



# Alden Central School District Financial Management

## Report of Examination

Period Covered:

July 1, 2012 – September 2, 2016

2016M-372



Thomas P. DiNapoli

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# State of New York Office of the State Comptroller

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## **Division of Local Government and School Accountability**

February 2017

Dear School District Officials:

A top priority of the Office of the State Comptroller is to help school district officials manage their districts efficiently and effectively and, by so doing, provide accountability for tax dollars spent to support district operations. The Comptroller oversees the fiscal affairs of districts statewide, as well as districts' 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 district operations and Board of Education governance. Audits also can identify strategies to reduce district costs and to strengthen controls intended to safeguard district assets.

Following is a report of our audit of the Alden Central School District, entitled Financial Management. 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 New York State General Municipal Law.

This audit's results and recommendations are resources for district 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 Alden Central School District (District) is located in the Towns of Alden, Lancaster, Marilla and Newstead in Erie County; the Town of Darien in Genesee County; and the Town of Bennington in Wyoming County. The District is governed by an elected seven-member Board of Education (Board), which is responsible for the general management and control of the District's financial and educational affairs. The Superintendent of Schools (Superintendent) is the District's chief executive officer and is responsible, along with the Business Administrator, for the District's day-to-day management and for the development and administration of the budget under the Board's direction.

The District operates four schools with approximately 1,690 students and 310 employees. The District's 2016-17 general fund appropriations totaled \$33.9 million and were funded primarily with real property taxes, State aid and sales tax.

## Objective

The objective of our audit was to review the District's financial management practices. Our audit addressed the following related question:

- Did the Board properly manage District finances by ensuring that budgets were realistic and fund balance and reserves were reasonable?

## Scope and Methodology

We examined the District's financial management practices for the period July 1, 2012 through September 2, 2016.

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 C of this report.

## Comments of District Officials and Corrective Action

The results of our audit and recommendations have been discussed with District officials, and their comments, which appear in Appendix A, have been considered in preparing this report. District officials generally agreed with most of our findings and recommendations and indicated they planned to implement corrective action. Appendix B includes our comment on an issue raised in the District's response.

The Board has the responsibility to initiate corrective action. Pursuant to Section 35 of the General Municipal Law, Section 2116-a (3)(c) of the New York State Education Law and Section 170.12 of the Regulations of the Commissioner of Education, a written corrective

action plan (CAP) that addresses the findings and recommendations in this report must be prepared and provided to our office within 90 days, with a copy forwarded to the Commissioner of Education. To the extent practicable, implementation of the CAP must begin by the end of the next fiscal year. 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. The Board should make the CAP available for public review in the District Clerk's office.

# Financial Management

The Board, Superintendent and Business Administrator are responsible for accurate and effective budgeting and financial planning. These officials should prepare and the Board should adopt annual budgets that contain realistic estimates of revenues, appropriations and the use of fund balance as a funding source for operations. District officials must ensure that unrestricted fund balance does not exceed the amount allowed by law. New York State Real Property Tax Law limits the amount of unrestricted fund balance a school district can retain to no more than 4 percent of the subsequent year's budget. A school district can also legally establish reserves and accumulate funds for certain future purposes (e.g., capital projects or retirement expenditures). The Board should appropriately fund reserves, monitor reserve balances and use them as intended to pay related expenditures.

The Board and District officials did not prepare accurate budgets for the 2012-13 through 2015-16 fiscal years as appropriations were overestimated by an average of \$5.5 million per year, or 15.8 percent (see Figure 1). Furthermore, appropriated fund balance was never used as budgeted because the District's budgeting practices produced operating surpluses in all four fiscal years reviewed. When unneeded appropriated fund balance is added back to unrestricted fund balance, unrestricted fund balance exceeds the statutory limit by 9 percentage points (see Figure 3). Finally, the employee benefit accrued liability reserve (EBALR), the unemployment insurance reserve and the insurance reserve are overfunded.

## Budget Estimates

The Board and District officials are responsible for accurately estimating revenues and appropriations in the annual budget. Accurate budget estimates help ensure that the real property tax levy is not greater than necessary.

