



# Village of Fairport Urban Renewal Agency

## Board Governance

### Report of Examination

Period Covered:

October 1, 2012 – March 12, 2015

2015M-196



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# State of New York Office of the State Comptroller

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

March 2016

Dear Agency Officials:

A top priority of the Office of the State Comptroller is to help local officials manage government resources efficiently and effectively and, by so doing, provide accountability for public dollars spent to support government operations. The Comptroller oversees the fiscal affairs of local governments and certain other public entities 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 governance. Audits also can identify strategies to reduce costs and to strengthen controls intended to safeguard governmental assets.

Following is a report of our audit of the Village of Fairport Urban Renewal Agency, entitled Board Governance. This audit was conducted pursuant to the State Comptroller's authority as set forth in Article X, Section 5 of the State Constitution and Article 3 of the New York State General Municipal Law.

This audit's results and recommendations are resources for agency 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*



## State of New York Office of the State Comptroller

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# EXECUTIVE SUMMARY

Urban Renewal Agencies (URAs) are independent public benefit corporations whose purpose is to undertake projects for the rehabilitation of substandard, insanitary, blighted, deteriorated or deteriorating conditions within the State's municipalities. In doing this, the overall goal of URAs is to reduce the number of areas that may be injurious to the public safety, health, morals and welfare of the people of the State. The powers and duties of URAs are set forth generally in Article 15-A of New York State General Municipal Law (GML).

The Village of Fairport Urban Renewal Agency (FURA) was established pursuant to Section 625 of GML to plan and undertake one or more urban renewal projects. The FURA currently administers three grant and loan programs.<sup>1</sup> Additionally, the FURA administers a Section 8 Housing Choice Voucher Program to provide low-income housing for qualified individuals in accordance with the rules and regulations prescribed by the Federal Department of Housing and Urban Development (HUD). The FURA's 2014 fiscal year<sup>2</sup> operating expenses totaled approximately \$2.36 million. The FURA receives the majority of its funding from HUD, and it must expend those funds in compliance with applicable HUD requirements. The FURA's remaining funding consists primarily of interest payments derived from its various commercial and residential loans.

The FURA operates in conjunction with the Village of Fairport Industrial Development Agency (FIDA) and the Village of Fairport Local Development Company (FLDC). These three entities have been termed the Village of Fairport Office of Community and Economic Development (OCED). The FURA is governed by a Board of Directors (Board) whose five members are appointed by the Village Board.<sup>3</sup> The Board is responsible for the general management and control of the FURA's financial and operational affairs. The FURA's day-to-day operations are the responsibility of its Executive Director (Director)<sup>4</sup> and Housing Director.

### **Scope and Objective**

The objective of our audit was to evaluate the propriety of the FURA's financial and operational activities for the period October 1, 2012 through March 12, 2015. Our audit addressed the following related question:

<sup>1</sup> Home improvement loan program, senior home improvement grant program and residential investor/owner loan program

<sup>2</sup> October 1, 2013 through September 30, 2014

<sup>3</sup> GML Section 553 provides that, for a village URA, the mayor appoints the members. For purposes of this report, we have assumed that all members of the FURA have been properly appointed.

<sup>4</sup> The Executive Director of OCED (as listed on the FURA page of the OCED website) is shared between the three OCED entities. However, her salary is only allocated between the FURA and the FIDA.

- Did the Board and Director implement a sound governance structure and manage the FURA's operations consistent with governing statutes?

### **Audit Results**

The Board and Executive Director did not manage FURA operations within the authority provided by law. The FURA's governance structure was highly inappropriate and not consistent with applicable legislation for URAs. The Board manages the FURA as if it is a department of OCED – an overarching umbrella in name only – which includes the separate and distinct corporate entities of the FURA, the FIDA and the FLDC. Each of these entities has its own distinct statutory purposes, responsibilities, powers and duties. This governance structure inappropriately gives the appearance that the three entities are legally affiliated with each other or subsidiaries of the OCED.

This intertwined governance structure has caused the FURA to act outside its statutory authority. Specifically, the FURA inappropriately gifted \$250,000 in assets to the FLDC. The FURA also made an annual contribution to the Village, totaling \$10,560 for the 2014 fiscal year, without a basis for the budgeted amount or a contract stipulating the services to be covered by this contribution. Furthermore, the FURA inappropriately received subsidies from the FIDA totaling \$250,000 from 2010 through 2014 and incorrectly recorded \$350,000 as due from the FIDA instead of cash in the accounting records. Management's improper governance practices have led to inappropriately commingled bank accounts and combined and inaccurate accounting records for the three OCED entities, as well as significantly misstated annual financial statements.

### **Comments of Agency Officials**

The results of our audit and recommendations have been discussed with Agency officials, and their comments, which appear in Appendix A, have been considered in preparing this report. Agency officials disagreed with certain aspects of our audit findings and recommendations but indicated their intent to implement corrective action for many of them. Appendix B contains OSC's comments on the issues raised in the Agency's response.

# Introduction

## Background

Urban Renewal Agencies (URAs) are independent public benefit corporations whose purpose is to undertake projects for the rehabilitation of substandard, insanitary, blighted, deteriorated or deteriorating conditions within the State's municipalities. In doing this, the overall goal of URAs is to reduce the number of areas that may be injurious to the public safety, health, morals and welfare of the people of the State. The powers and duties of URAs are set forth generally in Article 15-A of New York State General Municipal Law (GML).

