driveway that provides safe entry onto the street, and in the more than two years use of the site, there have been no accidents or other safety concerns reported. All of these issues identified by the State Comptroller's audit were evaluated by the Board prior to the purchase of the existing building. In light of the information above, the Board feels that the decision to purchase the existing building was the best option for the Village. The Village Board acted prudently and in the best interest of the taxpayers based on the information available at the time decisions were required to be made.

See
Note 2
Page 16

See
Note 3
Page 16

See
Note 4
Page 16

- The Board should take appropriate action to determine how much if any, Federal and State aid reimbursement the Village will receive and develop a plan to address any shortfalls in expected reimbursement.*

The Village Board has never received any type of communication from FEMA or SEMO that the purchase of an existing building would not be reimbursed. FEMA did not require the Village to build a new DPW building. The first partial request for reimbursement for the purchase of the existing building has been made and the Village has no reason to believe that this request will be denied. During the preparation of the Village's next fiscal year's budget the Village will assess the status of the federal and state reimbursements and will prepare a plan for shortfalls in funding, if any shortfalls are identified.

See
Note 5
Page 16

Sincerely,



Kurt Lindstrom
Village of Silver Creek Mayor

APPENDIX C

OSC COMMENTS ON THE VILLAGE'S RESPONSE

Note 1

In January of 2010, the Village received approval from FEMA to build a new DPW facility at an alternate location. In June of 2010, the Board instead, and without obtaining prior written approval from FEMA, voted to purchase an existing building and request funding for an “alternate project.” The Village’s request for funding the “alternate project” was denied in March 2011.

Note 2

As stated in the report, the Board created a Committee to assist in the process of locating potential properties upon which the Village could build a new facility. However, the Committee maintained no records to document their actions or key decisions; therefore, Village officials could not demonstrate that all potential sites were identified and evaluated using an objective process that was in the best interest of Village taxpayers.

Note 3

The cost analysis presented by Village officials was based on the inaccurate assumption that the Village would receive additional funding if it opted to purchase an existing facility rather than build a new one. Furthermore, Village officials did not provide any documentation from FEMA or SEMO that indicates this was a possibility. Information available on FEMA’s website indicates that funding could not be used in the manner described by Village officials.

Prior to purchasing the building, Village officials were informed by SEMO that funding would not be provided as they had anticipated. However, Village officials could not demonstrate that they ever re-evaluated or reconsidered the options upon realizing their original assumptions had been incorrect.

Note 4

Our report does not state that the building should not have been purchased due to safety concerns. Rather, it was the Village Planning Board that advised the Board not to purchase the building due to safety concerns. Our report merely cites the additional costs the Village will incur to remedy the driveway safety issues.

Note 5

FEMA has not approved the Village’s funding request for this project and Village officials have not obtained written assurance from FEMA that the project will be approved and reimbursed as anticipated.

APPENDIX D

AUDIT METHODOLOGY AND STANDARDS

To accomplish the objective of the audit and obtain valid audit evidence, we interviewed appropriate Village officials and employees, tested selected records, and examined pertinent documents for the period August 1, 2009 to September 19, 2011. Our audit focused on reviewing the Village's acquisition of real property for the purpose of relocating the Village DPW operations. Our procedures included the following steps:

- We reviewed the purchase contract to determine the terms and conditions of the real property acquisition.
- We reviewed property tax records for the specific parcel to determine the equalization rate in effect at the time of purchase and the property's assessed value.
- We interviewed the Village Mayor, Treasurer, DPW Supervisor, Village Attorney, and the Trustees who were on the Building Committee.
- We reviewed minutes of the Village Board and Planning Board and correspondence that the Village received from FEMA. We also contacted representatives from SEMO to obtain more information.
- We reviewed the engineering firm's report and FEMA project worksheets to identify the Village's general needs and space requirements for a new DPW facility.
- We conducted a guided tour of the purchased property to determine its condition and evaluate whether the facility met the Village's needs. We also reviewed a building condition survey report provided by contractors hired by the Village to inspect the condition of the building prior to purchase.
- We calculated the estimated cost of each of the building options considered by the Board and analyzed and compared the financial impact of each.

We conducted this performance audit in accordance with generally accepted government auditing standards (GAGAS). Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

APPENDIX E

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