We compared budgeted appropriations and estimated revenues with actual operating results from July 1, 2012 through June 30, 2016. While actual revenues were slightly greater than budget estimates, appropriations were overestimated by an average of \$5.5 million per year or a cumulative total of \$21.8 million (15.8 percent) over the last four years.

<b>Figure 1: Overestimated Appropriations</b>					
	2012-13	2013-14	2014-15	2015-16	Totals
Appropriations <sup>a</sup>	\$33,042,533	\$36,362,052	\$34,294,365	\$34,763,521	<b>\$138,462,471</b>
Expenditures	\$27,882,441	\$30,710,602	\$28,823,327	\$29,227,291	<b>\$116,643,661</b>
Overestimated Appropriations	\$5,160,092	\$5,651,450	\$5,471,038	\$5,536,230	<b>\$21,818,810</b>
Percentage Overestimated	15.6%	15.5%	16.0%	15.9%	<b>15.8%</b>

<sup>a</sup> Includes prior-year encumbrances and voter-approved propositions for the use of capital reserves.

The most significant appropriation variances were found in salaries, employee benefits<sup>1</sup> and the operation and maintenance of plant. Expenditures for these accounts averaged between \$1.9 million (12 percent) and \$665,000 (26 percent) less per year than budgeted. Because salary costs and employee benefits are primarily determined by contractual agreements, budgeted appropriations should be accurately projected and not consistently overestimated.

The District also included contingency appropriations, noted as “allowances,” in the adopted budget. The budget included over 20 separate appropriations where the allowance account code was used, with a cumulative total of approximately \$1.2 million per year. During the last four years, no expenditures were charged against these contingency accounts. There is no authority for a school district to include appropriations for contingencies in an adopted budget. Eliminating the contingency appropriations would have reduced the budget variance by \$1.2 million (22 percent) each year. Accurate budget estimates help ensure that the real property tax levy is not greater than necessary to fund operations.

### **Appropriation of Fund Balance and Reserves**

Fund balance represents the cumulative residual resources from prior fiscal years that can, and in some cases must, be used to lower property taxes for the subsequent fiscal year. A school district may retain a portion of fund balance at the end of the fiscal year for cash flow needs or unexpected expenditures. This amount, which is known as unrestricted fund balance, should not exceed the statutory limit. The portion of fund balance used to help finance budgeted appropriations and reduce the property tax levy is referred to as appropriated fund balance. Reserves can also be used to finance budgeted appropriations. When reserves and fund balance are appropriated, the expectation is that there will be a planned operating deficit in the subsequent fiscal year, financed by the amounts appropriated.

District officials annually appropriated both reserves and unrestricted fund balance to help finance budgeted appropriations. From 2012-13 through 2015-16, the District annually appropriated \$3 million from fund balance and an average of \$142,000 from reserves<sup>2</sup> to help finance general fund appropriations. However, appropriated fund balance was not needed as the District ended each year with an operating surplus rather than a planned deficit. Due to the District’s practice of significantly overestimating appropriations, it has experienced an average operating surplus of \$2.1 million per year (see Figure 2). The Board, through resolution, then used the operating surplus to

<sup>1</sup> Includes payments for retirement contributions, health insurance, Social Security, unemployment insurance and workers’ compensation

<sup>2</sup> These appropriations are from the unemployment, retirement and debt reserves. The use of the capital reserves was approved in separate propositions.

increase certain reserves and establish new reserves. However, this action always occurred after the fiscal year ended. A more appropriate method the Board could use to demonstrate its intent to fund reserves would be to include a provision in the proposed budget to increase the reserves. In this way, District residents would be aware of the Board's intent to fund reserves during the upcoming year.