The Village of Fairport Urban Renewal Agency (FURA) was established pursuant to Section 625 of GML to plan and undertake one or more urban renewal projects. The FURA currently administers three grant and loan programs.<sup>5</sup> Additionally, the FURA administers a Section 8 Housing Choice Voucher Program to provide low-income housing for qualified individuals in accordance with the rules and regulations prescribed by the Federal Department of Housing and Urban Development (HUD). The FURA's 2014<sup>6</sup> fiscal year operating expenses totaled approximately \$2.36 million. The FURA receives the majority of its funding from HUD, and it must expend those funds in compliance with applicable HUD requirements. The FURA's remaining funding consists primarily of interest payments derived from its various commercial and residential loans.

The FURA operates as part of the Village of Fairport Office of Community and Economic Development (OCED). OCED acts as an umbrella organization<sup>7</sup> that oversees the operations of the FURA, the Village of Fairport Industrial Development Agency (FIDA)<sup>8</sup> and the Village of Fairport Local Development Corporation (FLDC).<sup>9</sup> The FURA's Board of Directors (Board) is composed of five directors who are appointed by the Village Board. The Board is responsible for the general management and control of the FURA's financial

<sup>5</sup> Home improvement loan program, senior home improvement grant program and residential investor/owner loan program

<sup>6</sup> October 1, 2013 through September 30, 2014

<sup>7</sup> OCED is not a corporate entity or a Village department. However, it acts as if it is governing three separately incorporated entities. This structure gives the appearance that the FURA, the FIDA and the FLDC are legally affiliated with each other or subsidiaries or departments of OCED when, in fact, they are separate corporate entities. The OCED website previously referred to itself as a non-profit organization that is overseeing three different programs.

<sup>8</sup> The FIDA was established by an act of the New York State Legislature in 1976.

<sup>9</sup> The FLDC was incorporated as a local development corporation in April 2012 under not-for-profit corporation law.

and operational affairs. The FURA's day-to-day operations are the responsibility of its Executive Director (Director)<sup>10</sup> and Housing Director. A FURA employee enters daily financial transactions for all OCED entities. The OCED has also contracted with an external accountant to separate the three entities' activities into three general ledgers.

As part of the Public Authorities Reform Act of 2009, the State created an oversight body known as the Authorities Budget Office (ABO) to monitor the operations of authorities. As part of its oversight responsibilities, the ABO receives annual reports<sup>11</sup> from State and local authorities and contacts the authorities as deemed necessary.

## **Objective**

The objective of our audit was to evaluate the propriety of the FURA's financial and operational activities. Our audit addressed the following related question:

- Did the Board and Director implement a sound governance structure and manage the FURA's operations consistent with governing statutes?

## **Scope and Methodology**

We examined the FURA's financial and operational activities for the period October 1, 2012 through March 12, 2015.

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 B of this report. Unless otherwise indicated in this report, samples for testing were selected based on professional judgment, as it was not the intent to project the results onto the entire population. Where applicable, information is presented concerning the value and/or size of the relevant population and the sample selected for examination.

## **Comments of Agency Officials and Corrective Action**

The results of our audit and recommendations have been discussed with FURA officials, and their comments, which appear in Appendix A, have been considered in preparing this report. Agency officials disagreed with certain aspects of our audit findings and recommendations but indicated their intent to implement corrective action for many of them. Appendix B contains OSC's comments on the issues raised in the Agency's response.

<sup>10</sup> The Executive Director of OCED (as listed on the FURA's page of the OCED website) is shared between the three OCED entities. However, her salary is only allocated between the FURA and the FIDA.

<sup>11</sup> The Public Authorities Reporting Information System (PARIS) report to the ABO provides a summary of the FIDA's annual financial information.

The Board 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 to make this plan available for public review in the FURA's office.

## Board Governance

The Board is ultimately responsible for ensuring that the FURA's operations are efficient and effective and within the FURA's statutory authority. The Director is responsible for overseeing the FURA's day-to-day operations, including executing Board policies, leading operations and guiding personnel. Together, the Board and Director (Management) can achieve these responsibilities by implementing a corporate governance structure – including rules, policies and management practices – to help the FURA conduct business consistent with its corporate and public responsibilities. These governance principles establish the culture, values, organizational structure and control systems that promote accountability and integrity; set a standard of ethical behavior; support comprehensive, accurate and transparent reporting; and provide an objective review of financial practices. When followed, effective corporate governance contributes to public confidence in the organization's performance and decision making.

We found that Management did not implement a sound governance structure or adequately oversee and manage the FURA's operations. While the Board was involved in overseeing FURA operations, we found that its governance structure was highly inappropriate and not consistent with the statutory scheme governing URAs. The Board manages the FURA as if it is a department of the Village of Fairport Office of Community and Economic Development – an overarching umbrella organization in name only – which includes the separate and distinct corporate entities of the FURA, the Fairport Industrial Development Agency and the Fairport Local Development Corporation.

The FURA and the FIDA are public benefit corporations, while the FLDC is incorporated under New York State Not-For-Profit Corporation Law. Each of these entities has its own distinct statutory purposes, responsibilities, powers and duties. This governance structure gives the appearance that the three entities are legally affiliated with each other or subsidiaries of the OCED, which runs counter to the statutory scheme for establishment and operation of the FIDA, the FURA and the FLDC as separate corporate entities. This governance structure also violates the Public Authorities Accountability Act of 2005,<sup>12</sup> which prescribes various reporting and governance requirements for “every” local authority, not a single requirement for several local authorities acting as a consolidated entity.

<sup>12</sup> New York State Public Authorities Law (PAL) Section 2(2); L 2005, ch 766, as amended

This intertwined governance structure has caused the FURA to act outside its statutory authority. For example, the FURA made unauthorized gifts of \$250,000 in assets to the FLDC. The FURA also made an annual contribution to the Village totaling \$10,560 for the 2014 fiscal year without a basis for the budgeted amount or a contract stipulating services to be covered by this contribution. The FURA inappropriately received subsidies from the FIDA totaling \$250,000 from 2010 through 2014 and incorrectly recorded \$350,000 as due from the FIDA instead of cash in the accounting records. Management's improper governance practices have led to inappropriately commingled bank accounts and combined and inaccurate accounting records for the three OCED entities, as well as significantly misstated annual financial statements.

## Governance Structure

The FURA and the FIDA were established by special acts of the New York State Legislature in 1965 and 1976, respectively. They are local authorities<sup>13</sup> that are set up to be separate public benefit corporations, with separately appointed governing boards and separate and distinct purposes, powers and duties. By statutory design, they are independent from each other and the Village. The FLDC was incorporated as a private not-for-profit corporation in April 2012.

All three entities are essentially managed and operated by the same people,<sup>14</sup> under the same policies, and with commingled accounting records and bank and investment accounts. The Village Board appoints the same individuals to the five-member Board of Directors for each of the three OCED entities. In 2012, the Village Board appointed the newest member to what the Village's minutes referred to as the OCED Board rather than specifically to the FURA Board. The fact that the same Board members manage three separate corporate entities raises question as to their independence and ability to objectively manage each separate entity in its best interests.<sup>15</sup>

PAL provides that Board members of local authorities must, among other things, "apply independent judgment in the best interest of the authority, its mission and the public" and execute an acknowledgement to the effect that he or she "understands his or her duty of loyalty and care to the organization and commitment to the authority's mission and the public interest." These functions are targeted to each

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<sup>13</sup> For purposes of PAL

<sup>14</sup> The same FURA staff handle the operations of all three entities, with the exception of three FURA employees whose assigned duties strictly relate to the Section 8 Housing Program, but all are officially employed by the FURA.

<sup>15</sup> It is within the jurisdiction of the New York State Attorney General's office to issue opinions regarding the compatibility of offices, which warrants resolution related to the various Board members and their service as Board members for the other entities.

separate local authority, and there is no implication that a single oversight entity could perform these functions on behalf of several local authorities. PAL also requires each local authority to establish its own audit and governance committees comprised of independent members. However, here it is the OCED, not the FURA itself, which has created a single audit committee and governance committee for all three entities. Furthermore, the policies that have been developed and adopted by the Board are identified as policies of the OCED, not of the separate entities.<sup>16</sup>

The FURA employs four full-time and two part-time employees. The Board entered into a contract with the FIDA for leased employee services that provided for three FURA employees<sup>17</sup> to work for the FIDA with the employees' time and wages allocated between the two entities.<sup>18</sup> However, the employee lease agreement allocated the shared staff and Director's employment costs based on a time study that was performed in July 2010, prior to the creation of the FLDC. Therefore, the agreement does not accurately reflect current time demands and is not equitable. Additionally, the part-time administrative assistant's employment costs were allocated 50 percent to the FIDA when the time study indicated it should have been 91 percent. The OCED completed an updated time study in January 2015, but still excluded the FLDC from the study.<sup>19</sup> We reviewed payroll and expense allocation records and confirmed that there is no sound basis on which the OCED's shared staff employment costs are equitably allocated among the three entities.

In addition, OCED selects and begins projects that it feels are beneficial to the community but often does not determine which entity should manage, report and finish the projects until the projects are well underway. Maintaining commingled cash and accounting records for the entities enables the OCED to incur costs for new projects before deciding which entity will "own" them. OCED has, on various occasions, transferred projects to other entities without recouping costs initially incurred by the FIDA. Because each entity

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<sup>16</sup> Most of the FLDC's policies are specific to that entity. Only the FLDC's online banking and real property acquisition policies are shared with other OCED entities.

<sup>17</sup> The three employee titles included in the contract were Executive Director, IDA specialist and administrative assistant. It is unclear why the FURA would have had an IDA specialist on its payroll, but we understand this individual recorded financial transactions for all entities.

<sup>18</sup> For purposes of this report, we have assumed that there is underlying statutory authority for this employee sharing agreement between the FIDA and the FURA (but see OSC Opinion Number 2011-1; compare GML Section 119-o).

<sup>19</sup> On March 12, 2015 the Director told us that the Board is being careful about how to handle the FLDC due to retirement benefit implications. FLDC employees are not public employees and cannot, in that capacity, belong to the New York State and Local Employees Retirement System. The Director said they may end up contracting out the FLDC's work.

is statutorily created for specific purposes and to undertake specific types of projects, the tendency to pursue or begin a project without first deciding which entity will be the “lead agency” demonstrates disregard for the legal intent of and restrictions on the statutory authority of these local authorities.

We found that this governance structure is not appropriate. It is not consistent with the statutory scheme requiring each entity to act separately, to have independent boards and committees making decisions in the best interest of their own corporation and to have independent accounting and reporting structures. Additionally, this confused and commingled governance structure, including the extra layer of the OCED, has led to inappropriate financial and accounting transactions and significantly inaccurate accounting records and financial reports.

## Gifts

A URA may acquire property as part of the implementation of an urban renewal program. The URA must sell or lease its property at the highest marketable price or rental at public auction or by sealed bids.<sup>20</sup> On April 19, 2012, the FURA purchased a property in the Village for \$250,000. The FURA then transferred this property to the FLDC for \$1 on August 9, 2012. Therefore, the FURA never benefited financially from the purchase of this property and did not obtain a marketable price for it.

Management stated that they saw the location of this property as a gateway to the Village, so they actively sought its purchase. Management also stated that the property fit within the FLDC’s mission better than it did with the FURA’s. Therefore, they chose to transfer it to the FLDC. Because Management transferred the property to the FLDC without providing adequate consideration to the FURA, this was an inappropriate transaction. Subsequent to the transfer, the FLDC obtained a tenant to rent the facility for \$500 a month. The FLDC has retained these rental payments, with no plans to repay the FURA for its \$250,000 purchase cost.