<b>Figure 2: Unrestricted Fund Balance at Year-End</b>				
	2012-13	2013-14	2014-15	2015-16
Beginning Fund Balance	\$12,306,588	\$13,675,843	\$12,739,663	\$14,326,638
Add: Operating Surplus	\$1,804,123	\$1,834,063	\$2,012,873	\$2,736,573
Less: Use of Capital Reserves <sup>a</sup>	\$434,868	\$475,243	\$425,898	\$602,347
Less: Transfer From Capital Reserve to Capital Projects Fund	\$0	\$2,295,000	\$0	\$0
Net Change in Fund Balance	\$1,369,255	(\$936,180)	\$1,586,975	\$2,134,226
Ending Fund Balance	\$13,675,843	\$12,739,663	\$14,326,638	\$16,460,864
Less: Restricted Fund Balance (Reserves)	\$8,882,948	\$7,798,147	\$9,358,315	\$11,629,903
Less: Encumbrances	\$470,163	\$611,869	\$627,816	\$474,519
Less: Appropriated Fund Balance for the Subsequent Year	\$3,000,000	\$3,000,000	\$3,000,000	\$3,000,000
Unrestricted Fund Balance at Fiscal Year-End	\$1,322,732	\$1,329,647	\$1,340,507	\$1,356,442
Subsequent Year's Budgeted Appropriations	\$33,073,889	\$33,256,496	\$33,512,705	\$33,911,106
Unrestricted Fund Balance as a Percentage of Subsequent Year's Budget	4%	4%	4%	4%

<sup>a</sup> Purchase of school buses and equipment

When appropriated fund balance that was not needed to finance operations is added back, the District's unrestricted fund balance would have exceeded the statutory limit by 9 percentage points in all four years.

<b>Figure 3: Unused Fund Balance</b>				
	2012-13	2013-14	2014-15	2015-16
Unrestricted Fund Balance at Fiscal Year-End	\$1,322,732	\$1,329,647	\$1,340,507	\$1,356,442
Add: Appropriated Fund Balance Not Used to Fund Subsequent Year's Budget	\$3,000,000	\$3,000,000	\$3,000,000	\$3,000,000
Recalculated Unrestricted Fund Balance	\$4,322,732	\$4,329,647	\$4,340,507	\$4,356,442
Recalculated Unrestricted Fund Balance as a Percentage of Subsequent Year's Budget	13%	13%	13%	13%

Based on our assessment of the 2016-17 budget, we project that the amount of overestimated appropriations will be similar to prior years (Figure 1). Therefore, we forecast that appropriated fund balance (\$3 million) will not be used as budgeted and the District will experience an operating surplus.

## Reserve Funds

The Board may establish reserve funds to finance future costs for a variety of specified objects or purposes but must do so in compliance with statutory requirements. While school districts are generally not limited as to how much money can be held in reserves, balances should be reasonable. The Board should periodically assess the reasonableness of the amounts accumulated in each reserve and, when warranted, reduce reserve balances to a reasonable level or discontinue a reserve that is no longer needed or whose purpose has been achieved. Therefore, it is important that the Board adopt a written policy that states its rationale for establishing reserve funds, objectives for each reserve, targeted funding levels and conditions under which reserves will be used or replenished.

The Board adopted a reserve policy and regulation that is supplemented by a reserve report prepared by the Business Administrator on an annual basis. While the annual reserve report satisfies the majority of the requirements of the policy and regulation, it does not identify the optimal funding levels for each reserve and the conditions under which reserve assets will be used. This information is necessary in order for the Board to periodically evaluate the reasonableness of the amounts accumulated in the reserves and properly determine whether a reserve should be increased, reduced or discontinued.

As of June 30, 2016, the District reported 14 general fund reserves<sup>3</sup> with a combined balance of \$11.6 million. We found that the EBALR, the unemployment insurance reserve and the insurance reserve were overfunded. While the remaining reserves were generally reasonably funded, we discussed our observations of certain reserves with District officials.

EBALR — This reserve is authorized for the cash payment of accrued and unused sick, vacation and certain other accrued but unused leave time owed to employees when they leave District employment. As of June 30, 2016, the balance of this reserve was \$2.4 million. We found the liability that can be properly paid from the EBALR to be approximately \$2.1 million. As a result, this reserve is overfunded by more than \$300,000 (14 percent). The District's calculation of the liability incorrectly included costs that cannot be legally financed with the EBALR, such as Social Security and Medicare taxes and contributions to the New York State and Local Retirement System. While the District has incurred expenditures that could be paid from this reserve, no expenditures have been charged to this reserve since June 2012.