In addition, the FURA had a budget line item for a “contribution to Village” of \$10,560<sup>21</sup> for the 2014 fiscal year. The Director said this payment is intended to cover plowing, utilities and other services that are part of the routine maintenance of Village Hall. The Director also said that there was no real basis for the budgeted amount, and the FURA and the Village did not have a contract which stipulated services to be covered by this contribution. The Board authorized a 3 percent increase to the budget in the 2014 fiscal year, with still

<sup>20</sup> With certain exceptions not applicable here

<sup>21</sup> This equates to 20 percent of the total (\$52,800) paid to the Village by the FURA and the FIDA.

no basis for the increase or total amount. The lack of a contract documenting services received for reasonable consideration can give the appearance of an unauthorized gift or gratuitous contribution to the Village. Further, this demonstrates the Board's questionable governance and provides no assurance that either party is receiving or paying appropriate consideration for services rendered.

Because of Management's willingness to disregard its legal limitations and its failure to provide the necessary direction and oversight of the FURA's operations, these transactions occurred outside of the statutory authority of URAs.

### **Commingled Accounts and Records**

As an independent public corporation, the FURA must manage its operations and maintain and account for its assets and resources separately from any other organization, in the absence of statutory authority to act otherwise. We are aware of no statutory authority for the FURA to combine its assets and operations with other entities. Thus, the Board must ensure that the Director keeps all FURA assets separate and accounted for. This includes accurately accounting for and depositing all cash assets in the FURA's own bank or investment accounts, maintaining a separate and complete set of accurate accounting records, accurately recording every FURA receipt or expenditure in the records, providing accurate and timely reports to the Board and filing an annual PARIS<sup>22</sup> report with the ABO. The PARIS report provides a summary of the FURA's annual financial information that should agree with and be supported by the accounting records.

The Board did not ensure that the Director kept all FURA assets separate from other agencies and accurately accounted for. The staff and the contracted accounting company (Company) maintained combined records and bank accounts for the FURA and FIDA and then developed very complex and inappropriate methods to attempt to allocate transactions to produce separate quarterly and annual reports. These egregious methods, described further, resulted in the following significant unauthorized activities:

Inappropriate IDA Subsidy – the FURA's revenues are primarily derived from payments of principal and interest on the loans it holds.<sup>23</sup> Revenues should be recorded in the FURA's accounting records when they are earned and reasonably expected to be received. The

<sup>22</sup> PARIS is the online, electronic data entry and collection system used by authorities to annually report required information to the ABO.

<sup>23</sup> Aside from federal funds received for the Section 8 Housing Program, which are more accurately accounted for with a separate general ledger and bank accounts. For purposes of this audit, we have assumed the legal propriety of the loans referred to in this section.

Company records a revenue, “Interprogram Income,” for the FURA in the amount of expenses the FURA has been allocated.<sup>24</sup> However, Interprogram Income is not a revenue because the FURA has done nothing to earn it. It is instead a subsidy from the FIDA, which has amounted to nearly \$250,000 for the period 2010 through 2014. There is no authority for the FIDA to subsidize the FURA’s operations. This has resulted in ongoing and significant misstatements of the FURA’s (and the FIDA’s) financial position.<sup>25</sup>

Unsubstantiated Promissory Note – The FURA’s 2014 audited financial statements included an asset due from the FIDA of approximately \$350,000. We determined that this should have been classified as the FURA’s cash balance. This occurred because the FURA does not have a separate bank account or general ledger cash account. Therefore, FURA staff deposit the FURA’s loan receipts into the FIDA’s project expenditures account and record them as a “due to the FURA” on the FIDA’s general ledger and a “due from the FIDA” on the FURA’s general ledger (with corresponding credits to the loan receivable and interest revenue accounts).

The Director told us that the improper practice of recording what should be the FURA’s cash balance as a “due from the FIDA” serves, in part, as an attempt to show that the FIDA has outstanding debt. In October 2011, the ABO informed Management that the FIDA no longer met the provisions of Section 882 of GML<sup>26</sup> and should no longer be in operation.<sup>27</sup> In response to this letter, Management formalized a promissory note between the FURA and the FIDA in the amount recorded at year end as due from the FIDA on the FURA’s reports, even though this amount really approximates what should be recorded and reported as FURA cash<sup>28</sup> and is not truly a debt.

<sup>24</sup> Because it did not have a general ledger cash account or bank account to credit to offset the debit to the expense accounts when allocating expenses to the FURA (with the exception of the Section 8 Housing Program), which are initially all paid by and charged against the FIDA

<sup>25</sup> The Company also recorded these disbursements backwards in the FIDA records by decreasing the individual expense accounts that were allocated to the FURA but then posting the corresponding total debit to an Interprogram Transfer expense account.

<sup>26</sup> At that time, Section 882 of GML stated that when “all the bonds or notes issued by the agency have been redeemed or canceled, the agency shall cease to exist.” In 2012, Section 882 was amended to provide that an IDA shall cease to exist when all of its bond or notes have been redeemed or canceled “and all straight-lease transactions have been terminated...”

<sup>27</sup> The ABO has questioned the FIDA’s existence, and the Director indicated that the FURA had received similar correspondence from the ABO about its own existence. To the extent that this issue remains open, the Director and Board should resolve this issue with the ABO. However, for purposes of the audit, we have presumed that the FIDA and the FURA are each a going concern.

<sup>28</sup> Excluding the additional reduction in the cash balance that should have resulted if FURA expenses had been properly recorded

Furthermore, we found that between the beginning of our risk assessment in April 2014 and our return for the audit in November 2014, the amounts on the promissory notes going back to 2011 had been changed and new notes had been issued back to 2008 to make it appear that legitimate notes had been in place. We also found that money was never exchanged between the two entities and the notes specifically state that no interest will be charged. However, a new note is signed every year with an updated amount reflecting the change in the “due from the FIDA” account balance. These promissory notes do not represent true debt, and the recording and reporting of amounts due from and to the two agencies is simply an inappropriate and unnecessary accounting tactic to make it appear that the FIDA has outstanding debt.

Bank Accounts – The Board did not require the Director and the Company to maintain the FURA’s cash assets in separate bank accounts independent of the other OCED entities. The OCED maintains combined bank accounts with commingled cash of the FURA and the FIDA: a project expenditures account used for all disbursements, two money market/savings accounts and a combined investment account. Neither the FURA’s employees nor the Company keep accurate ledger accounts to track the portion of each bank account balance that belongs to each entity. All of the shared bank accounts are reported by the FIDA. FURA staff make all disbursements for the FURA and the FIDA out of the FIDA checking account. Thus, the FURA does not report cash balances on its annual financial reports.<sup>29</sup>

Financial Records and Reports – The Company maintains the FURA’s general ledger. A FURA employee<sup>30</sup> enters daily transactions for the FURA and other OCED entities and provides transaction reports to the Company. The Director is responsible for ensuring that the employee and the Company properly perform the basic accounting functions.

The Board did not require the Director and the Company to maintain the FURA’s accounting records independent of the other OCED entities or in an accurate and complete manner as prescribed by the State Comptroller.<sup>31</sup> Management considered the Company’s records to be the FURA’s official accounting records. These records did not provide Management with an accurate depiction of the financial activity that belonged to the FURA because of inappropriate accounting methods used. Additionally, the information was not timely. The Company recorded its cost allocations and other transactions on a quarterly

<sup>29</sup> With the exception of the FURA’s Section 8 Housing Program, which maintains separate bank accounts

<sup>30</sup> This is the individual referred to as the IDA specialist in the leased employee services agreement.

<sup>31</sup> As required by GML

basis, but did not provide the general ledger reports to Management until six weeks after the quarter had ended.<sup>32</sup> Additionally, the PARIS reports and audited financial statements did not agree to the FURA's accounting records. The Company did not see any value in posting external auditor adjustments and providing Management with a final general ledger that agreed to the PARIS reports and audited financial statements. As a result of many improper accounting practices, the Board does not have and has not filed an accurate report of the FURA's financial position.

Because FURA staff make all FURA disbursements out of the FIDA checking account, they also inappropriately charge all expenses against the FIDA in the FIDA's accounting records and record nothing in the FURA's records at that time.<sup>33</sup> Furthermore, they do not adequately code or separate expenses by entity when making disbursements and, thus have no true and accurate record or measure of the expenses attributable to the FURA verses the other entities. Therefore, when the Company makes adjustments on a quarterly basis, its allocations to the FURA are not representative of actual expenses. For most of the audit period, the Company allocated expenses quarterly to the FURA based on 25 percent of the FURA's portion of the OCED budget.

Beginning in June 2014, Management directed the Company to change its allocation method to record actual expenses to each OCED entity – but only for individual payments of \$500 or more – and charge all other expenses to the FIDA. Therefore, the only expenses recorded on the FURA general ledger during the last two months of 2014 were for payroll and related taxes. This expense allocation method further understates the FURA's operating costs and overstates the FIDA's.<sup>34</sup>

Investment Accounts – PAL<sup>35</sup> requires the Board to adopt and annually review a comprehensive investment policy to establish procedures and instructions for depositing and investing the FURA's money in a manner that complies with statutory requirements and safeguards public funds. GML and PAL<sup>36</sup> authorize urban renewal agencies to temporarily invest moneys not required for immediate use in FDIC covered deposit accounts in, or certificates of deposit issued by, a

<sup>32</sup> One Board member told us she had never seen these reports.

<sup>33</sup> Notwithstanding the impropriety of maintaining combined bank accounts for two separate local authorities, when using combined bank accounts, staff must charge each expenditure against the actual applicable entity in its own general ledger expenditure and cash accounts, with shared costs such as a utility bill being split equitably between the entities, when the disbursement is made.

<sup>34</sup> During a meeting with the Director on March 12, 2015, she indicated that if an expense clearly belongs to the FURA, she is instructing the Company to record it as such even if it is below \$500.

<sup>35</sup> PAL Section 2925

<sup>36</sup> GML Section 554 (10) and PAL Section 2927

bank or trust company located and authorized to do business in the State, or in obligations of the State or the United States government or certain obligations of which the principal and interest are guaranteed by the State or United States government.

The Board adopted an investment policy that, prior to a January 20, 2015 amendment, properly restricted authorized investments to those allowed by law. However, the Board ignored its policy when making investments and ultimately updated it to allow for improper investments. We found that OCED staff invested the FURA's money in combined accounts with the FIDA's money, without statutory authority to do so, and had improper investments with an investment brokerage firm. As of October 31, 2014, the combined FURA and FIDA investment account had approximately \$911,000 improperly invested in bonds of local governments and government-sponsored enterprises<sup>37</sup> not guaranteed by the federal government (in addition to allowable investments totaling approximately \$819,000).

According to the FURA's audited financial statements, about \$350,000 of the invested money belonged to the FURA. Improper investments put FURA moneys at risk and could result in a loss of principal. For example, the FIDA's September 30, 2014 audited financial statements indicated that there was a (\$10,653) change in the market value of the account. Although the account had an overall gain on investments during the year due to interest and dividends, the drop in the account's market value shows the market volatility of the principal balance. This is a primary reason GML does not allow public entities to invest moneys in unguaranteed investments. In addition, although the investment account includes money that belongs to both the FURA and the FIDA, all of the investment activity is recorded in the FIDA's general ledger. Furthermore, FURA staff do not allocate any interest and dividend income or investment gains and losses to the FURA as required. Therefore, the FIDA is receiving more income and a larger share of investment gains and losses than it is entitled to, and Management does not have accurate cash balances for the FIDA or the FURA.