Unemployment Insurance Reserve — This reserve is authorized to fund payments made when a school district elects to reimburse the

<sup>3</sup> Seven of the 14 reserves are capital reserves.

New York State Unemployment Insurance Fund for actual claims filed. As of June 30, 2016, the District reported a balance in this reserve of approximately \$479,000. On average, over the last four years, the District has paid approximately \$18,000 each year in unemployment expenditures. Based on this average cost, the current reserve balance is sufficient to pay unemployment insurance expenditures for more than 20 years. In addition, no expenditures have been charged to this reserve since at least 2001. This level of funding appears excessive. Therefore, the Board should consider reducing the balance to a more reasonable amount.

Insurance Reserve — This reserve is authorized to fund certain uninsured losses, claims, actions or judgments for which a school district is authorized or required to purchase insurance. As of June 30, 2016, the District reported a balance in this reserve of approximately \$91,000. Because the District has not used this reserve since at least 2003 and currently does not have any outstanding claims that could be paid with this reserve, we question the District's need for this reserve.

While it is fiscally prudent to provide for unforeseen circumstances, retaining excessive reserve balances results in a tax levy that is higher than necessary.

## Recommendations

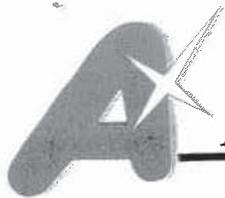
The Board and District officials should:

1. Develop realistic estimates of appropriations and use of fund balance in the annual budget.
2. Use surplus funds as a financing source for:
  - Funding one-time expenditures;
  - Funding needed reserves; and
  - Reducing District property taxes.
3. Discontinue the use of contingency, or allowance, accounts within the annual budget.
4. Update the reserve policy to ensure it clearly describes the optimal funding levels for each reserve and the conditions under which reserves will be used.
5. Review all reserves at least annually to determine if the amounts reserved are necessary and reasonable, and use the excess amounts in accordance with applicable statutory provisions in a manner that benefits residents.

## **APPENDIX A**

### **RESPONSE FROM DISTRICT OFFICIALS**

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



February 3, 2017

State of New York  
Office of the State Comptroller  
Attn: Jeffrey D. Mazula  
110 State Street  
Albany, New York 12236

**RE: Alden Central School District Response and Corrective Action Plan to Financial Examination for the financial management period of July 1, 2012 through June 30, 2016.**

Dear Mr. Mazula:

The Alden Central School District is in receipt of the State Comptroller's Office draft Report of Examination for Financial Management for the period of July 1, 2012 through June 30, 2016. On behalf of Aden Central School District, we appreciate the feedback and thank the staff of the Comptroller's office, as we found them to be professional throughout the audit process.

The District will reflect on the feedback provided by the Comptroller's Office, and is open to making any necessary changes it sees fit to adjust and/or strengthen our current practices moving forward.

While pleased that the State Comptroller's audit did not identify any instances of fraud or misappropriation of funds, nor did the audit identify any instances of waste or misuse, the District disagrees with some of the viewpoints referenced in the audit. In addition, as part of the closing discussion, a State-assigned staff member commented favorably on the fact that over the last four years, the true value tax rates of the District have decreased from \$19.03 to \$17.33 per thousand, an 8.9% decrease.

See  
Note 1  
Page 14

The draft report contains a few conclusions that, in our viewpoint, are subjective opinion statements by the Comptroller's auditors as related to the District's financial management, specifically in the area of budget practices. We acknowledge the Comptroller's perspective in this area; however, believe that our conservative approach to financial management is consistent with our legal authority and our fiscal responsibility to taxpayers and educational program.