Accounting for the three OCED entities in such a combined and convoluted manner gives the appearance that all of these entities function together as one, or as legally affiliated entities or subsidiaries of OCED, and are not separate and distinct entities. It also makes it impossible to determine the true financial position of each separate entity. As a result, the FURA's actual revenues and expenses are not easily distinguishable from those of the other entities. Therefore, the FURA likely did not pay for all expenses it was responsible for and may not have received all revenues that belonged to it.

<sup>37</sup> Such as the Federal National Mortgage Association, Federal Home Loan Mortgage Corporation and Federal Farm Credit Banks

## Recommendations

The Village Board should:

1. Appoint distinct Board members for each of the three OCED entities to ensure that all entities are governed individually.

The FURA Board should:

2. Direct and manage the FURA's operations as a separate and independent entity with its own governance structure and separate and distinct bank accounts and accounting records.
  3. Adopt its own policies including a code of ethics and policies for bill payment.
  4. Contact the Attorney General's office to obtain an opinion regarding the compatibility of offices for the various Board members (in relation to their service as Board members for the other entities).
  5. Seek remuneration from the FLDC for the unauthorized gift of FURA property.
  6. Finalize a written agreement with the Village specifying appropriate consideration the FURA will pay for the services the Village provides.
  7. Require the Company to maintain separate and distinct records and reports for the FURA, following appropriate accounting rules.
  8. Repay the FIDA for expenses not properly reimbursed (approximately \$250,000 over the last five years).
  9. Require the Company to provide accurate general ledger reports in a timely fashion. Also, require the Company to provide a year-end general ledger that matches the FURA's audited financial statements.
  10. Adopt an investment policy for the FURA that complies with legal requirements.
  11. Only invest the FURA's funds as statutorily authorized.
- FURA officials should:
12. Complete a new time study that includes the FLDC and use the actual results as the basis for charging employees' time to the three entities.

13. Accurately report all FURA revenues, expenses, assets and liabilities in its own accounting records and reports.
14. Maintain the FURA's accounting records and bank accounts separate and distinct from the FIDA and the FLDC and discontinue the practice of recording the cash balance as a liability from the FIDA due to the FURA.
15. Record all FURA transactions in the FURA's general ledger, with accurate allocation of shared expenses as they occur.

The FURA Board and officials should:

16. Cease portraying the FURA under the umbrella agency of the OCED, implying that the FURA is not an independent corporate entity.
17. Make decisions for the FURA independently from other entities and within the public's best interest and within the FURA's mission.

**APPENDIX A**  
**RESPONSE FROM AGENCY OFFICIALS**

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



Office of Community +  
Economic Development

January 22, 2016

Mr. Edward V. Grant, Jr., Chief Examiner  
Local Government and School Accountability  
Office of the State Comptroller  
The Powers Building  
16 West Main Street, Suite 522  
Rochester, New York 14614

RE: Audit Response  
Village of Fairport Urban Renewal Agency  
Audit Report Title: Board Governance, Report of Examination  
Audit Report Period: October 1, 2012 – March 12, 2015  
Audit Report Number: 2015M-196

Dear Mr. Grant:

Please accept this letter as the Village of Fairport Urban Renewal Agency’s (“FURA”) response to the Draft Audit Report referenced above (“Report”). We appreciate the external audit of our board’s governance structure and acknowledge the usefulness of certain findings and recommendations contained therein for further improvement of our operations. However, as explained below we take exception to the broad characterization that FURA’s governance structure was highly inappropriate and not consistent with applicable legislation for Urban Renewal Agencies.

See  
Note 1  
Page 23

The Village of Fairport is strongly committed to creating a vibrant and healthy local economy. Toward that end, the Village (i) pursuant to the General Municipal Law organized the Fairport Industrial Development Agency (“FIDA”) and the FURA and (ii) pursuant to the Not-For-Profit Corporations Law incorporated the Fairport Local Development Corporation (“FLDC”)<sup>1</sup>. All three entities are the creation of the Village and, in accordance with New York State law, all three boards are appointed by the Village. The missions and purposes of all three entities are substantially similar in that they promote and encourage private enterprises to invest in the Village in order to advance the opportunities and general prosperity of its inhabitants. In order to coordinate services and provide for “one-stop” shopping in a cost effective manner, the Village utilized a model deployed by the State of New York in the delivery of its economic development services.

See  
Note 2  
Page 23

<sup>1</sup> GML§910-B, GML§625, NFP§1411

Industrial Development Agency  
Urban Renewal Agency  
Section 8 Housing Program  
Local Development Corporation

31 South Main Street  
Fairport, New York 14450  
T 585.223.0313  
F 585.223.5466  
www.fairportoced.org

Similar to the marketing nomenclature of Empire State Development, which is simply a name assigned to the joint management and marketing of the NYS Department of Economic Development and the Urban Development Corporation, the Village appointed the same individuals to the boards of each entity and the same individual is the executive director of each. In order to market the “one-stop” shopping for the coordinated services of all three entities, the Village created the term the Village of Fairport Office of Community and Economic Development (“OCED”).  
Sincerely,

See  
Notes 2 & 3  
Page 23

The Report states the governance structure gives the appearance that the three entities are legally affiliated with each other, which runs counter to the statutory scheme for the establishment and operation of the FIDA, FURA and FLDC as separate corporate entities. However, the FIDA, FURA and FLDC are, in fact, affiliated with each other since all three entities are the creation of the Village and all three boards are appointed by the Village. Nevertheless, all three entities properly follow the corporate formalities of separately meeting, adopting resolutions, adopting policies, appointing committees, keeping minutes and records, and complying with the reporting requirements of Public Authorities Accountability Act of 2005, as amended (“PAAA”).

See  
Note 2  
Page 23

See  
Note 4  
Page 23

The Report incorrectly states that OCED and not FURA created a single audit committee and governance committee for all three entities. To the contrary, all three entities appointed their own audit and governance committees that are comprised of the same individuals. In addition, the Report incorrectly states that policies are identified as policies of the OCED and not of the three separate entities. Although the marketing name of OCED appears on all the policies, certain documents that are unique to an entity (e.g. By-Laws) are clearly identified as such. In addition, the policies that are shared among all three entities clearly identify the three separate entities, which such policies apply to. The Report goes on to state that this governance structure is highly inappropriate and not consistent with the statutory scheme governing URAs. The Report concludes that this structure violates the PAAA. We strongly disagree that by utilizing an efficient structure involving (i) shared management, (ii) the same individuals serving on three different boards and (iii) a single marketing name is “highly inappropriate” or “not consistent with the statutory scheme governing URAs” or “violates the PAAA”. We are not aware of any statutory provision that would prevent such a structure or that would deem holding such board and management positions to be incompatible, and none were cited in the Report other than broad brushed generalities. Nevertheless, FURA will consider initiatives to more clearly distinguish the entities under the OCED umbrella.

See  
Note 5  
Page 23

See  
Note 4  
Page 23

The FURA disagrees with the Report’s finding that FURA did not accurately account for its assets and that such information was not timely. The FIDA, FURA and FLDC accounting records are prepared independently, as evidenced by the quarterly separate financial statements and are timely reviewed by the boards of each entity as well as the fiscal year end reports. The FURA believes its accounting records are accurate as reflected in its independently audited financial statements, for which the FURA received an unqualified opinion. Although the FIDA and FURA did not maintain separate bank accounts, there was separate accounting for each entity, reflective of a common practice used by local governments. The Report is highly critical of a bookkeeping process, which utilized an allocation method for expenses and revenues since the entities shared a bank account and all expenses were initially paid by the FIDA. This process was utilized as a simple method to keep track of the expenses. The proper adjustments were made and the expenses were accurately reported quarterly by the independent auditors in the financial reports. The audited financials were used for PAAA reporting and therefore matched what was submitted to the Authorities Budget Office’s electronic information reporting system known as PARIS. Therefore, the financial position of FURA was not misstated on the audited financials and matched the PARIS system. Nevertheless, FURA accepted the Report’s recommendation and has established its own bank account and changed its bookkeeping method.

See  
Note 6  
Page 23

See  
Note 7  
Page 24

See  
Note 8  
Page 24

See  
Note 9  
Page 24

The FURA objects to the Report’s characterization of FIDA’s \$350,000 obligation to FURA as “unsubstantiated”. FIDA’s obligation to FURA is the result of it collecting on FURA’s outstanding loans. Until such time as FIDA turns the collected funds over to FURA, the obligation remains and changes every year based upon the amount collected. FIDA and FURA decided to memorialize this obligation by a written promissory note. Nevertheless, the need for this obligation has been eliminated through the establishment of the separate bank accounts and the changed bookkeeping process.

See  
Note 10  
Page 24

The FURA acknowledges that its investment policy and certain investments were not in accordance with the requirements of the GML. The FURA has already divested itself of a portion of these investments and will continue to work with its investment advisor to divest itself of the remainder. In addition, the FURA will update its investment policy accordingly. However, it should be noted that it is unlikely that the principal amount of these investments would be lost if such investments were held to maturity, since the majority of the local government and authority bonds acquired by the FURA were rated in the highest bond rating category and/or were insured, thereby minimizing the risk to the FURA.

The Report cites to a transfer of real property from FURA to the FLDC as an inappropriate gift outside of its statutory authority. Given the absence of express language in the GML prohibiting such a transaction and coupled with the express authority to transfer real property to the Village, with or without consideration, FURA undertook the transfer to the FLDC, the sole member being the Village, under the belief that such transfer was authorized. Nevertheless, FURA acknowledges the issue raised in the Report and will take it into consideration. The Report also characterizes payments made to the Village that was intended to cover services received such as plowing, utilities etc. as an unauthorized gift due to a lack of a written contract. However, FURA has the express authority to contract, whether written or not, and to use the agents, employees, and facilities of the Village, and to agree to pay for a portion of such costs. Nevertheless, FURA no longer makes these types of reimbursements to the Village and in the event it does in the future, it will be pursuant to a written contract. Lastly, the Report mischaracterizes the internal bookkeeping process for handling loan revenues as an inappropriate IDA subsidy. First, this issue was the result of the shared bank account with the FIRA and also having all revenues and expenses initially go through the FIDA. This has been resolved through the establishment of separate bank accounts and a change in the bookkeeping process. Secondly, even if such bookkeeping entry was considered to be a subsidy, the FURA has the express authority to accept subsidies. Therefore, it would not be inappropriate for FURA to accept such.

See  
Note 11  
Page 24

See  
Note 12  
Page 24

The FURA is proud of its success in advancing its mission and believes the current structure is an effective and efficient model for the delivery of economic development services within the Village. The FURA’s success is the direct result of its dedicated staff and board members. The Village is pleased that with a population of approximately 5,300 people it is able to find highly qualified civic-minded individuals willing to volunteer to serve on the boards of these three entities. These board members fully understand that the FIDA, FURA and the FLDC are separate legal entities as evidenced by their separate meetings. The boards do not see a need to create different PAAA mandated policies for each entity, especially since each entity separately adopted the policies and are each named therein. Nevertheless, FURA will take into consideration the Report’s recommendation to more clearly distinguish the operations of the entities under the OCED umbrella. The FURA also believes that its financial accounting was properly separated and accurate based upon independent financial audits. However, FURA respects the Report’s recommendations for separate bank accounts, which it has already implemented, as well as a new bookkeeping process. The FURA has an updated employee time study and will base its reimbursement rates from FIDA on such. In the event the FLDC will remain staffed by the FURA, the time study will be updated accordingly. The FURA acknowledges its restrictions on investments and will update its investment policy and investments accordingly.