As we reviewed the draft report, the District was pleased to learn that, "A top priority at the Office of the State Comptroller is to help school district officials manage their districts efficiently and effectively and by so doing, provide accountability for tax dollars spent to support district operations." Over the last several years we have adopted this same philosophy and are consistently

looking at ways to run programs and operations more effectively and efficiently, while being able to provide the necessary educational opportunities to the students of the District. The following are a few examples of how the Alden Central School District has done a remarkable job meeting all three (3) of the above mentioned areas:

- Buildings & Grounds Superintendent duties currently performed by Business Administrator
- Athletic Director duties assigned to a teacher with Superintendent's assistance
- Curriculum Director – Director of Student and Staff Learning position handles curriculum and special education responsibilities
- Personnel duties performed by Superintendent and Business Administrator
- Work with local municipalities to provide cost-sharing services between the District and town and local government entities
- Work collaboratively with other districts for cost-saving opportunities (collective bidding on supplies and services), special education services and transportation
- Bid out services and commodities regularly to reduce operating costs

One of the recommendations the draft report made was that the Board and District officials should develop realistic estimates of appropriations and use of fund balance in the annual budget. Over the last several years, Alden Central School District has been operating in one of the most volatile economic times in decades; and yet has kept the tax levy at an average increase of 1% over the time of this audit. Over the same time period, the District has experienced unpredictable health care, pension and special education costs as well as collective bargaining agreements not settled prior to budget adoption, coupled with unforeseen legislatively initiated unfunded mandates; such as carbon monoxide detectors, lead water testing and Annual Professional Performance Review requirements, after the budgets had been adopted. These challenges have been met while the District operates with a Tax Levy Cap and a frozen Foundation Aid formula. Until this last budget session, the District was without their share of the Gap Elimination Adjustment. While we are grateful to finally receive this funding, it is important to note that since 2008, over \$10 million was withheld from our District.

We are pleased to read the Comptroller's press release dated January 6, 2017, as he recognizes, "Many of New York's local governments are coping with slow or no revenue growth, making it difficult for them to maintain services while keeping pace with rising fixed costs such as health care, according to the 2016 annual report on the state's local governments released today by State Comptroller Thomas P. DiNapoli." "New York's municipal governments are seeing sales tax revenue growth slow and state aid remain essentially flat while they and school districts are coping with tax cap and tax freeze initiatives that limit growth in property taxes," DiNapoli said.

The Comptroller cites projected local tax revenue falling from "3.6 percent to 1.8 percent in the first nine months of 2016 from the same period a year earlier." On a larger scale, it is our understanding that currently New York State is projecting a \$700-million to \$1-billion-dollar shortfall to their current year's budget, which may impact the State Aid that the Alden Central School District receives in future years. These are just two factors that are unpredictable and out of the District's control. Unfortunately, we have experienced significant reductions in State Aid, including, but not limited to, the Gap Elimination Adjustment and Foundation Aid hold-backs.

The District received \$14.82 million in State Aid during the 2008-2009 fiscal year. For the 2016-2017 fiscal year, the District is projecting State Aid of \$14.26 million, a decrease of almost 4% from the 2008-2009 fiscal year.

Over the last several years, the District has employed conservative budgeting practices in an effort to maintain programming for our students, and to avoid becoming educationally insolvent. If we did not take these steps, reserves would have been depleted and/or the District would have been forced to present a budget(s) over our allowable tax levy cap to sustain programming. Instead, our budget practices have yielded a zero percent (0%) increase in the tax levy in each of the last two years, and tax rates that have decreased by 8.9% over the last four (4) years, even with the implementation of the Veterans Tax Exemption.

The draft report made a second recommendation that annual surplus funds be used as a financing source for one-time expenditures, needed reserves, and reducing District property taxes. The District agrees with this recommendation and believes it has historically used surplus funds to fund reserves, thus minimize the impact to taxpayers on large purchases, such as new buses and grounds equipment.

The District agrees with the third recommendation from the draft audit to discontinue the use of contingency, or allowance accounts within the annual budget. While no expenditures were charged against these accounts over the last four years, appropriations were transferred out of these allowance accounts to cover unanticipated expenditures in other budget accounts per Board of Education policy, thus reducing the contingency or allowance budget lines. In the future, estimated unforeseen expenditures will be coded more specifically, therefore budget transfers will not need to be completed.