The FIDA does, however, for the reasons stated above, object to the references to the FURA's organizational structure as "inappropriate", "violation of PAAA" and "not consistent with the statutory scheme governing URAs". The substantive issues identified in the Report are not the result of the governance structure, but stem from utilizing a shared bank account and the resulting bookkeeping for which FURA has acknowledged and has already implemented corrective action.

We are thankful for the identification of certain legitimate issues raised in the Report for which FURA will address, if it has not already done so. However, we do request that the rhetoric used to describe FURA's governance structure be revised to reflect a more objective tone rather than inflammatory subjective comments. We hope you will take our comments into consideration by correcting the inaccuracies and adjusting the tone.

Sincerely,

H. Kevin Clark, Chairman  
Fairport Urban Renewal Agency

## APPENDIX B

### OSC COMMENTS ON THE AGENCY'S RESPONSE

#### Note 1

On December 29, 2015 we held an exit conference with FURA officials. A primary purpose of the exit conference is to allow officials an opportunity to refute findings or provide additional information. FURA officials chose not to share any concerns.

#### Note 2

The FIDA, the FURA and the FLDC are separate corporate entities with separate and distinct purposes, powers, duties and fiduciary responsibilities. They are not legally affiliated with each other. By statutory design, these entities are independent from each other and from the Village. While it may be effective to coordinate the activities of the three, they remain independent and distinct entities.

#### Note 3

In 1995, the New York State Department of Economic Development and the Urban Development Corporation were consolidated into one State agency – Empire State Development.

#### Note 4

While the three entities have separate meeting minutes and adopt resolutions and policies, they generally adopted one OCED policy which indicated “the FIDA, FURA and LDC will be collectively referred to as the Village of Fairport Office of Community [and] Economic Development (OCED).” Thus, officials apply these policies to all three entities, instead of developing separate policies that address each entity’s individual needs.

#### Note 5

While the audit and governance committees were appointed in the separate minutes of each entity, the committees are clearly indicated as the OCED’s Board committees on the OCED’s website. Further, the Audit Committee Charter “was adopted by the Board of Directors of OCED on March 20, 2007.”

#### Note 6

The accounting records are not prepared independently. FURA staff records all transactions into one transaction log. Because these are separate entities, all transactions always should be initially recorded in separate accounting records for the applicable entities. There should be no need to improperly allocate expenses or improperly record amounts owed to another entity. Furthermore, even the separate quarterly reports prepared by the Company (to separate the combined records into individual records) inappropriately did not report cash balances for each entity.

#### Note 7

A Board member told us that she had never seen the quarterly reports (as discussed in footnote 32 in the report).

#### Note 8

There is no separate accountability, the allocation methods used to separate transactions by entity were not equitable and adjustments made were significantly flawed. This resulted in significantly misstated financial reports. As described in detail in the report, there was nothing “simple” or “common” about the accounting practices used.

#### Note 9

The allocation method used resulted in the FURA never being charged for its own expenses and the FIDA being charged for both the FURA’s and FIDA’s expenses. In addition, the new allocation method used beginning in June 2014 further understates the FURA’s operating costs and overstates the FIDA’s costs. These misstated expenses were included in the audited financial statements and the PARIS report to the ABO.

#### Note 10

The FIDA should not be collecting the FURA’s revenues and should never have recorded the FURA’s cash balance or its revenues from outstanding loans in the FIDA accounting records.

#### Note 11

The inappropriate subsidy finding in the report addresses the improper process used to reallocate expenses to the FURA that were initially paid by the FIDA. The improper adjustment results in recording a nonexistent revenue (“Interprogram Income”) for the FURA which offsets the expenses allocated to the FURA, resulting in those expenses not being reflected in the FURA’s final cost figures.

#### Note 12

The OCED did not have the authority to use FIDA money to subsidize the FURA.

## APPENDIX C

### AUDIT METHODOLOGY AND STANDARDS

The objective of our audit was to evaluate the propriety of the FURA's financial and operational activities for the period October 1, 2012 through March 12, 2015. To achieve our audit objective and obtain valid audit evidence, we performed the following audit procedures.

- We interviewed FURA officials and Board members and reviewed the FURA's policies, bylaws and Board meeting minutes to gain a general understanding of how the FURA operates.
- We reviewed general ledger activity, PARIS reports and audited financial statements. We evaluated the propriety of the FURA's accounting records in conjunction with the FIDA's and the FLDC's records and the combined investment activities based on pertinent statutes.
- We assessed whether the FURA has the authority to operate under the current governance structure or to perform the various gifting, lending and payment activities. We based this on our review of the pertinent statutes, Opinions of the State Comptroller and a recent Opinion of the Attorney General. We also reviewed guidance published by the ABO.
- We identified and reviewed various transactions between the FURA and the Village.
- We reviewed the 2010 and 2015 time studies.
- We interviewed Village officials regarding transactions between FURA and the Village.
- We reviewed the various expense allocation methods utilized during our audit period.
- We reviewed the documented promissory notes and discussed them with the FURA officials.
- We scheduled payroll costs for the three FURA employees shared by the FIDA for three months (October through December 2013) and tested payroll cost allocations in comparison to the contract for leased employee services.

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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