The fourth recommendation included in the draft report suggests that the Board update the current reserve policy to outline optimal funding levels for each reserve, and the conditions under which reserves will be used. The District has implemented this suggestion in its long-range plan and reserves fund report approved by the Board of Education on January 19, 2017.

The last recommendation from the draft report offered, was an annual review by the Board to determine if the amounts reserved are necessary and reasonable, and use the excess amounts in accordance with applicable statutory provisions in a manner that benefits residents. The District and Board will continue to review this as part of the annual budget work sessions.

The Alden Central School District's Board of Education continues to be fiscally judicious in protecting against future financial instability. Given the financial status of New York State and the Comptroller's latest press release, we continue to be concerned that future State budgets will include a freeze to Foundation Aid or the re-introduction of the Gap Elimination Adjustment.

The Alden Central School District has yet to receive their fair share of Foundation Aid it is owed as a result of a freeze in calculations almost nine years ago. If the phase-in formula created by the Campaign for Fiscal Equity lawsuit had not been adjusted, our District would have received an estimated \$20 million in aid over this time. In fact, the Governor's 2017-18 State Aid run, published January 18, 2017, projects the Alden Central School District receiving a mere 1.5%

increase in Foundation Aid, or approximately \$137,000. The projected health insurance premium increase we are contractually obligated to cover in the 2017-18 budget year is projected to be approximately \$360,000. So as you can see, at the very early stages of our annual budget process, we are already looking to close a significant negative gap. The District needs to budget not only in the short-term, but in the long-term, because of the Tax Cap and the fact that the State continues to fail to provide a consistent and reliable funding methodology from year to year.

In September 2016 on the New York State School Boards Association news segment, Comptroller DiNapoli advised school districts to be cautious as the economy is slowing, and schools could face a tighter budget picture next year. This statement, coupled with his remarks last week and a CPI calculation for the 2017-18 school year of 1.26%, is why we continue to employ conservative budget practices. Without this philosophy, the potential for another large staff and program reduction exists each year that New York State fails to fund school districts through State aid.

In conclusion, we appreciate and respect the comments and recommendations in this draft report by the staff of the State Comptroller's office. The Alden Central School District and its Board of Education believe that our current budgeting and financial management practices will allow us to exhibit long-range fiscal responsibility to our community and ensure the integrity of our program and physical space.

Sincerely,

Adam Stoltman  
Superintendent of Schools  
Alden Central School District

Jill Hopcia  
President  
Board of Education

## **APPENDIX B**

### **OSC COMMENT ON THE DISTRICT'S RESPONSE**

#### Note 1

While we acknowledged at the exit discussion that the tax levy has not increased since the 2014-15 fiscal year, as indicated in the audit report, the Board and District officials' financial management practices resulted in a higher tax levy than necessary to support operating expenditures.

## APPENDIX C

### AUDIT METHODOLOGY AND STANDARDS

To achieve our audit objective and obtain valid audit evidence, we performed the following audit procedures:

- We interviewed District officials to gain an understanding of the District's financial management practices.
- We reviewed District policies and procedures related to budgeting and reserves.
- We identified all reserves in place during the last four years and assessed if they were properly established.
- We analyzed 2012-13, 2013-14, 2014-15 and 2015-16 budgeted appropriations and estimated revenues for the general fund and compared them to actual results. We calculated if there was an operating surplus or deficit for each of these years.
- We evaluated selected appropriation codes for the most recent four years for the general fund and compared them to actual results. We identified those with significant budget variances.
- We analyzed the fund balance reported in the general fund for the most recent four years and assessed if appropriated fund balance was used as budgeted.
- We documented the flow of funds in and out of the reserves over the last four years and assessed if reserve funds were used towards related expenditures.
- We evaluated select expenditures that would be eligible to be paid from a reserve for the most recent four years. We calculated the average amount and assessed how many years' worth of payments could be made from the related reserve.
- We recalculated the compensated absence calculation such that it only included amounts that could be properly funded by an EBALR.

We conducted this performance audit in accordance with 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 D

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